**Model Preaudit Policy**

\*This model preaudit policy reflects a basic preaudit process that is required before a unit obligates the expenditure of public monies to pay for the purchase of goods or services, or executes a contract obligating the unit to pay monies. Each unit must edit the policy to reflect its specific preaudit process undertaken by the finance officer or a duly appointed deputy finance officer.

1. **Purpose and Scope**

As required by N.C.G.S.§ 159-28(a), the [JURISDICTION NAME] shall not incur an obligation to support any program, function, or activity unless the annual budget ordinance or a project/grant ordinance includes an appropriation authorizing the obligation and an unencumbered fund balance remains in the appropriation that is sufficient to pay the sums obligated by the transaction.[[1]](#footnote-1) The purpose of this policy is to establish a preaudit process to assure that the [COUNTY/CITY/TOWN (hereinafter “UNIT”)] obligates and expends funds in compliance with the preaudit requirements set forth in N.C.G.S. § 159-28.

The terms of this policy shall apply to the finance officer, any deputy finance officer(s) duly appointed by the governing board, and any employee(s) who is responsible for initiating purchases or otherwise obligating public monies to support any program, function or activity accounted for in a budgeted fund.

1. **Preaudit Requirement**

A preaudit is required by law when:

1. The [UNIT] will enter into a contract or agreement, or place an order for goods or services, that is accounted for in the budget ordinance or a project/grant ordinance; and
2. The [UNIT] will be obligated to pay money by the terms of the contract, agreement, or purchase order, and
3. If the obligation is accounted for in the annual budget ordinance, the [UNIT] anticipates paying at least some of the money in the fiscal year in which the contract, agreement, or purchase order is entered. If the obligation is accounted for in a project ordinance, a preaudit is required when the first two criteria are satisfied.
4. **Requisition Process[[2]](#footnote-2)**

Authorized staff who are responsible for entering into contracts, agreements, or purchase orders that obligate the unit to pay money to an external vendor or contractor, shall submit an email request to the finance department at [INSERT EMAIL ADDRESS] to initiate the preaudit process. The request shall include the following information:

* Description of the contract/purchase;
* Any quotes received related to the purchase;
* Bid documents, when applicable;
* Name and contact information of the selected vendor/service provider/contractor.
* Estimated date of delivery of goods or performance of services (the anticipated date upon which payment will be due and owing);
* Identification of the budget appropriation that allows for the expenditure (i.e., which department, function, or project will be paying for the obligation);
* Any additional supporting documentation as required by local policy (*e.g.,* documentation of internal approvals for expenditures),

**Review Purchase Requisition Request:** Finance staff shall review submissions of purchase requisitions for completeness. Incomplete requests shall be returned to the requestor.

1. **Preaudit Process for Non-Electronic Purchases**

To preaudit an obligation of public moneys, the finance officer or a duly appointed deputy finance officer shall take the following steps:

1. **Verify Budget Appropriation:** The finance officer/deputy finance officer shall review the annual budget ordinance or a project/grant ordinance to determine whether the ordinance includes an appropriation authorizing the obligation.  Obligations of appropriations within the annual budget ordinance shall be reviewed at the budgeted level—either by department, function, or activity.[[3]](#footnote-3)

1. **Verify Sufficient Funds Remain in the Appropriation:** The finance officer/deputy finance officer shall verify that there is sufficient unencumbered fund balance in the respective budget appropriation to cover the cost of the obligation as follows:
2. For obligations that have been appropriated in the annual budget ordinance, the finance officer/deputy finance officer shall verify that an unencumbered fund balance remains in the appropriation that is sufficient to pay the amount of the obligation that is expected to become due and payable during the current fiscal year.
3. For multi-year or continuing contracts accounted for in the annual budget ordinance, the finance officer/deputy finance officer shall verify that an unencumbered fund balance remains in the appropriation that is sufficient to pay the amount of the obligation that is expected to become due and payable during the current fiscal year.[[4]](#footnote-4)
4. For obligations that support a capital project or grant-project ordinance, the finance officer/deputy finance officer shall verify that the project/grant project ordinance includes an appropriation authorizing the obligation and that an unencumbered balance remains in the appropriation sufficient to pay the full amount of the obligation.[[5]](#footnote-5)
5. **Record Encumbrance**: The finance officer or deputy finance officer shall ensure that an encumbrance for the obligation is recorded in the annual budget ordinance or project ordinance.
	1. For appropriations in the annual budget ordinance, the encumbrance shall be for the total amount anticipated to be expended during the current fiscal year.
	2. For appropriation in a project/grant ordinance, the encumbrance shall be for the full amount of the obligation.

1. **Affix and Sign Preaudit Certificate:** If an obligation is reduced to a written contract, agreement, or purchase order requiring the payment of money, the contract, agreement, or purchase order shall include on its face a preaudit certificate. The certificate shall be signed by the finance officer/deputy finance officer and take substantially the following form: *“This instrument has been preaudited in the manner required by the Local Government Budget and Fiscal Control Act.”*
2. **Exemptions from Preaudit Certificate Requirement**

In limited circumstances, certain transactions are exempted from the preaudit certificate requirement even when the contract, agreement, or purchase order is in writing. The finance officer/deputy finance officer shall still perform the preaudit steps 1-3 outlined in Section IV. The exemption only applies to the preaudit certificate.

1. **Any obligation or document that has been approved by the Local Government Commission**. A preaudit certificate is not required for any loan agreements, debt issuances, and other leases and financial transactions, including audit contracts, that are subject to LGC approval and have, in fact, been approved by the LGC.
2. **Payroll expenditures, including employee benefits.** Salary and benefit changes for current employees, even if in writing, do not require a preaudit certificate.
3. **Electronic payments, which include payments made by credit cards, debit cards, gas cards, or procurement cards (P-Card).** A preaudit certificate is not required to be attached to the writing evidencing the transaction made by an electronic payment. To take advantage of this exemption, the finance officer/deputy finance officer shall preaudit electronic purchases according to the process set forth in section VI of this policy.
4. **Preaudit Process for Electronic Transactions[[6]](#footnote-6)**

In order to take advantage of the exemption from the preaudit certificate requirement for electronic transactions, the finance officer/deputy finance officer shall preaudit electronic payment transactions (i.e., purchases made by credit cards, debit cards, gas cards, or procurement cards) as follows:

1. **Verify Budget Appropriation:** The finance officer/deputy finance officer shall review the annual budget ordinance or the respective project ordinance to determine whether the ordinance includes an appropriation authorizing the obligation. The review of the annual budget ordinance shall take place at the budgeted level—either by department, function, or activity.
2. **Verify Sufficient Funds Remain in the Appropriation:** The finance officer/deputy finance officer shall verify that there is sufficient unencumbered fund balance in the respective budget appropriation to cover the cost of the obligation.
3. **Encumber Obligated Funds**: The finance officer or deputy finance officer shall ensure that sufficient funds are preencumbered on a [weekly or monthly basis] to cover any amount of electronic payments that may become due and payable. When preauditing electronic payments, the Finance Officer or duly authorized deputy shall ensure that sufficient funds remain within the encumbrance. If not, additional funds may need to be encumbered to cover the costs expected to become due.

(For example, the police department will need to preencumber funds that will be used to fill patrol cars with gasoline every month. Blanket purchase orders may be used to preencumber funds. Funds should not be preencumbered on an annual basis--monthly or weekly encumbrances for electronic payments are recommended.)

1. **Use of Automated System for Preaudit**

The use of an automated financial comuter system may be used to meet preaudit requirements if the automates system meets the following requirements: (1) rmbedded functionality that determines that there is an appropriation to the department, function code, or project in which the transaction appropriately falls; (2) functionality ensuring that unencumbered funds remain in the appropriation to pay out any amounts that are expected to come due during the budgeted period; and (3) real‑time visibility to budget compliance, alert threshold notifications, and rules‑based compliance measures and enforcement.

When an automated system is used, the finance officer shall certify to the Secretary of the Commission no later than 30 days after the start of the fiscal year that the automated financial computer system meets all the requirements of subsection of this section.

1. **Penalties for Noncompliance**

If an obligation accounted for in the annual budget ordinance is not preaudited in accordance with the requirements of G.S. 159-28, the contract, agreement, or purchase order is void and unenforceable.

If an officer or employee of a local government incurs an obligation in violation of the preaudit forth in G.S. § 159-28, or gives a false preaudit certificate to any contract, agreement, purchase order, check, draft, or another document, that officer or employee, and the sureties on any official bond for that officer or employee, are liable for any sums illegally committed or disbursed thereby.

The governing board shall determine, by resolution, if payment from the official bond shall be sought and if the governing body will seek a judgment from the finance officer or duly appointed deputy finance officer for any deficiencies in the amount.

1. An obligation is incurred any time the [UNIT] enters into a contract, agreement, purchase order, or otherwise commits itself to pay money, in any amount, to another entity. [↑](#footnote-ref-1)
2. Note to drafter: This section is not required to be included in the preaudit policy. Local governments may have a separate purchasing policy that addresses the requisition process. [↑](#footnote-ref-2)
3. For example, if the obligation is related to a purchase request from the parks and recreation department, the finance officer will check the budget for that department to determine if the obligation is allowable. The finance officer will also check the Parks and Recreation fund in verifying that sufficient funds remain, which is the second step in the preaudit process. [↑](#footnote-ref-3)
4. For a multi-year or continuing contract accounted for in the annual budget ordinance, a preaudit of the full contract price is not required. It is only the amount expected to come due in the current fiscal year that is subject to the preaudit process. However, G.S. § 159-13 generally requires a governing board to appropriate sufficient moneys each year to cover the amounts due that year under continuing contracts, but [↑](#footnote-ref-4)
5. Because project ordinances and grant project ordinances extend for the life of the project, it does not matter in which fiscal year monies will be paid. The finance officer must preaudit the total cost of the obligation during the preaudit process. [↑](#footnote-ref-5)
6. Note to Drafter: To take advantage of the third exemption for electronic transactions, the local government is required by law to take the following steps:

	1. **Resolution**: Adopt a resolution authorizing the unit to engage in electronic transactions. Model resolution available here
	2. **Encumbrance system**: Implement an encumbrance system that tracks expenditures against budget appropriations.
	3. **Written Policy**. The governing board or finance officer if authorized to do so, must adopt written policies that outline the procedures for using p-cards, credit cards, and/or fuel cards.
	4. **Staff training**: All personnel must be provided with training.
	5. **Financial reports**: Each quarter, the unit shall provide a budget-to-actual statement that includes budget accounts, payments made, encumbrances, including electronic obligations; and the amount of the unobligated fund balance for all major funds. [20 NCAC 03.0409](http://reports.oah.state.nc.us/ncac/title%2020%20-%20state%20treasurer/chapter%2003%20-%20local%20government%20commission/20%20ncac%2003%20.0409.pdf)To comply with the written policy requirement, all units must establish a process for preauditing electronic transactions. Each unit may handle electronic transactions differently. At minimum, the process must incorporate the steps outline in section VI of this model policy. The unit may want to address how it encumbers funds for electronic purposes (e.g., is a blanket PO issued; do P-Care holders have funds encumbered on a monthly/weekly basis, etc.). [↑](#footnote-ref-6)