

Feasibility of Restructuring Budget and Financial Management of North Carolina State Government



**Final Report to the Joint Legislative
Program Evaluation Oversight Committee**

Report Number 2010-02

April 29, 2010



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John W. Turcotte
Director

April 29, 2010

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Representative Nelson Cole, Co-Chair, Joint Legislative Program Evaluation Oversight Committee

Senator Daniel G. Clodfelter, Co-Chair, Joint Legislative Program Evaluation Oversight Committee

Senator Fletcher L. Hartsell, Jr., Co-Chair, Joint Legislative Program Evaluation Oversight Committee

North Carolina General Assembly

Legislative Building

16 West Jones Street

Raleigh, NC 27601

Honorable Co-Chairs:

Session Law 2009-451, Section 22.1 directed the Program Evaluation Division to study the feasibility of consolidating the Office of State Budget and Management, the Office of the State Controller, and some functions of the State Treasurer or reallocating functions of those state agencies, with the goal of achieving economies or improving management. This report reviews the structure for budgeting and financial management in North Carolina and identifies the functions provided by the three entities.

I am pleased to report that the Office of State Budget and Management, the Office of the State Controller, and the Department of the State Treasurer cooperated with us fully and were at all times courteous to our evaluators during the evaluation.

Per Session Law 2009-451, Section 22.1, this report also was submitted to the full chairs of the Senate and House Appropriations Committees and the Fiscal Research Division.

Sincerely,

A handwritten signature in black ink, appearing to read "John W. Turcotte".

John W. Turcotte
Director



PROGRAM EVALUATION DIVISION

NORTH CAROLINA GENERAL ASSEMBLY

April 2010

Report No. 2010-02

Feasibility of Restructuring Budget and Financial Management of North Carolina State Government

Summary

Evaluation purpose. The North Carolina General Assembly directed the Program Evaluation Division to study the feasibility of consolidating the Office of State Budget and Management, the Office of the State Controller, and some functions of the State Treasurer or reallocating functions of those state agencies, with the goal of achieving economies or improving management. These agencies are responsible for much of the budgeting and financial management of state government in North Carolina. This report reviews the structure for budgeting and financial management in North Carolina and identifies functions provided by each entity.

There is no duplication of budget and financial management functions. Together, State Budget, the Controller, and the Treasurer, spent \$56.3 million in Fiscal Year 2008-09 to perform budget and financial management functions with 475.3 employees. The Program Evaluation Division identified 29 budget and financial management functions performed by these three entities and determined that there is no duplication of effort among them.

The structure and location of budget and financial management functions varies among states. Data from other states shows that location and organization of budget and financial management functions vary based on specific legal requirements and local custom. However, the Program Evaluation Division observed that North Carolina is one of 22 states with the structure of locating State Budget, the Controller, and the Treasurer in three separate agencies.

Consolidation of budget and financial management functions of state government is feasible but constrained by constitutional requirements. The Program Evaluation Division identified the following options requiring statutory changes:

- establishing a separate budget and financial management agency in the Department of Administration by combining State Budget and the Controller into one agency would save an estimated \$788,000 in Fiscal Year 2010-11; or
- merging the Controller into a division under the Treasurer would save an estimated \$387,000 in Fiscal Year 2010-11.

Consolidation of budget and financial management functions is not advised. Although consolidation would save money, the Program Evaluation Division determined that consolidation would sacrifice the independence of the Controller.

Scope

The North Carolina General Assembly directed the Program Evaluation Division to study the feasibility of consolidating the Office of State Budget and Management, the Office of the State Controller, and some functions of the Department of the State Treasurer or reallocating functions of those state agencies, all with the goal of achieving economies or improving management.¹ Hereafter, these agencies are respectively referred to as State Budget, the Controller, and the Treasurer. This report reviews the structure for budgeting and financial management in North Carolina and identifies the functions provided by the three entities.

This evaluation addressed the following questions:

- What is the constitutional and statutory framework for budget and financial management functions performed by State Budget, the Controller, and the Treasurer?
- How are state budget and financial management functions performed in North Carolina?
- What budget and financial management functions are performed by budget offices, controllers, and treasurers in other states?
- Is it feasible and appropriate to consolidate some budget and financial management functions performed by State Budget, the Controller, and the Treasurer?

Because the Department of Revenue and the State Auditor are responsible for important budget and financial management functions of state government (i.e., tax revenue collection and auditing, respectively), how they perform their budget and financial management functions in coordination with State Budget, the Controller, and the Treasurer are covered as a part of this report. However, consolidation or reallocation of budget and financial management functions performed by the Department of Revenue and the State Auditor are not addressed in this review.

The Program Evaluation Division collected and analyzed data from several sources, including

- the North Carolina Constitution and laws for the Governor, State Budget, the Controller, and the Treasurer;
- fiscal and operational data from each agency;
- query responses describing how each agency performs budget and financial management functions of state government;
- interviews with agency leadership for State Budget, the Controller, the Treasurer, the State Auditor, and the Fiscal Research Division;
- literature on state government organization and collaboration;
- data from national organizations on the location and selection of budget offices, controllers, and treasurers in other states;² and
- query responses from budget offices, controllers, and treasurers in five southeastern states that identified which budget and financial management functions were performed by their offices.

¹ 2009 NC Sess. Laws, 2009-451, Section 22.1.

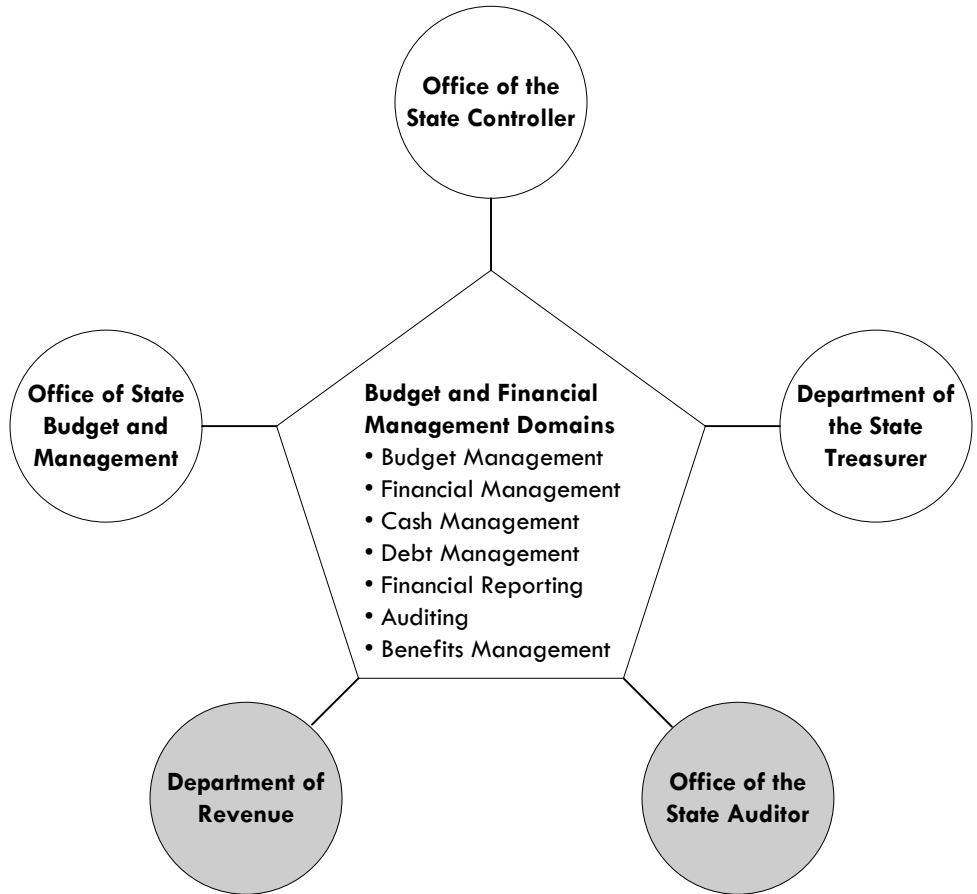
² The following organizations were contacted: National Association of State Budget Offices; Government Accounting Standards Board; National Association of State Auditors, Comptrollers and Treasurers; Government Finance Officers Association; National Association of State Treasurers; and Advancing Government Accountability.

Background

In North Carolina, five agencies perform budget and financial management functions of state government: State Budget, the Controller, the Treasurer, the Department of Revenue, and the State Auditor. Exhibit 1 shows the budget and financial management functions performed by each of these agencies.

Exhibit 1

Five State Agencies Perform Budget and Financial Management in North Carolina



Note: State agencies outside the scope of this evaluation are shaded.

Source: Program Evaluation Division.

Several other state agencies are involved in the performance of budget and financial management functions, but their involvement is limited to coordination with one of the primary agencies. For example, the Office of State Personnel sets personnel policy and the Department of Administration sets purchasing and contracting policy, but the Controller is responsible for the state’s payroll system and records expenditures when government purchases occur. The Office of Information Technology Services reviews budget requests for new computer software and hardware, but State Budget is responsible for budget development and execution for information technology.

North Carolina’s performance of budget and financial management compares favorably when several factors are considered:

- North Carolina is one of seven states with the highest bond rating from all three rating services.

- Since 1994, the Controller has received the “Certificate of Achievement for Excellence in Financial Reporting” from the Government Finance Officers Association. This award is presented to governmental units whose Comprehensive Annual Financial Report (CAFR) achieves the highest standards in governmental accounting and financial reporting.
- During the past three years, North Carolina has been among the first five states to issue their CAFR report. The CAFR was issued 161 days after the end of the state fiscal year in 2008.
- United States Census data from 2007 show that North Carolina had 4.51 financial administration positions per 10,000 population in comparison to the 50-state average of 5.74. Other states with the highest bond ratings had less favorable ratios.³
- During an interview with staff of the Governmental Accounting Standards Board, North Carolina was one of the states mentioned that had a good structure and utilized best practices in their operation along with Maryland, Tennessee, Utah, and Virginia.

Questions and Answers

1. What is the constitutional and statutory framework for budget and financial management functions performed by State Budget, the Controller, and the Treasurer?

The North Carolina Constitution and General Statutes establish the legal framework for budget and financial management in North Carolina.

Office of State Budget and Management. The basis for State Budget’s authority is constitutional and statutory. Under the North Carolina Constitution, the Governor is responsible for the development and management of the state’s budget.⁴ The Governor is required to prepare and recommend to the North Carolina General Assembly a comprehensive budget, and the Governor is directed to administer the budget as enacted by the General Assembly. The State Budget Act specifies that the Governor is the Director of the Budget, but authorizes the Governor to delegate authority to State Budget, which the Governor has chosen to do.⁵

Office of the State Controller. The basis for the Controller’s authority is statutory. The General Assembly established the Controller in 1986⁶ following the recommendations of a legislative study commission to solve the following problems with the state accounting system:

- fragmented and dispersed authority for the operation and management of the state accounting system;
- lack of a single control authority staff to operate and manage the state accounting system; and

³ The other states with the highest bond ratings and their number of financial administration positions per 10,000 population are Delaware (9.50), Georgia (4.70), Maryland (6.32), Missouri (5.58), Utah (9.59), and Virginia (5.58).

⁴ North Carolina Constitution, Article III, Section 5(3).

⁵ NC Gen. Stat. § 143C-2-1(a).

⁶ 1986 NC Sess. Laws, 1986-2136.

- decentralized accounting system processing that affected the accuracy of state financial information.

The Controller was created from the transfer of state accounting, disbursing, and financial reporting functions from the State Auditor and State Budget. The Controller is responsible for prescribing, developing, operating, and maintaining a uniform state accounting system for all state agencies, in accordance with generally accepted principles of governmental accounting.⁷ The Controller's responsibilities include operating the state payroll system, developing and maintaining a state cash management system, and compiling the Comprehensive Annual Financial Report.

Department of the State Treasurer. The basis for the Treasurer's authority is constitutional and statutory. Under the North Carolina Constitution, the Treasurer is an elective officer of the state, and the Constitution states that the duties of the Treasurer shall be prescribed by law.⁸ Statutes define the Treasurer's responsibilities as receiving and disbursing funds from the state treasury, establishing and maintaining state banking operations, issuing state debt, investing state funds, operating the retirement system, and managing the unclaimed property program.⁹

Other Agencies. The State Auditor is an elective officer of the state¹⁰ and is responsible for performing or coordinating all audit functions for state government.¹¹ The Department of Revenue is responsible for collecting and accounting for the state's tax funds, ensuring uniform administration of tax laws and regulations, conducting research on revenue matters, and exercising general and specific supervision over property valuation and taxation.¹²

2. How are budget and financial management functions performed in North Carolina?

Budget and financial management functions fall into the following seven domains:

- **Budget management** – functions related to the development and execution of the state budget;
- **Financial management** – functions related to developing, maintaining, and operating the state's accounting and payroll systems;
- **Cash management** – functions related to the management of state funds including investments, banking operations, and collections and disbursements;
- **Debt management** – functions related to managing debt or obligations resulting from borrowing money;

⁷ NC Gen. Stat. §143B-426.39(1).

⁸ North Carolina Constitution, Article III, Section 7(1), (2).

⁹ NC Gen. Stat. § 116B, 135, 142, 147-68(a), 147-68.1, 147-69, 147-69.1, 147-69.2.

¹⁰ North Carolina Constitution, Article III, Section 7(1), (2).

¹¹ NC Gen. Stat. § 147-64.3.

¹² NC Gen. Stat. § 143B-218.

- **Financial reporting** – functions related to providing budget, compliance, and financial information for state government;
- **Auditing** – functions performed to ascertain the validity and reliability of state government finances and operations; and
- **Benefits management** – functions related to the provision and operation of benefits for state government employees.

To identify and define budget and financial management functions typically performed by state government, the Program Evaluation Division reviewed *Governmental Accounting, Auditing, and Financial Reporting*,¹³ the North Carolina State Budget Manual, and information provided by State Budget, the Controller, and the Treasurer. Exhibit 2 provides definitions for each of the 29 budget and financial management functions that fall under the seven domains. These definitions are used throughout this report. State Budget, the Controller, and the Treasurer estimated that they expended \$56.3 million in Fiscal Year 2008-09 to perform these functions with 475.3 positions. A detailed summary of these expenditures is located in Appendix A.

Using these definitions, the Program Evaluation Division asked State Budget, the Controller, and the Treasurer to describe the functions they perform related to each budget and financial management function. Summaries of agency descriptions of their involvement with each budget and financial management function are located in Appendix B. The Program Evaluation Division used the following criteria to determine each agency's level of involvement in each budget and financial management function:

- **Primary responsibility.** The agency has primary responsibility for the function including statutory authority and is held accountable for their performance of the function.
- **Significant involvement.** The agency has significant involvement in the function including contributing one or more of the components, and the function is dependent upon the information or resources provided by the agency.
- **Limited involvement.** The agency has limited involvement in the function including performing a limited scope of tasks related to the function.
- **No involvement.** The agency has no involvement in the function.¹⁴

¹³ Government Finance Officers Association. (1988). *Governmental Accounting, Auditing, and Financial Reporting*. Chicago, Illinois: Government Finance Officers Association.

¹⁴ The level of involvement for the State Auditor and the Department of Revenue was determined through review of their statutes.

Exhibit 2: Glossary of Budget and Financial Management Functions

Budget Management	
Budget execution	Formally certify the legislatively enacted budget and administer the budget to ensure appropriations are expended for the purposes for which they were authorized. Functions include interpreting legislation and other governing language and developing and issuing budget polices and procedures; monitoring and considering budget adjustments within the framework of the State Budget Act and other relevant state and federal legislation, rules, and policies; maintaining a balanced budget through the allotment process; and providing assistance and guidance to state agencies in carrying out their delegated responsibilities related to budget execution.
Budget development	Prepare and present the Governor's recommended budget for consideration by the North Carolina General Assembly. Functions include defining the process for budget preparation; budget and revenue projections; developing the continuation and expansion budgets (includes information technology requests and capital improvements). Develop "results-based budgeting" performance information and provide technical assistance and analysis to state agencies in developing budget requests and to the Governor and other decision makers in prioritizing requests and final recommendations.
Federal and other grant funds oversight	Oversee funds received from federal government agencies or other granting entities (received through block grants, entitlement programs, and specific grants) for the support of state programs. Oversight includes authorizing the expenditure of federal and other grant funds through budget development or adjustments to the authorized budget.
Grant monitoring and oversight	Oversee the uniform administration of state grants by all grantor state agencies and grantees including establishing policies and procedures for disbursement of state grants and state agency oversight, monitoring, and evaluation of grantees.
Internal service fund oversight	Oversee a fund used to account for the financing of goods and services provided by one department or agency to other departments or agencies of a government, or to other governments, on a cost-reimbursement basis (e.g., motor fleet management, information technology services).
Salary and position control systems	Monitor state agency maintenance of position control over salaries and salary reserves. Maintain an accurate number of positions, record the establishment of new positions, reconcile certification, and assist agencies in reconciling position accounts and budgeted salaries. Ensure that each position established has sufficient funds budgeted to support it on an annual basis.
Financial Management	
Cost allocation plan	Develop and maintain a plan that describes how the direct and indirect costs for a government program are allocated to and recovered from funding sources such as state appropriations, federal funds, and other receipts.
Fixed asset management	Manage long-lived tangible assets obtained or controlled as a result of past transactions, events, or circumstances. Fixed assets include buildings, equipment, improvements other than buildings, and land.
Internal control structure	Establish and maintain policies and procedures that provide reasonable assurance that specific government objectives will be achieved.
Payroll/Human resources	Manage and operate the centralized payroll system for most state agencies including organizational management, personnel administration, and benefit plan enrollment.
Accounting system	Maintain the methods and records established to identify, assemble, analyze, classify, record, and report a government's transactions and maintain accountability for the related assets and liabilities. Operate the North Carolina Accounting System that facilitates internal control over fiscal operations and provides a structure (chart of accounts) for recording accounting data for the purpose of preparing standardized and meaningful financial statements and reports.
Cash Management	
Cash management	Manage the receipt, deposit, and disbursement of state funds through statewide policy and procedures.
Banking operations	Provide banking services for state government agencies including maintaining relationships with major banks in the state, providing depository services for state agencies, monitoring public deposits, and insuring state funds are swept into the state's main bank.

Cash Management (continued)	
Departmental receipt collection	Oversee the collection of fees, licenses, federal funds, grants, fines, penalties, tuition, and other similar collections or credits generated by state agencies in the course of performing their governmental functions that are applied to the cost of a program administered by the state agency or transferred to the Civil Penalty and Forfeiture Fund and that are not defined as tax proceeds or non-tax revenues.
Investment management	Invest the combined assets of the state's pension funds, escheats funds, and assets in the cash management program.
Non-tax revenue collection	Collect revenue that is not generated from tax proceeds and that is required by statute to be credited to the General Fund.
Tax revenue collection	Collect revenue that is generated from tax proceeds and that is required by statute to be credited to the appropriate funds.
Unclaimed property	Manage the program that safeguards and returns abandoned property (bank accounts, wages, utility deposits, insurance proceeds, stocks, bonds, and safety deposit boxes) to its rightful owners. Manage the investments of the Escheats Fund.
Debt Management	
Debt management	Manage debts or obligations resulting from the borrowing of money or from the purchase of goods and services including bonds, time warrants, and notes. Perform all functions associated with issuing bonds, certificates of participation, and other debt instruments. Manage and pay for state debt service.
Bond rating	Maintain the state's financial condition to ensure favorable evaluations from rating services.
Financial Reporting	
Budget reporting	Oversee the monthly and year-end budget reports prepared by state agencies. Review other budget reports including the biennial fee report and the annual report listing of committees and councils.
Financial reporting	Communicate information concerning the government's financial position and financial functions.
Comprehensive Annual Financial Report (CAFR)	Compile the official annual report of state government.
Compliance	Demonstrate state compliance with financial-related laws and regulations. Examples of common compliance items include bond indentures, grant provisions, debt limitations, and employment regulations.
Auditing	
Financial auditing	Perform audits to determine whether the financial statements of a government entity are presented fairly and in conformity with generally accepted accounting principles.
Internal auditing oversight	Oversee the independent appraisal of the diverse operations and controls within a government entity to determine whether acceptable policies and procedures are followed, established standards are met, resources are used efficiently and economically, and the organization's objectives are being achieved. This function covers all forms of appraisal of functions undertaken by auditors working for and within an organization.
Performance auditing	Perform an audit function that provides an independent, third-party review of management's performance and the degree to which the performance of the audited entity meets pre-stated expectations. Objectively obtain and evaluate evidence regarding the performance of state-funded organizations, programs, or functions.
Benefits Management	
Health care benefits	Perform functions related to the premium payment, accounting, and financial reporting of health care benefits for state employees.
Retirement system	Operate retirement services for state employees including enrollment, payment processing, counseling services, and reporting.

Source: Program Evaluation Division based on Governmental Accounting, Auditing, and Financial Reporting, the North Carolina State Budget Manual, and information provided by the agencies being evaluated.

One agency has primary responsibility and the technical expertise for most budget and financial management functions in four of the seven domains.

- **Budget management.** State Budget has primary responsibility for all budget management functions. The other agencies are not involved in budget management with the exception of federal and other grants oversight where the Controller has limited involvement.
- **Financial management.** The Controller has primary responsibility for most financial management functions including cost allocation planning, internal control structure, payroll/human resources, and the accounting system. State Budget has significant responsibility for fixed asset management.
- **Cash management.** The Treasurer has primary responsibility for most cash management functions including investment management, banking operations, and unclaimed property. The Treasurer shares primary responsibility with the Controller for managing the receipt, deposit, and disbursement of state funds. The Department of Revenue is solely responsible for tax collection.
- **Auditing.** The State Auditor has primary responsibility for auditing though State Budget and the Controller have significant involvement with internal auditing oversight.

Responsibility for budget and financial management functions under the three remaining domains is shared between at least two agencies.

- **Debt management.** The Treasurer has primary responsibility for issuing and managing the state's debt. State Budget has significant involvement with recommending debt options, overseeing debt authorized projects, and projecting debt expenditures; the Controller has significant involvement with debt service and monitoring statewide special indebtedness. All three agencies have significant involvement in maintaining the state's bond rating.
- **Financial reporting.** State Budget, the Controller, the Treasurer, and the State Auditor all have significant involvement in at least one of the financial reporting functions. State Budget has primary responsibility for budget reporting, but the Controller has significant involvement because it prepares expenditure reports that interface with the budget preparation system. The Controller has primary responsibility for the Comprehensive Annual Financial Report (CAFR) with significant involvement from the Treasurer, who provides information on debt, investments, and pension plans, and limited involvement from State Budget, who assists with data collection. The State Auditor conducts the external audit of the report.
- **Benefits management.** The Treasurer has primary responsibility for the retirement system, and the Controller has significant involvement with retirement and health care benefits through the operation of the payroll/human resources system.

Exhibit 3 summarizes each agency's involvement with budget and financial management functions.

Exhibit 3: Agency Involvement in Budget and Financial Management Functions

Function	State Budget	State Controller	State Treasurer	State Auditor	Dept. of Revenue
Budget Management					
Budget execution	●				
Budget development	●				
Federal and other grant funds oversight	●	○			
Grant monitoring and oversight	●				
Internal service fund oversight	●				
Salary and position control systems	●				
Financial Management					
Cost allocation plan	○	●			
Fixed asset management	◐	○			
Internal control structure		●	○		
Payroll/human resources	○	●			
Accounting system		●			
Cash Management					
Cash management		●	●		
Banking operations		○	●		
Departmental receipt collection	◐	○	◐		
Investment management			●		
Non-tax revenue collection		◐	◐		
Tax revenue collection					●
Unclaimed property			●		
Debt Management					
Debt management	◐	◐	●		
Bond rating	◐	◐	◐		
Financial Reporting					
Budget reporting	●	◐			
Financial reporting	◐	◐	◐		
Comprehensive Annual Financial Report	○	●	◐	◐	
Compliance	○	◐	◐		
Auditing					
Financial auditing	○	○		●	
Internal auditing oversight	◐	◐		○	
Performance auditing	○			●	
Benefits Management					
Health care benefits	○	◐			
Retirement system	○	◐	●		
● – Agency has primary responsibility for function		○ – Agency has limited involvement in function			
◐ – Agency is significantly involved in function		Blank – Agency has no involvement in function			

Source: Program Evaluation Division based on data provided by the agencies being evaluated.

The Program Evaluation Division's analysis of how the three agencies perform budget and financial functions did not find any duplication. As shown in Appendix B, shared responsibility among the agencies is an indication of collaboration, not duplication of effort. When more than one agency is involved in a function, each agency has responsibility for specific tasks that do not overlap with the tasks performed by other agencies. Completing the function requires collaboration between agencies.

The collaboration between State Budget, the Controller, and the Treasurer is not a unique strategy for dealing with complex government operations. Collaboration can be described as an organizational strategy to deal with complex problems that elude unilateral action by a single entity.¹⁵ This process allows parties who see different aspects of a problem to constructively search for solutions that move beyond a single vision.¹⁶

Agencies collaborate with one another because of interdependencies. Interdependencies occur when one agency provides resources to and depends on resources from another organization,¹⁷ or when one agency does not control all the conditions necessary for executing an action or function.¹⁸ Under these circumstances, agencies must collaborate with each other to complete all aspects of a function.

There are many types of organizational interdependencies across state government. During this review of budget and financial management functions, the Program Evaluation Division found organizational interdependencies were largely the result of dependence on resources. State Budget, the Controller, and the Treasurer collaborated on some budget and financial management functions because they depended on each other for information sharing and technical expertise.

The following budget and financial management functions highlight how State Budget, the Controller, and the Treasurer collaborate with each other to perform specific functions.

- **Cash management.** The Controller and Treasurer share responsibility for some tasks within this function. Exhibit 4 shows how the Treasurer is responsible for recording deposits of state funds and the Controller is responsible for receipt and disbursement of state funds.
- **Debt management.** Exhibit 5 shows that the Treasurer has primary responsibility for debt management and how State Budget and the Controller contribute to the function.
- **Comprehensive Annual Financial Report.** Exhibit 6 shows that the Controller has primary responsibility for the CAFR and how State Budget, the Treasurer, and the State Auditor contribute to the completion of the report.

¹⁵ Gray, B., & Wood, D. (1991). Collaborative alliances: Moving from practice to theory. *Journal of Applied Behavioral Science*, 27, 3-22.

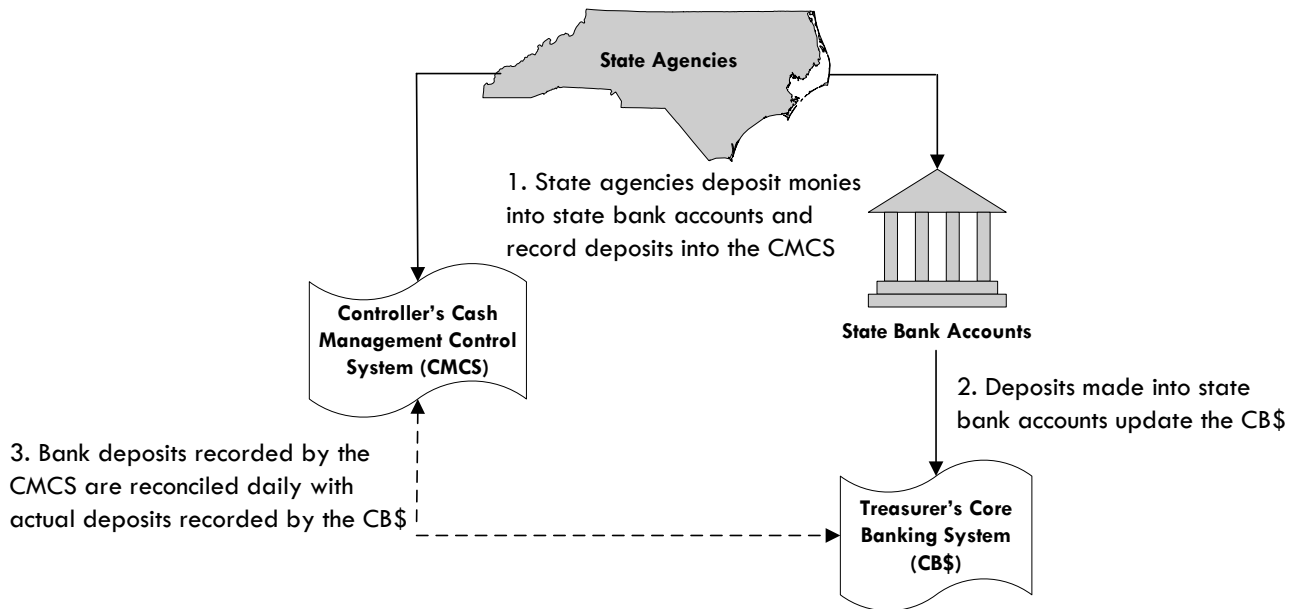
¹⁶ Gray, B. (1985). Conditions facilitating inter-organizational collaboration. *Human Relations*, 38, 911-936.

¹⁷ Saidel, J. (1989). Dimensions of interdependence: The state and voluntary-sector relationship. *Nonprofit and Voluntary Sector Quarterly*, 18, 335-347.

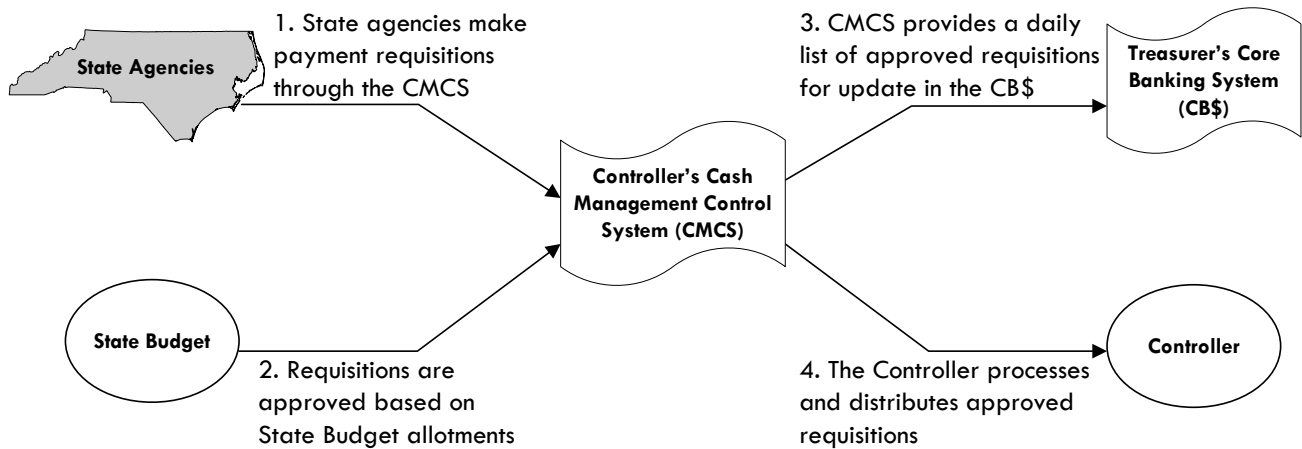
¹⁸ Pfeiffer, J., & Salancik, G. R. (1978). *The external control of organizations: A resource dependency perspective*. New York: Harper & Row.

Exhibit 4: Controller and Treasurer Share Responsibility for Cash Management

Deposits



Requisitions

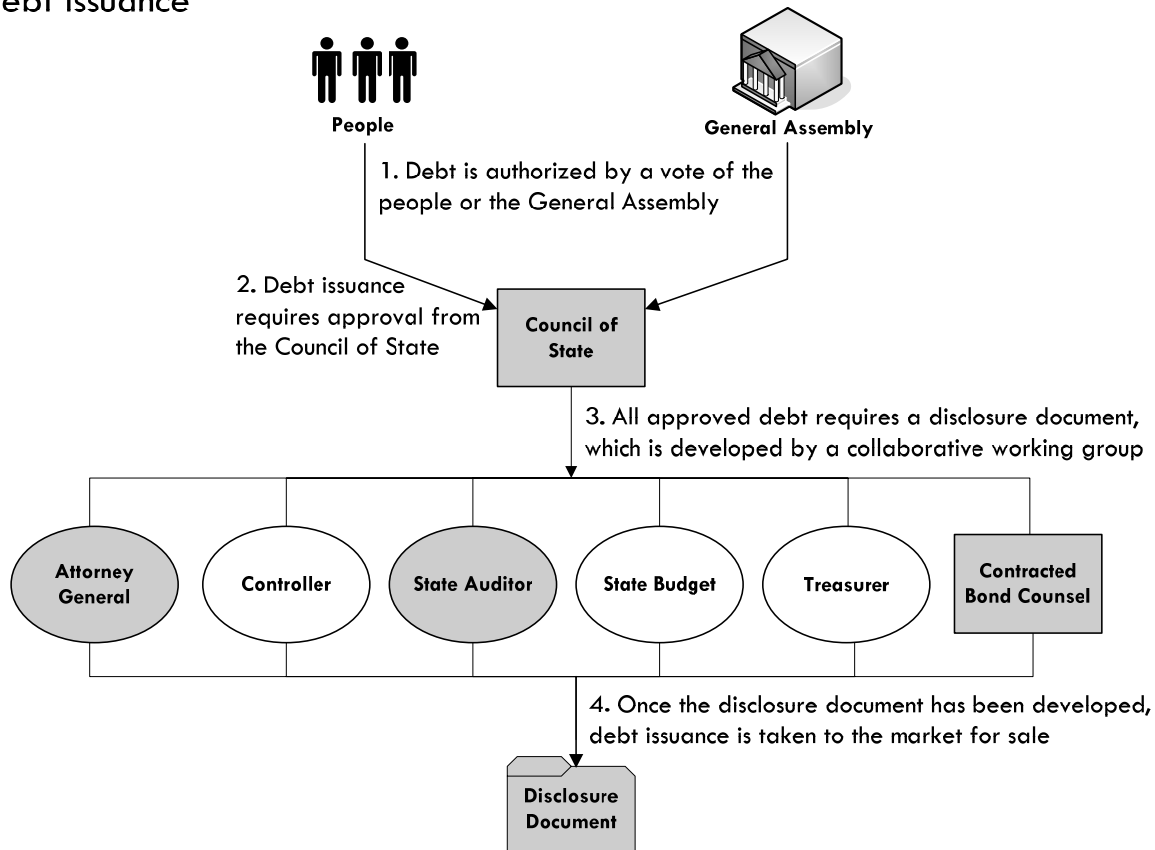


Note: State agencies and other entities outside the scope of this evaluation are shaded. The official acronym for the Treasurer's Core Banking System is CB\$.

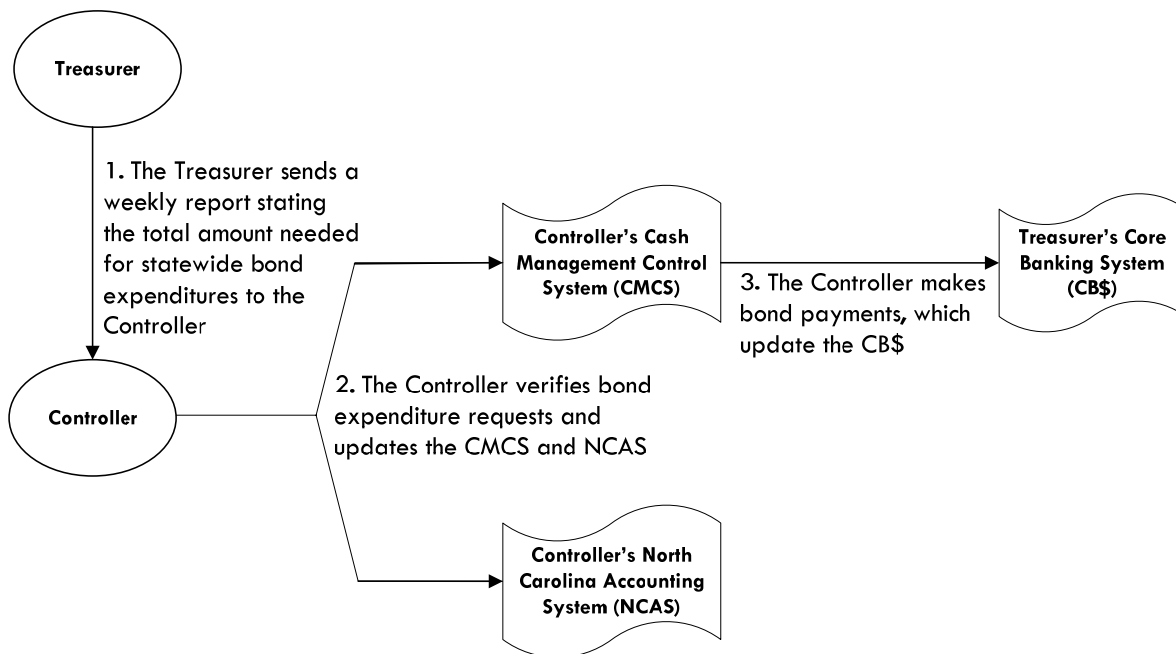
Source: Program Evaluation Division based on interviews with and documents provided by the agencies being evaluated.

Exhibit 5: Treasurer Has Primary Responsibility for Debt Management

Debt Issuance



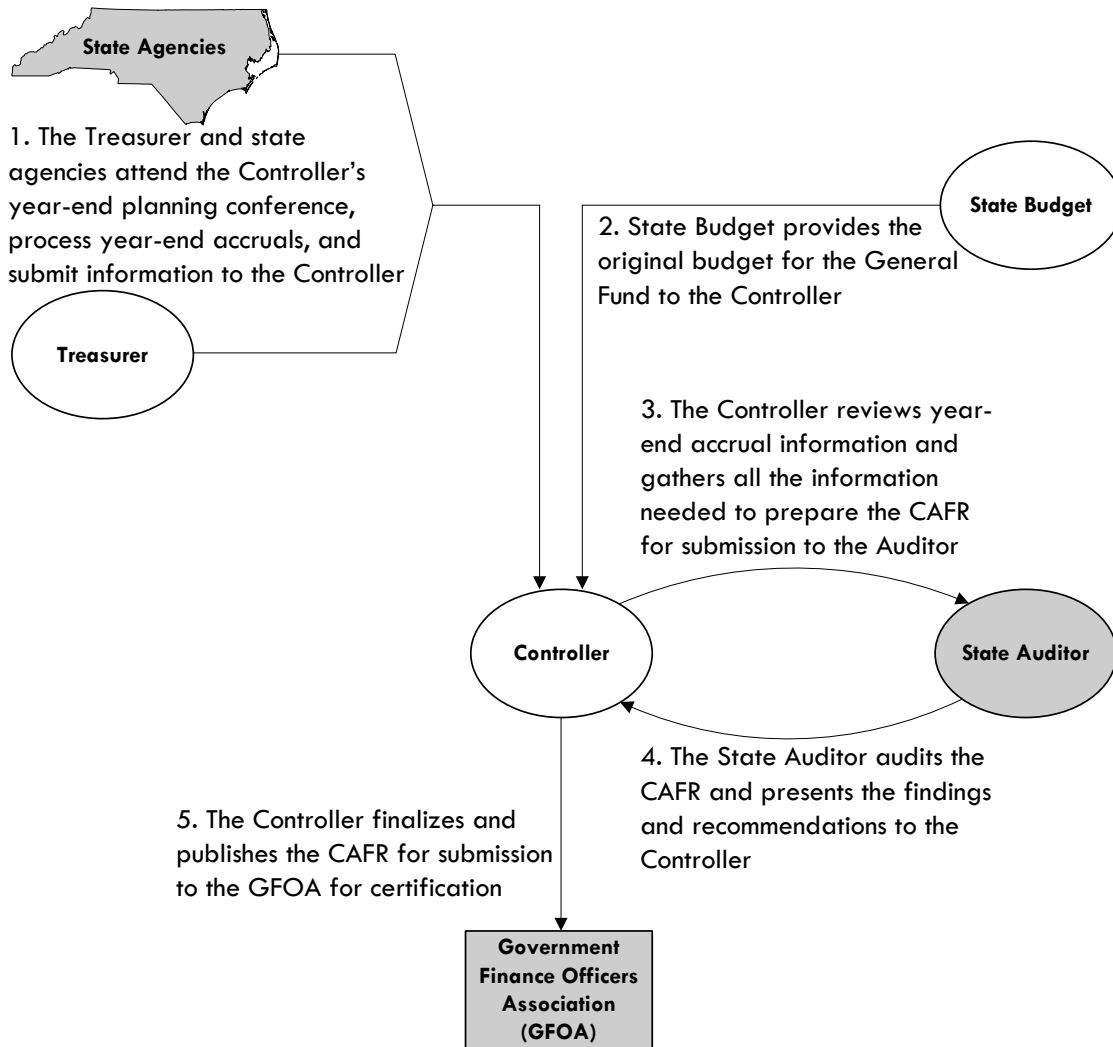
Debt Service



Note: State agencies and other entities outside the scope of this evaluation are shaded. The official acronym for the Treasurer's Core Banking System is CB\$.

Source: Program Evaluation Division based on interviews with and documents provided by the agencies being evaluated.

Exhibit 6: Controller Has Primary Responsibility for the Comprehensive Annual Financial Report



Note: State agencies and other entities outside the scope of this evaluation are shaded.

Source: Program Evaluation Division based on interviews with and documents provided by the agencies.

3. What budget and financial management functions are performed by budget offices, controllers, and treasurers in other states?

The Program Evaluation Division contacted six national organizations that provide oversight and assistance to state agencies performing budget and financial management functions of state government to identify best practices for structuring these functions.¹⁹ The intent of this request was to compare North Carolina's structure for budget and financial management to best practices. All of the organizations reported they did not recommend best practices for structuring the budget and financial management functions for state government. Several of the organizations had standards

¹⁹ The following organizations were contacted: National Association of State Budget Offices; Government Accounting Standards Board; National Association of State Auditors, Comptrollers and Treasurers; Government Finance Officers Association; National Association of State Treasurers; and Advancing Government Accountability.

or recommended best practices for specific budget and financial management tasks, but these standards or best practices did not speak to where these functions should be located in state government because local custom affects the structure for budget and financial management functions. Staff at the Governmental Accounting Standards Board stated they did not set standards for structuring budget and financial management functions because some states have constitutional requirements that affect their structure.

Even though the national organizations were unable to provide information on best practices, several of them had compiled information on how all 50 states structure the budget and financial management functions of state government. Exhibit 8 summarizes the different methods used by states to select their controllers and treasurers. North Carolina is one of 16 states where the state controller is appointed by the Governor, and one of 37 states where the state treasurer is elected by the people. The leadership for state budget offices is appointed by the Governor in all 50 states and is not shown in the exhibit.

Exhibit 8

Selection of Controllers and Treasurers in the 50 States

Selection Method	State Controller	State Treasurer
Elected by voters	CA, CT, FL, ID, IL, IN, MD, NV, NY, SC, SD, TX, WV, WY (14)	AL, AZ, AR, CA, CO, CT, DE, FL, ID, IL, IN, IA, KS, KY, LA, MA, MS, MO, NE, NV, NM, NC , ND, OH, OK, OR, PA, RI, SC, SD, TX, UT, VT, WA, WV, WI, WY (37)
Elected by state legislature	TN (1)	ME, MD, NH, TN (4)
Appointed by Governor	AK, AR, DE, GA, HI, LA, MA, MN, MS, NH, NJ, NM, NC , ND, OH, VA (16)	AK, HI, MI, MN, MT, NJ, NY, VA (8)
Appointed by department leadership	AL, AZ, CO, IA, KS, KY, ME, MI, MO, NE, OK, OR, PA, RI, TN, UT, VT, WA, WV (19)	
Other	MT, WI (2)	GA (1)

Notes: Montana’s controller is appointed or hired, and Wisconsin’s controller is selected based on a civil service exam. Georgia’s treasurer is appointed by a depository board. Most of Tennessee’s controller functions are performed by its Department of Finance and Administration, which is appointed by department leadership, but the Comptroller of the Treasury is elected by the legislature. Because West Virginia’s controller functions are split between two agencies with different selection methods, it is listed under both elected by voters and appointed by department leadership. In four states (DE, HI, NJ, and **NC**), the controller is appointed by the governor and approved by the state legislature.

Source: Program Evaluation Division based on two reports: National Association of State Auditors, Controllers and Treasurers. (2008). State Controllers: Technical Activities and Functions; and National Association of State Treasurers. (2004-05). State Treasury Activities & Functions.

The location of state budget offices, controllers, and treasurers within state government include the following arrangements:

- **Freestanding.** The agency is independent and not part of another state agency.
- **Governor’s office.** The agency is part of the Governor’s office.
- **Finance department.** The agency is part of a department that primarily performs financial functions of state government such as budgeting, accounting, and tax collection.
- **Administrative department.** The agency is part of a department that performs management and administrative functions of state government such as personnel, property management, and information technology.
- **State auditor.** The agency is a part of the state auditor’s office.

Exhibit 9 shows where the state budget offices, controllers, and treasurers are located in the 50 states. Overall, state budget offices and controllers are more likely to be located in a finance or administrative department, and state treasurers are more likely to be freestanding agencies.

Exhibit 9: Location of Budget Offices, Controllers, and Treasurers in the 50 States

Location	State Budget Office	State Controller	State Treasurer
Freestanding	CA, CT, ID, IA, KY, NY, VA, WV (8)	CA, CT, GA, ID, IL, MD, MA, NV, NY, NC , SC (11)	AL, AZ, AR, CA, CO, CT, DE, GA, ID, IL, IN, IA, KS, KY, LA, ME, MD, MA, MI, MS, MO, NE, NH, NV, NM, NC , ND, OH, OK, OR, PA, RI, SC, SD, TN, UT, VT, VA, WA, WV, WI, WY (42)
Governor’s office	AK, AZ, CO, FL, GA, IL, MT, NC , TX, UT (10)		
Finance department	AL, HI, IN, ME, MN, MS, NE, NJ, NM, OH, OK, PA, SD, TN, VT, WA (16)	AL, AR, DE, FL, KY, ME, MI, MN, MS, NE, NJ, NM, ND, OH, OK, PA, SD, TN, TX, VT, VA, WA, WI (23)	AK, FL, HI, MN, NJ, NY, TX (7)
Administration department	AR, DE, KS, LA, ME, MD, MA, MI, MO, NE, NV, NH, ND, OR, RI, SC, TN, WI, WY (19)	AK, AR, AZ, CO, HI, IA, KS, KY, LA, ME, MS, MO, MT, NE, NH, OR, RI, TN, UT, WV (20)	MT (1)
State auditor’s office		IN, TN, WV, WY (4)	

Notes: States with budget offices (NE, ME, TN) and states with controllers (AR, KY, ME, MS, NE, TN) in agencies that perform administrative and financial functions are listed under both finance and administration departments. Most of Tennessee’s controller functions are performed by its Department of Finance and Administration, but the Comptroller of the Treasury, who acts as the state auditor, manages and issues debt. Most of West Virginia’s controller functions are performed by the state auditor, but its administration department produces the Comprehensive Annual Financial Report.

Source: Program Evaluation Division based a review of agency websites and on three reports: National Association of State Budget Officers. (2008, Summer). Budget Processes in the States; National Association of State Auditors, Controllers and Treasurers. (2008). State Controllers: Technical Activities and Functions; and National Association of State Treasurers. (2009). State Treasury Profiles.

The Program Evaluation Division also reviewed information to determine if state budget offices, controllers, and treasurers were co-located in the same agency or located in three separate agencies. Exhibit 10 shows North Carolina is one of 22 states where the functions are located in three separate agencies. State budget offices and controllers are co-located in 22 states; four states have the treasurer co-located with either their budget office or their controller.

Exhibit 10

North Carolina Is One of 22 States where Budget and Financial Management Functions Are Located in Three Separate Agencies

Location	States
State Budget Office, Controller, and Treasurer Functions Located in Separate Agencies	AK, AZ, CA, CO, CT, DE, GA, ID, IL, IN, IA, KY, MD, MA, NV, NY, NC , SC, UT, VA, WV, WY (22)
State Budget Office, Controller, and Treasurer Functions Located in Same Agency	MN, NJ (2)
State Budget Office and Controller Functions Located in Same Agency	AL, AR, KS, LA, ME, MI, MO, MS, NE, NH, NM, ND, OH, OK, OR, PA, RI, SD, TN, VT, WA, WI (22)
State Budget Office and Treasurer Functions Located in Same Agency	HI (1)
Controller and Treasurer Functions Located in Same Agency	FL, MT, TX (3)

Source: Program Evaluation Division based on a review of agency websites and three reports: National Association of State Budget Officers. (2008, Summer). Budget Processes in the States; National Association of State Auditors, Controllers and Treasurers. (2008). State Controllers: Technical Activities and Functions; and National Association of State Treasurers. (2009). State Treasury Profiles.

Two states, New Jersey and Minnesota, have co-located their state budget office, controller, and treasurer in a single agency. The New Jersey Department of the Treasury is a large agency that develops and administers the state budget, collects taxes and other revenue, manages statewide services including accounting functions, issues and manages debt, and manages the state’s investments. The department is one of New Jersey’s original state agencies and responsibilities have been added over the years. Minnesota passed a constitutional amendment in 1998 that abolished the election of the state treasurer; an administrative order moved the functions of the state treasury to the Department of Management and Budget in 2003.

The Program Evaluation Division selected five southeastern states to compare the location of their budget and financial management functions to North Carolina’s. The following southeastern states were selected because they were ranked among the top 20 states for their bond rating: Georgia, Florida, South Carolina, Tennessee, and Virginia.²⁰ Agency staff in these states responded to a survey asking whether their agency performed any of the 29 budget and financial management functions identified for this evaluation. Their responses are summarized and compared to North Carolina in Exhibit 11.

²⁰ Program Evaluation Division. (2009, June). *How North Carolina Compares: A Compendium of State Statistics*. Raleigh, NC: General Assembly.

Exhibit 11: Performance of Functions in North Carolina and Selected Southeastern States

Function	State Budget		State Controller		State Treasurer	
	NC	Other States	NC	Other States	NC	Other States
Budget Management						
Budget execution	●	FL, GA, SC, TN, VA				SC
Budget development	●	FL, GA, SC, TN, VA				
Federal and other grant funds oversight	●	FL, GA, SC, TN, VA				SC
Grant monitoring and oversight	●	TN		FL		
Internal service fund oversight	●	TN, VA				
Salary and position control systems	●	FL, GA, SC, TN, VA				
Financial Management						
Cost allocation plan		GA, SC, TN, VA	●	FL, VA		
Fixed asset management	◐	TN		VA		
Internal control structure		FL, TN	●	FL, GA, VA		
Payroll/human resources		TN	●	GA, SC, VA		
Accounting system		TN	●	FL, GA, SC, VA		
Cash Management						
Cash management		GA, TN	●	FL, GA	●	GA, SC, VA
Banking operations				FL	●	GA, SC, TN, VA
Departmental receipt collection	◐	GA, TN			◐	SC, TN
Investment management				FL	●	GA, SC, TN
Non-tax revenue collection			◐		◐	SC, TN
Tax revenue collection						TN
Unclaimed property				FL	●	SC, TN, VA
Debt Management						
Debt management	◐		◐	TN	●	SC, VA
Bond rating	◐	GA, TN, VA	◐	FL, TN	◐	SC, VA
Financial Reporting						
Budget reporting	●	FL, GA, TN	◐	GA		
Financial reporting	◐	TN	◐	FL, GA, SC, TN, VA	◐	GA, SC
Comprehensive Annual Financial Report		TN	●	FL, GA, SC, TN, VA	◐	
Compliance		TN	◐	FL, TN	◐	SC
Auditing						
Financial auditing			◐	TN		TN
Internal auditing oversight	◐		◐	TN		SC, TN, VA
Performance auditing		GA		TN		TN, VA
Benefits Management						
Health care benefits		TN	◐	FL, TN, VA		SC
Retirement system			◐		●	SC, TN

● – NC agency has primary responsibility for function

◐ – NC agency is significantly involved in function

Notes: Because Florida's controller and treasurer are in the same department, their functions only appear in the state controller column. The response from the Tennessee Department of Finance and Administrative is shown under the state budget column, and the response from the Tennessee Comptroller of the Treasury is shown under the state controller column.

Source: Program Evaluation Division based on data provided by the agencies being evaluated and similar agencies in other states.

Three of the states (Georgia, South Carolina, and Virginia) have the same structure as North Carolina with three separate agencies performing budget and financial management functions. In Florida, the state controller and treasurer were located in the same agency in 2003 because Florida voters elected to amend the Florida Constitution to combine the elected comptroller and state treasurer positions into the elected chief financial officer. In Tennessee, the state budget office and controller functions are combined under the Department of Finance and Administration, but the Comptroller of the Treasury, who acts as the state auditor, manages and issues debt for the state.

Research on comparison states shows that certain budget and financial management functions gravitate to the same agencies and that the organization of these functions varies based on specific legal requirements and local custom. For example, in North Carolina and the comparison states, state budget offices have responsibility for most budget management functions, the controller is usually responsible for financial reporting and the Comprehensive Annual Financial Report, and the treasurer is responsible for most cash management functions. Across the five comparison states, multiple agencies are involved in performing the same budget and financial management functions, confirming the literature that state government agencies are interdependent and must collaborate to fulfill their responsibilities.

4. Is it feasible and appropriate to consolidate some or all of the budget and financial management functions in North Carolina?

Consolidation of budget and financial management functions within North Carolina is constrained by constitutional requirements that the Governor prepares and executes the budget and the State Treasurer is an elective officer.²¹ The full consolidation of all budget and financial management functions performed by all three agencies would require amendments to the North Carolina Constitution. Amending the Constitution by legislative initiative requires a three-fifths vote of the North Carolina General Assembly to submit the proposal to the qualified voters of the state for their ratification or rejection by majority vote.²² However, the Program Evaluation Division identified two possible consolidation options that do not require a constitutional amendment. The following options would require statutory changes:

- **Separate budget and financial management agency.** This option would remove State Budget from the Office of the Governor and merge it with the Controller under the Department of Administration to form a budget and financial management agency. The separate positions of state budget officer and state controller would be merged into a chief financial officer position that would oversee the budget and financial management functions of state government.

²¹ North Carolina Constitution, Article III, Sections 5(3), 7(1), (2).

²² North Carolina Constitution, Article XIII, Section 4.

The agency would have two separate divisions. The budget and management division would perform the functions provided by State Budget, and the controller division would perform the functions provided by the Controller. To maintain the constitutional requirement that the Governor prepare and execute the budget, the Governor would appoint the agency head, and the agency head would report directly to the Governor. This option does not affect the financial management functions performed by the Treasurer. The Program Evaluation Division estimates this option would save \$788,000 in Fiscal Year 2010-11 by eliminating management functions that are duplicated by having separate agencies.²³

- **Controller merged with the Treasurer.** Under this option, the Controller would no longer be appointed by the Governor. The Controller would become a division in the Department of the State Treasurer, and the head of the division would report directly to the Treasurer. State Budget would remain in the Office of the Governor so this option adheres to the constitutional requirement that the Governor prepares and executes the budget. The Program Evaluation Division estimates this option would save \$387,000 in Fiscal Year 2010-11 by eliminating management functions for the Controller that are not needed if the controller functions are performed by a division supervised by the Treasurer.²⁴

Although both options have cost savings, they are limited to reductions in the management of the agencies because the Program Evaluation Division did not identify any duplicative functions that could be consolidated or eliminated. In addition, the level of technical expertise needed to perform the budget and financial management functions of state government does not offer immediate opportunities for cross-training or consolidation.

The most significant repercussion of both options is that budget and financial management functions under the Controller would no longer be performed by an independent entity. With a budget and financial management agency, the Governor would have direct control of the budget and financial management functions of state government. If the Controller were merged with the Treasurer, the controller functions would be under the supervision of the Treasurer.

The independence of the Controller in North Carolina was a major priority when the original legislation was enacted in 1986 based on the recommendations of the State Controller Study Commission.

According to the minutes for the legislative commission, Ed Renfrow, the State Auditor in 1986, told the legislative commission that having the

²³ These savings are based on eliminating the salaries and benefits for the following positions from State Budget and the Controller: one agency head, two deputies, two executive assistants, one human resources director, one business officer, and one information technology director. There is only one communications director between the two agencies, so this estimate assumes that position will continue under the separate budget and financial management agency option.

²⁴ These savings are based on eliminating the salaries and benefits for the following positions from the Controller: one agency head, one executive assistant, one human resources director, one business officer, one information technology director, and one communications director. Because the controller division would be led by a deputy under the Treasurer, this estimate does not eliminate the deputy state controller position.

central accounting functions assigned to State Budget could lead to weaknesses in accounting and internal controls because of political pressures to develop "creative accounting schemes" or other unsound accounting practices. He proposed the establishment of a department-level organization that would centralize accounting functions under one management and be isolated from political pressures and changes in administration. C. C. Cameron, the State Budget Officer in 1986, endorsed the proposal to establish a separate controller. He recommended the controller's office be housed in the Department of Administration to comply with the constitutional limit on the number of principal state departments, but he also recommended the office be independent of any daily supervision by the principal department in which it was located.

Based on the recommendations from the State Auditor and the State Budget Officer, the General Assembly enacted legislation establishing the Controller and locating the office administratively within the Department of Administration, but the law specified that the office would exercise its prescribed powers independently of the Secretary of Administration. State law also stipulates that the Governor appoints and the Legislature confirms the Controller for a seven-year term. Because the Controller can only be removed by the Governor for cause, the Controller operates independently, reducing the likelihood of political influence.

Twenty-four years after the enactment of legislation establishing the Controller, the independence of the Controller continues to be a priority. During interviews with staff from each agency, the Program Evaluation Division heard that an independent controller was one of the strengths of North Carolina's structure for the budget and financial management of state government. The Controller emphasized that budgeting is a political process and accounting is an independent, objective process and noted that being an independent, non-partisan entity made the office unique because its decisions are informed by accountants, not swayed by politics. State Budget noted that they were closely identified with the Governor and the budget process, and the Controller is more independent, which keeps the information from each agency separate and objective. The Treasurer stated that accounting functions should not be under the purview of the Treasurer because there could be issues with internal controls for cash management.

The Program Evaluation Division also interviewed staff from the Office of the State Auditor and the Fiscal Research Division because they have regular interaction with the three agencies being evaluated and are involved with the budget and financial management of state government. The staff for the State Auditor indicated that an independent controller is not as easily influenced by the Governor as the director of State Budget, and the separation of budget from accounting functions improves the "control environment" when they audit the Comprehensive Annual Financial Report. The staff suggested that combining budget and accounting functions could increase the risk that auditors would not find problems with financial reports if there was an attempt to cover up errors. The State Auditor's staff also expressed

concern about merging the Controller with the Treasurer because they preferred the responsibility for reporting receipts remain segregated from the custody of assets to insure that the loss of funds cannot be hidden. Staff from the Fiscal Research Division reported they benefited from a separate controller because the Controller was an independent source for financial information.

In summary, the Program Evaluation Division's analysis of how State Budget, the Controller, and the Treasurer perform budget and financial management functions determined that there is no duplication of effort among the three agencies. Although data from other states shows that location and organization of budget and financial management functions vary based on specific legal requirements and local custom, the Program Evaluation Division observed that North Carolina is one of 22 states with the structure of locating budget and financial management functions in three separate agencies. Consolidating some budget and financial management functions of state government is feasible for North Carolina and could save money, but the Program Evaluation Division determined that consolidation would sacrifice the independence of the Controller.

Appendices

Appendix A: Summary of Fiscal Year 2008-09 Expenditures for Budget and Financial Management Functions Performed by State Budget, the Controller, and the Treasurer

Appendix B: Description of Budget and Financial Management Functions Performed by State Budget, the Controller, and the Treasurer

Agency Response

A draft of this report was submitted to the Office of State Budget and Management, the Office of the State Controller, and the State Treasurer to review and respond. Their responses are provided following the appendices.

Program Evaluation Division Contact and Acknowledgments

For more information on this report, please contact the lead evaluator, Carol Shaw, at carol.shaw@ncleg.net.

Staff members who made key contributions to this report include Sean Hamel, E. Kiernan McGorty, and Pamela L. Taylor. John W. Turcotte is the director of the Program Evaluation Division.

Appendix A: Summary of Fiscal Year 2008-09 Expenditures for Budget and Financial Management Functions Performed by State Budget, the Controller, and the Treasurer

Domain	State Budget		State Controller		State Treasurer		Domain Totals	
	Expenditures	Positions	Expenditures	Positions	Expenditures	Positions	Expenditures	Positions
Budget Management	\$ 5,207,486	33.65	\$ 45,780	0.60	\$ 0	0.00	\$ 5,253,266	34.25
Financial Management	231,036	2.79	19,547,924	152.71	20,200	0.25	19,799,160	155.75
Cash Management	19,606	0.38	690,887	8.24	10,439,524	65.70	11,150,017	74.32
Debt Management	172,000	2.00	77,948	0.80	480,000	4.00	729,948	6.80
Financial Reporting	95,236	1.83	962,963	10.00	646,000	7.50	1,704,199	19.33
Auditing	1,079,000	11.20	27,613	0.28	0	0.00	1,106,613	11.48
Benefits Management	52,300	0.30	775,610	12.11	15,739,657	161.00	16,567,567	173.41
Totals	\$ 6,856,664	52.15	\$ 22,128,725	184.74	\$ 27,325,381	238.45	\$ 56,310,770	475.34

Source: Program Evaluation Division based on data provided by the state agencies shown.

Appendix B: Description of Budget and Financial Management Functions Performed by State Budget, the Controller, and the Treasurer

Function	State Budget	State Controller	State Treasurer
Budget Management			
Budget execution	<ul style="list-style-type: none"> • Perform budget certification • Review and approve budget adjustments and revisions • Review and approve new budget codes and cost centers • Monitor state revenue collection • Review information technology budget changes and capital project adjustments • Control allotments to state agencies • Monitor and review monthly budget reports • Perform year-end closeout of budgets and review requests to carry forward funds • Review and approve budget deviations • Monitor salary and position control • Review and approve new positions • Monitor federal funds 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Budget development	<ul style="list-style-type: none"> • Issue budget preparation instructions • Forecast tax and non-tax revenue estimates • Review, adjust, and prepare agency continuation budgets • Review and analyze expansion budget requests, capital improvements, and information system requests • Prepare and present Governor's Summary of Recommendations to the General Assembly 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Federal and other grant funds oversight	<ul style="list-style-type: none"> • Oversee development and submission of federal block grant plans • Develop continuation and expansion budgets for state programs where costs are shared with the federal government or other sources of receipts • Review and approve state agency requests for budget adjustments related to increased or decreased availability of federal funds or other receipts 	<ul style="list-style-type: none"> • Collect data from state agencies that receive funds from federal programs identified by the Cash Management Improvement Act of 1990 and review for compliance with the Treasury State Agreement 	<ul style="list-style-type: none"> • None

Function	State Budget	State Controller	State Treasurer
Budget Management continued			
Grant monitoring and oversight	<ul style="list-style-type: none"> • Establish rules, policies, and procedures for disbursement of grants for agency oversight, monitoring, and evaluation of grantees and subgrantees • Oversee adherence to annual reporting requirements • Maintain NCGrants online reporting website • Maintain suspension of funding list identifying all noncompliant grantees • Develop and provide training for grantees • Submit annual report to the General Assembly 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Internal service fund oversight	<ul style="list-style-type: none"> • Provide budget oversight for all agency internal service funds • Approve rates and fees for shared statewide technology services provided by the Office of Information Technology Services on a fee-for-service basis and not covered by another fund • Provide assistance in developing rates and fees for internal service funds as requested by state agencies 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None
Salary and position control systems	<ul style="list-style-type: none"> • Monitor agency salary commitments as compared to the authorized budget • Maintain the Salary Control System as a record-keeping tool for state agencies • Review budgeted position counts and ensure they match BEACON/Human Resources position counts • Approve new positions in BEACON before employees can be paid 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None

Function	State Budget	State Controller	State Treasurer
Financial Management			
Cost allocation plan	<ul style="list-style-type: none"> Assist state agencies by analyzing cost allocation methodologies and offering improvement suggestions 	<ul style="list-style-type: none"> Contract for and assist with the compilation of a Statewide Indirect Cost Allocation Plan 	<ul style="list-style-type: none"> None
Fixed asset management	<ul style="list-style-type: none"> Manage and oversee capital assets including information technology systems and physical construction Prepare Governor's capital budget and six-year Capital Improvement Plan Manage the Capital Budget and Repair and Renovation Program Oversee funding for information technology projects including stopping funding for cancelled projects, approving projects at each phase from a cost-benefit standpoint, and approving change requests 	<ul style="list-style-type: none"> Establish fixed asset policy for state agencies in accordance with generally accepted accounting principals Monitor and maintain compliance with capital asset policies Provide a fixed asset module through the North Carolina Accounting System 	<ul style="list-style-type: none"> None
Internal control structure	<ul style="list-style-type: none"> None 	<ul style="list-style-type: none"> Establish standards, policies, and procedures for a system of internal control Develop guidance materials and provide training on internal control best practices Assist state agencies in evaluating their internal control effectiveness Perform periodic reviews of the effectiveness of state agency internal control structures and ensure compliance with state law 	<ul style="list-style-type: none"> None
Payroll/Human resources	<ul style="list-style-type: none"> Conduct annual salary/full-time equivalent survey with the Fiscal Research Division to determine salary and benefit costs for state government 	<ul style="list-style-type: none"> Manage and operate the centralized payroll system for most state agencies Manage statewide benefit plan administration and enrollment Provide training and technical support to agencies 	<ul style="list-style-type: none"> None
Accounting system	<ul style="list-style-type: none"> None 	<ul style="list-style-type: none"> Develop, maintain, and support uniform accounting policies, a uniform statewide chart of accounts, and comprehensive and uniform financial accounting and reporting Provide and support the core business functions for agency and central managers through several enterprise systems including the North Carolina Accounting System, Decision Support System, and Cash Management Control System 	<ul style="list-style-type: none"> None

Function	State Budget	State Controller	State Treasurer
Cash Management			
Cash management	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Develop and implement a statewide cash management plan prescribing policy and procedures for the receipt, deposit, and disbursement of state funds • Administer the state disbursing system and maintain a cash management system for state agencies • Reconcile and balance accounts with the Treasurer • Promote and manage the statewide E-Commerce Program 	<ul style="list-style-type: none"> • Establish and manage deposit relationships with banks across the state • Reconcile and balance accounts with the Controller • Pay warrants when state agencies spend money • Invest excess funds
Banking operations	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Establish security for online bank services for participants in the statewide master service agreement for electronic funds transfer 	<ul style="list-style-type: none"> • Provide banking services to state agencies • Maintain relationships with six major banks and 90 community banks • Provide depository services for nearly 800 locations • Reconcile all main and community bank accounts on behalf of the Treasurer • Compile cash flow daily and determine daily investment of excess funds • Manage electronic warrants issued by agencies
Departmental receipt collection	<ul style="list-style-type: none"> • Receive civil penalties and forfeitures from state agencies and transfer these funds to the Department of Public Instruction • Approve the percentage cost of collection that agencies are allowed to retain 	<ul style="list-style-type: none"> • Administer statewide budget codes that receive miscellaneous funds 	<ul style="list-style-type: none"> • Assist state agencies with the deposit of departmental receipts into state bank accounts and ensure funds are properly credited
Investment management	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Invest the assets of the state's pension funds, escheats funds, and cash management program utilizing both internal and external asset management
Non-tax revenue collection	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Receive funds for non-tax revenue deposited directly to the General Fund • Receive and account for funds identified as support for the General Fund as identified in the Appropriations Act (e.g., Highway Fund) 	<ul style="list-style-type: none"> • Assist state agencies with the deposit of non-tax revenue into state bank accounts and ensure funds are properly credited
Tax revenue collection	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None

Function	State Budget	State Controller	State Treasurer
Cash Management continued			
Unclaimed property	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • None 	<ul style="list-style-type: none"> • Collect and safeguard unclaimed and abandoned property • Ensure unclaimed property remitted to the Escheats Fund is reunited with the rightful owner if possible • Invest monies collected to maximize earnings for utilization by the North Carolina Education Assistance Authority
Debt Management			
Debt management	<ul style="list-style-type: none"> • Recommend options for debt financing of capital projects • Oversee debt authorized projects ensuring scope and time restrictions on debt issuance are met • Project expenditures to help inform debt issuance • Authorize budget changes to debt projects • Certify funds are available for debt service before new debt is authorized • Serve on the Debt Affordability Advisory Committee 	<ul style="list-style-type: none"> • For Statewide Special Indebtedness budget codes, update, verify, and monitor the amounts requested and expended by state agencies • For General Obligation Bonds, verify the amount needed for statewide bond expenditures and prepare, update, and reconcile the Cash Management Control System and the North Carolina Accounting System entries for bond proceeds and provide the information to the Treasurer 	<ul style="list-style-type: none"> • Plan, develop, and issue appropriate debt instruments consistent with the terms of the authorizing legislation or other directives • Manage the repayment of debt • Administer all debt instruments until maturity
Bond rating	<ul style="list-style-type: none"> • Maintain conservative fiscal management of the state budget • Maintain moderate debt levels 	<ul style="list-style-type: none"> • Prepare the Comprehensive Annual Financial Report • Contribute to and review documents related to full disclosure and due diligence activities for bond offerings and credit update meetings 	<ul style="list-style-type: none"> • Manage North Carolina's debt capacity

Function	State Budget	State Controller	State Treasurer
Financial Reporting			
Budget reporting	<ul style="list-style-type: none"> Oversee and monitor monthly budget reports for compliance with the Executive Budget Act and other policies Prepare the following reports: Biennial Fee Report, Lease-Purchase Report, Staffing Analysis of State Business Functions, Occupational Licensing Board Report, Civil Penalties Annual Collection Cost Analysis, and Personal Services Contract 	<ul style="list-style-type: none"> Create reports in the North Carolina Accounting System by interfacing with the Budget Preparation System that compares actual expenditures to authorized budgets Include budget to actual compliance statements and disclosures in the Comprehensive Annual Financial Report 	<ul style="list-style-type: none"> None
Financial reporting	<ul style="list-style-type: none"> Prepare Governor's recommended budget and <i>Post Legislative Summary</i> Complete national surveys of financial information Coordinate and prepare financial data for bond rating agencies Prepare data for the Official Bonds Statements 	<ul style="list-style-type: none"> Produce monthly General Fund and other state funds summaries Prepare the following reports: Annual Financial Report, Single Audit Schedule of Federal Awards, Statewide Accounts Receivable Report, and Information Technology Expenditure Report 	<ul style="list-style-type: none"> Prepare monthly, quarterly, and annual balance sheet and income statements for the various portfolios in the investment pool
Comprehensive Annual Financial Report (CAFR)	<ul style="list-style-type: none"> Provide limited statewide information for statewide CAFR footnotes and the Management's Discussion and Analysis Letter 	<ul style="list-style-type: none"> Plan, consult, compile, and publish the CAFR for North Carolina state government Research, interpret and implement generally accepted accounting principles Provide support to agencies to assure compliance with generally accepted accounting principles and state financial policies and procedures 	<ul style="list-style-type: none"> Provide statewide information for CAFR footnotes on investments, debt, pension plans, disability plans, death benefit plans, and supplemental retirement plans
Compliance	<ul style="list-style-type: none"> Provide data to bond rating agencies to demonstrate compliance with financial-related laws and regulations Identify state employees that owe debt to the state 	<ul style="list-style-type: none"> Serve as the state contact for resolving state agency tax and employment issues with the Internal Revenue Service, Social Security Administration, and North Carolina Department of Revenue Ensure statewide compliance with laws and regulations related to the employment of foreign nationals Prepare required reports related to the expenditure of federal funds 	<ul style="list-style-type: none"> Oversee compliance with secondary market disclosure requirements and arbitrage rebate requirements

Function	State Budget	State Controller	State Treasurer
Auditing			
Financial auditing	<ul style="list-style-type: none"> Conduct internal audits as requested by agencies Conduct testing of high-risk accounts to ensure proper internal controls are in place 	<ul style="list-style-type: none"> Coordinate inquiries from federal agencies and state entities to meet federal single audit requirements Manage the overpayment audit contract 	<ul style="list-style-type: none"> None
Internal auditing oversight	<ul style="list-style-type: none"> Maintain internal audit guidelines and state agency internal audit plans and reports Provide support and staff for the Council of Internal Audit Administer internal audit program Provide training and support to state agencies 	<ul style="list-style-type: none"> Serve as chair of the Council of Internal Auditing and lead the Council in fulfilling its legislative duties including promulgating guidelines for agencies and developing internal audit guides, technical manuals, and suggested internal audit best practices 	<ul style="list-style-type: none"> None
Performance auditing	<ul style="list-style-type: none"> Conduct operational audits to identify improvements in processes to ensure agencies are meeting their objectives Perform management and efficiency audits including agency structure, workload, staffing, program evaluations, and cost-benefit analysis Provide independent third-party review of statewide programs to assess their effectiveness and identify improvements 	<ul style="list-style-type: none"> None 	<ul style="list-style-type: none"> None
Function	State Budget	State Controller	State Treasurer
Benefits Management			
Health care benefits	<ul style="list-style-type: none"> Monitor and assist with development of the State Health Plan's benefit costs for the Governor's budget proposal 	<ul style="list-style-type: none"> Manage and coordinate payment, accounting, and reporting of the State Health Plan, NCFlex plans, and agency-specific after-tax plans Provide financial/accounting functions for NCFlex and the Workers' Compensation Cost Containment Program 	<ul style="list-style-type: none"> None
Retirement system	<ul style="list-style-type: none"> Monitor and assist with development of the retirement system's benefit costs as a part of the Governor's proposed budget 	<ul style="list-style-type: none"> Operate the BEACON system, which enrolls employees into the retirement system and processes retirement contributions through the accounting system 	<ul style="list-style-type: none"> Operate all aspects of the retirement system (e.g., member services, record keeping, retirement processing, benefits processing, compliance)



**STATE OF NORTH CAROLINA
OFFICE OF STATE BUDGET AND MANAGEMENT**

BEVERLY EAVES PERDUE
GOVERNOR

CHARLES E. PERUSSE
STATE BUDGET DIRECTOR

April 14, 2010

Mr. John Turcotte
Director, Program Evaluation Division
North Carolina General Assembly
212 Legislative Office Building
300 N. Salisbury St.
Raleigh, NC 27603

Dear Mr. Turcotte:

Thank you for the opportunity to review and comment on the Program Evaluation Division's report, "Feasibility of Restructuring the Budget and Financial Management of North Carolina State Government." The report documents the functions and responsibilities of OSBM, State Controller and State Treasurer for the budget and financial operations of the state.

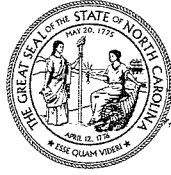
We find the report to be an accurate description of how OSBM, State Controller and State Treasurer operate in North Carolina. Since the report has no recommendations, we can only respond that the current operations of these three state agencies operate effectively for the state. As evidence, we continue to be one of only seven states with a Triple A rating from each of the major bond rating agencies.

Thank you again for the opportunity to review and comment and for the thoroughness of this report.

Sincerely,

A handwritten signature in black ink that reads "Charles Perusse".

Charles Perusse



State of North Carolina

Office of the State Controller

DAVID T. McCoy
STATE CONTROLLER

March 25, 2010

Mr. John Turcotte, Director
Program Evaluation Division
North Carolina General Assembly
Legislative Office Building, Suite 100
300 North Salisbury Street
Raleigh, North Carolina 27603-5925

Dear Mr. Turcotte:

I am writing to express my appreciation to the Program Evaluation Division (PED) Project Team led by Carol Shaw for the professional and objective manner in which the "*Feasibility of Restructuring the Budget and Financial Management of North Carolina State Government*" study was conducted.

The OSC office agrees with the PED report finding that there is no duplication of budget and financial management functions by the three entities studied. Further, OSC agrees with the PED conclusion that consolidation of the entities would sacrifice the independence of the State's Controller; a very important attribute that enhances the segregation of duties which provides enhanced internal controls that are important to the financial management of state funds and the investing community including the bond rating agencies. As only one of only three states that is the recipient of the GFOA Certificate of Excellence for Financial Reporting and is AAA bond rated, it is clear that the Legislature made a fiscally prudent decision 24 years ago when it created an independent State Controller's Office.

In addition to the "no duplication" finding, the PED report points out that North Carolina is performing the budget and financial management functions with about 22% less staff than the average of the other 50 states and with considerably less staff than the other AAA bond rated states.

OSC appreciates the opportunity to respond to the report's findings.

With regards, I am

Sincerely,


David T. McCoy



NORTH CAROLINA

OFFICE OF THE TREASURER

JANET COWELL, TREASURER

April 14, 2010

John Turcotte, Director
Program Evaluation Division
212 Legislative Office Building
300 N. Salisbury Street
Raleigh, NC 27603

Dear Mr. Turcotte:

Thank you for the opportunity to review the report on Feasibility of Restructuring the Budget and Financial Management of North Carolina, and for allowing us to respond to the findings. In general, we agree with the conclusions within the report. Although there could be some cost savings attributed to merging the State Controller with either the office of State Budget or State Treasurer, a vital component of the Controller's function is as an independent body and contributes to the strength of the internal controls over financial matters within state government. However, below are a few items we feel should be considered as clarifications or modifications for the report in order to provide an accurate overview of the financial operations of the state.

Our most significant concern with the report is your working definitions of the terms "cash management" and "financial management". We believe you have the definitions reversed in that the common understanding of cash management is narrowly defined as short-term cash flows and investments. Financial management is commonly understood to be much broader in scope and includes concepts of governance, long-term investments, fiscal oversight, and compliance. Therefore, we believe that the responsibility statements on page 9 are a misleading representation of the key roles of the offices of the state Controller and Treasurer. The report reflects that the Controller is primarily responsible for financial management and the Treasurer is primarily responsible for cash management.

Additionally, there are some key functions that should be realigned to clarify these roles further. Referring to Exhibits 2 and 3, we believe that investment management should be taken out of cash management and moved to financial management. The Compliance function should be removed from financial reporting and inserted under financial management.

The key function that seems to be missing from the domain lists is the concept of governance. This key function has been a core focus of the Treasurer's office and should be added under the financial management domain. Governance structure is a critical issue to consider in all areas of state government, especially in those areas that include investment of state funds. The fiduciary standard and oversight for all investments resides with the State Treasurer.

We believe that the most significant opportunity to improve financial management in the State lies not in the merging of centralized core financial functions (Department of State Treasurer, State Controller, etc.), but in exercising greater controls over decentralized financial functions operating in agencies that do not have these as traditional roles. Given the increasing complexity of financial transactions and oversight, building best practice professional teams is expensive, time-consuming, and requires specialized expertise. We support the

time honored tradition of centralized financial management and would strengthen it by, for example, requiring individuals or Departments investing money on behalf of the State to meet minimum professional standards, ethics policies, etc. We are already taking action by collaborating with the legislature to form a study commission to look at investment oversight and authority across the state.

In conclusion, while we agree with the overall conclusions drawn within the report, we believe that making these distinctions between financial management and cash management, and the inclusion of the governance function will provide better context and role definition for the report. Further, we support the centralized model of financial management that has served the State well in the past and believe the agencies reviewed in this study should leverage their expertise in financial matters by playing a stronger role in oversight of financial functions across the State to control risk and optimize financial outcomes.

Sincerely,

A handwritten signature in black ink that reads "Janet Cowell". The signature is written in a cursive, flowing style.

Janet Cowell
State Treasurer