

NORTH CAROLINA
DEPARTMENT OF STATE TREASURER



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Module 4: Preaudits & Disbursements



What is a Preaudit?

Under North Carolina law:

“No obligation may be incurred in a program, function, or activity accounted for in a fund included in the budget ordinance **unless** the budget ordinance includes an appropriation authorizing the obligation **and** an unencumbered balance remains in the appropriation sufficient to pay in the current fiscal year the sums obligated by the transaction for the current fiscal year.”^[1]

When a local government **preaudits** an obligation, it is simply ensuring that these requirements have been met.

^[1][G.S. 159-28\(a\)](#)



What is a Preaudit?

In essence, a **preaudit** is the act of ensuring that for every financial obligation a unit makes:

1. Funds have been budgeted
2. Funds are actually available

A preaudit must be carried out **before** any obligation is incurred.

- The **finance officer** is responsible for establishing procedures to ensure that the preaudit requirement is consistently met.^[2]
- Specific language must be included on written agreements, such as contracts and purchase orders, certifying that the document has been preaudited as required by statute.^[3]
 - This certificate must be signed by the finance officer or a deputy finance officer approved by the governing board.
 - An exemption to the certificate requirement is provided for certain electronic payments. See slide 8.

^[2][G.S. 159-28\(a2\)](#) ^[3][G.S. 159-28\(a1\)](#)



Why Preaudit?

Preaudits are a core component of effective fiscal management:

- The preaudit requirement ensures that no obligation is incurred without sufficient funds in the budget.
- By not spending money it does not have, a unit stands a better chance of staying within its budget throughout the fiscal year.





Fund Availability

To fulfill the second component of the preaudit requirement, a unit must ensure that enough **unencumbered funds** are on hand to cover all costs associated with an obligation for the current fiscal year.

Unencumbered funds are distinct from total funds in the budget, which may include money which has already been encumbered (set aside) for other purposes.

For Example:

The city of Dogwood wants to spend \$10,000 on new office furniture for the finance department during the current fiscal year.

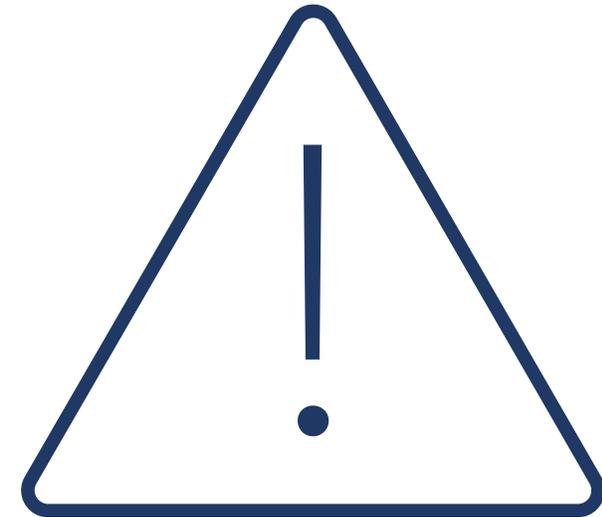
Dogwood has \$20,000 in the budget for furniture, but \$15,000 has already been encumbered to purchase items for the city's board room.

That means just \$5,000 are only unencumbered funds, so Dogwood cannot incur the \$10,000 obligation for the finance office furniture.



Failure to Preaudit

- If a unit fails to perform a preaudit for an obligation (contract, purchase order, etc.), that obligation is invalid and may not be enforced.^[4]
- The finance officer can be held personally liable for payments made against an invalid obligation.^[5]



^[4][G.S. 159-28\(a2\)](#) ^[5][G.S. 159-28\(e\)](#)



Disbursements

“When a bill, invoice, or other claim against a local government or public authority is presented, the finance officer shall either approve or disapprove the necessary disbursement.”^[6]

- Disbursements of local government funds are governed by separate but similar statutory requirements to those for preauditing obligations.
- The **finance officer** determines whether there are sufficient funds in the budget and the bank.
- With limited exceptions^[7], checks and claims must include a signed certificate attesting that the payment has been approved.^[8]

^[6][G.S. 159-28\(b\)](#) ^[7][G.S. 159-28\(f\)](#) ^[8][G.S. 159-28\(d1\)](#)



Automated Systems & Electronic Payments

- Units are allowed to use an **automated computer system** to fulfill the preaudit requirement, as long as the system meets certain technical requirements.^[9]
 - If using such a system, the finance officer must file an annual certification with the LGC within 30 days of the start of the fiscal year.
 - The certification can be filed digitally on the [LGC File Transfer Portal](#).
- Under North Carolina Administrative Code, certain **electronic payments** can be made exempt from certificate requirements for preaudits and disbursements.^{[10][11]}
 - [SLGFD Memo #2018-05](#) contains instructions related to this exemption.
 - Electronic payments **must still be preaudited**, even if a certificate is not required.

^[9][G.S. 159-28\(a3\)](#) ^[10][20 NCAC 03 .0409](#) ^[11][20 NCAC 03 .0410](#)



Setting Expectations

- When crafting policies/procedures and communicating with staff, governing boards should:
 - Set clear expectations that all preaudit and disbursement requirements will be followed.
 - Emphasize that these processes are required by law and carry penalties for noncompliance.
 - Support the finance officer when they must tell department heads that goods or services that are not budgeted cannot be purchased.





Resources

- [N.C. Local Government Finance Policy Manual, Chapter 12: Preaudits and Disbursements \(UNC School of Government\)](#)
- [Sample Preaudit and Disbursement Policies \(UNC School of Government\)](#)
- [Automated Systems and the Preaudit Requirement](#)
 - [Preaudit System Certification](#)
 - [Public list of verified certifications](#)
- [SLGFD memo on certificate exemptions for electronic payments with sample resolution for local governments](#)



Resources

- [UNC School of Government](#)
 - [NC Finance Connect](#)
 - [Finance Calendar of Duties](#)
 - [NC Local Government Finance 101](#)
- [NC League of Municipalities](#)
- [North Carolina Association of County Commissioners](#)
- [Government Finance Officers Association - Best Practices & Resources](#)



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Quiz: Module 4

1. When must the preaudit function be performed?
2. What happens to a contract or purchase order if a unit fails to perform the preaudit?
3. What can the preaudit process help a local government avoid?

