

**CITY OF KINSTON
NORTH CAROLINA**

COMPLIANCE LETTERS

FOR THE YEAR ENDED JUNE 30, 2011

**MARTIN ♦ STARNES
& ASSOCIATES, CPAs, P.A.**

"A Professional Association of Certified Public Accountants and Management Consultants"

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CITY OF KINSTON, NORTH CAROLINA

Compliance Letters For the Year Ended June 30, 2011

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Report On Internal Control Over Financial Reporting And On Compliance And Other Matters Based On An Audit Of Financial Statements Performed In Accordance With *Government Auditing Standards*

To the Honorable Mayor and
Members of the City Council
City of Kinston, North Carolina

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Kinston, North Carolina, as of and for the year ended June 30, 2011, which collectively comprise the City of Kinston's basic financial statements, and have issued our report thereon dated October 19, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the City of Kinston is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the City of Kinston's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City of Kinston's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Kinston's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the City of Kinston's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency, 2011-01, described in the accompanying Schedule of Findings and Questioned Costs to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Kinston's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings Questioned Costs as item 2011-01.

The City of Kinston's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the City's response and, accordingly, we express no opinion on the response.

We also noted certain matters that we reported to management of the City of Kinston in a separate letter dated October 19, 2011.

This report is intended for the information and use of management, others within the organization, members of the City Council, federal and State awarding agencies and pass-through entities, and is not intended to be, and should not be, used by anyone other than these specified parties.

Martin Starnes & Associates, CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
October 19, 2011

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Report On Compliance With Requirements That Could Have a Direct And Material Effect On Each Major Federal Program And Internal Control Over Compliance In Accordance With Applicable Sections of OMB Circular A-133 And The State Single Audit Implementation Act

To the Honorable Mayor and
Members of the City Council
City of Kinston, North Carolina

Compliance

We have audited the compliance of the City of Kinston with the types of compliance requirements described in applicable sections of OMB *Circular A-133 Compliance Supplement* and the *Audit Manual for Governmental Auditors in North Carolina*, issued by the Local Government Commission, that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011. The City of Kinston's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the City of Kinston's management. Our responsibility is to express an opinion on the City of Kinston's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and applicable sections of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, as described in the *Audit Manual for Governmental Auditors in North Carolina*, and the State Single Audit Implementation Act. Those standards, OMB Circular A-133, and the State Single Audit Implementation Act, require that we plan and perform the audit to obtain reasonable assurance about whether non-compliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Kinston's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City of Kinston's compliance with those requirements.

In our opinion, the City of Kinston complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011.

Internal Control Over Compliance

Management of the City of Kinston is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City of Kinston's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with applicable sections of OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City of Kinston's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, non-compliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material non-compliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Schedule of Expenditures of Federal and State Awards

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Kinston, North Carolina, as of and for the year ended June 30, 2011, which collectively comprise the City of Kinston, North Carolina's basic financial statements, and have issued our report thereon dated October 19, 2011 which contained an unqualified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the financial statements that collectively comprise the City of Kinston, North Carolina's basic financial statements. The accompanying Schedule of Expenditures of Federal and State Awards is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and the State Single Audit Implementation Act and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain other procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditure of federal and State awards is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended for the information and use of management, others within the organization, members of the City Council, federal and State awarding agencies and pass-through entities, and is not intended to be, and should not be, used by anyone other than these specified parties.

Martin Starnes & Associates, CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
October 19, 2011

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Report On Compliance With Requirements That Could Have a Direct And Material Effect On Each Major State Program And Internal Control Over Compliance In Accordance With Applicable Sections of OMB Circular A-133 And The State Single Audit Implementation Act

To the Honorable Mayor and
Members of the City Council
City of Kinston, North Carolina

Compliance

We have audited the compliance of the City of Kinston with the types of compliance requirements described in applicable sections of OMB *Circular A-133 Compliance Supplement* and the *Audit Manual for Governmental Auditors in North Carolina*, issued by the Local Government Commission, that could have a direct and material effect on each of its major State programs for the year ended June 30, 2011. The City of Kinston's major State programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major State programs is the responsibility of the City of Kinston's management. Our responsibility is to express an opinion on the City of Kinston's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and applicable sections of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, as described in the *Audit Manual for Governmental Auditors in North Carolina*, and the State Single Audit Implementation Act. Those standards, OMB Circular A-133, and the State Single Audit Implementation Act, require that we plan and perform the audit to obtain reasonable assurance about whether non-compliance with the types of compliance requirements referred to above that could have a direct and material effect on a major State program occurred. An audit includes examining, on a test basis, evidence about the City of Kinston's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City of Kinston's compliance with those requirements.

In our opinion, the City of Kinston complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major State programs for the year ended June 30, 2011.

Internal Control Over Compliance

Management of the City of Kinston is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to State programs. In planning and performing our audit, we considered the City of Kinston's internal control over compliance with the requirements that could have a direct and material effect on a major State program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with applicable sections of OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City of Kinston's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, non-compliance with a type of compliance requirement of a State program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material non-compliance with a type of compliance requirement of a State program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Schedule of Expenditures of Federal and State Awards

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Kinston, North Carolina, as of and for the year ended June 30, 2011, which collectively comprise the City of Kinston, North Carolina's basic financial statements, and have issued our report thereon dated October 19, 2011 which contained an unqualified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the financial statements that collectively comprise the City of Kinston, North Carolina's basic financial statements. The accompanying Schedule of Expenditures of Federal and State Awards is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and the State Single Audit Implementation Act and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain other procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditure of federal and State awards is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended for the information and use of management, others within the organization, members of the City Council, federal and State awarding agencies and pass-through entities, and is not intended to be, and should not be, used by anyone other than these specified parties.

Martin Starnes & Associates, CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
October 19, 2011

CITY OF KINSTON, NORTH CAROLINA

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2011**

1. Summary of Auditors' Results

Financial Statements:

Type of auditors' report issued Unqualified

Internal control over financial reporting:

- Material weakness(es) identified Yes
- Significant deficiency identified that are not considered to be material weaknesses No

Non-compliance material to financial statements noted Yes

Federal Awards:

Internal control over major federal programs:

- Material weakness(es) identified No
- Significant deficiency identified that are not considered to be material weaknesses No

Type of auditors' report issued on compliance for major State programs Unqualified

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A -133

Identification of major federal programs:

<u>CFDA #</u>	<u>Program Name</u>
10.780	USDA Rural Development Community Facilities Loans and Grants
10.780	USDA Rural Development Community Facilities Loans and Grants-ARRA
Dollar threshold used to distinguish between Type A and Type B Programs	\$300,000
Auditee qualified as low-risk auditee?	No

CITY OF KINSTON, NORTH CAROLINA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2011

State Awards:

Internal control over major State programs:

- Material weakness(es) identified No
- Significant deficiency identified that are not considered to be material weaknesses No

Type of auditors' report issued on compliance for major State programs

Unqualified

Any audit findings disclosed that are required to be reported in accordance with the State Single Audit Implementation Act

No

Identification of major State programs:

Program Name

Powell Bill

Clean Water Management Trust Fund – College Street Sewer Rehabilitation

Clean Water Management Trust Fund – Flood Buy-Out II Project

Clean Water Management Trust Fund – Battlefield Parkway/Soccer Complex

DOT –Martin Luther King Jr. Blvd Enhancement Golden LEAF grant

DOT - Heritage Street Improvements Golden LEAF grant

CITY OF KINSTON, NORTH CAROLINA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2011

2. Findings Related to the Audit of the Financial Statements

Finding 2011-01 Deficit Fund Equity

Criteria: North Carolina General Statutes preclude units from having funds that operate in a deficit.

Condition: In the current year, there were violations of the General Statutes regarding deficit fund equity in the Warehouse and the Fleet Maintenance Internal Service Funds.

Effect: The City was in violation of North Carolina General Statutes.

Cause: The City adopted a balance budget however revenues were insufficient to cover the cost of operations

Recommendation: The City should reevaluate the cost of providing services and adjust charges to insure that revenues cover all related cost.

Contact Person: Catherine Gwynn, Interim Finance Director

Views of Responsible Officials and Planned Corrective Actions: The City will re-evaluate the charges for services and the cost of providing services for the Warehouse and Fleet Maintenance Funds.

3. Findings and Questioned Costs Related to the Audit of State Awards

None

CITY OF KINSTON, NORTH CAROLINA

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2010**

None

CITY OF KINSTON, NORTH CAROLINA

**SCHEDULE OF EXPENDITURES OF FEDERAL AND STATE AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	State Pass-Through Grantor's Number	Federal Direct and Pass-Through Expenditures	State Expenditures
Federal Grants:				
U.S. Department of Energy				
Recovery Act Energy Efficiency and Conservation Block Grant - ARRA	81.128		\$ 4,003	\$ -
US Department of Justice				
2009 Ballistic Vest Grant	16.607		2,584	-
2010 Ballistic Vest Grant	16.607		7,725	-
2009 Justice Assistance Grant	16.738		144	-
2010 Justice Assistance Grant	16.738		27,501	-
2009 Justice Assistance Grant - ARRA	16.738		24,790	-
Community Oriented Policing Services - ARRA	16.710		55,470	-
Total US Department of Justice			<u>118,214</u>	<u>-</u>
USDA Rural Development				
Community Facilities Loans and Grants	10.780		988,899	-
Community Facilities Loans and Grants -ARRA	10.780		<u>2,337,500</u>	<u>-</u>
Total USDA Rural Development			<u>3,326,399</u>	<u>-</u>
State Grants:				
NC Department of Transportation				
Non-state System Street Aid Allocation (Powell Bill)		DOT-4	-	616,703
Martin Luther King Jr. Blvd Enhancement Golden LEAF grant			-	271,522
Spirit Aerosystems Rail Spur Project			-	97,609
Heritage Street Improvements Golden LEAF grant			-	220,957
Total NC Department of Transportation			-	<u>1,206,791</u>
NC Department of Environment and Natural Resources				
Clean Water Management Trust Fund -College Street Sewer Rehabilitation			-	332,774
Clean Water Management Trust Fund -Flood Buy-Out II Project			-	34,673
Clean Water Management Trust Fund -Battlefield Parkway/Soccer Complex				15,639
Rural Development Center Grant-Spirit AeroSystems Utilities			-	181,594
Rural Development Center Grant-Sanderson Farms Utilities			-	317,031
Rural Development Center Grant-Briery Run Sewer Phase III			-	71,913
Rural Development Center Grant-Pollock Street Sewer Project			-	313,684
Total NC Department of Environment and Natural Resources			-	<u>1,267,308</u>
NC Department of Commerce				
Division of Commerce Finance Center:				
Energy Efficiency Improvements grant			-	8,734
Industrial Development Fund-Lenox China Generator Project			-	791
Total NC Department of Commerce			-	<u>9,525</u>

CITY OF KINSTON, NORTH CAROLINA

**SCHEDULE OF EXPENDITURES OF FEDERAL AND STATE AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011**

Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	State Pass-Through Grantor's Number	Federal Direct and Pass-Through Expenditures	State Expenditures
NC Department of Crime Control and Public Safety				
Governor's Crime Commission			-	51,703
Gang Awareness, Training and Education Expansion			-	1,501
Total NC Department of Crime Control and Public Safety			-	53,204
Total federal expenditures			<u>\$ 3,448,616</u>	
Total State expenditures				<u>\$ 2,536,828</u>

Note 1. Basis of Presentation

The accompanying schedule of expenditures of federal and State awards includes the federal and State grant activity of City of Kinston, North Carolina and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* . Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Note 2. Loans Outstanding

City of Kinston had the following loan balances outstanding at June 30, 2011. These loan balances outstanding are also included in the federal expenditures presented in the schedule.

USDA Rural Development:	CFDA Number	Amount Outstanding
Community Facilities Loans and Grants	10.780	860,000
Community Facilities Loans and Grants -ARRA	10.780	2,337,500

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