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NORTH CAROLINA  
**DEPARTMENT OF STATE TREASURER**  
STATE AND LOCAL GOVERNMENT FINANCE DIVISION  
AND THE LOCAL GOVERNMENT COMMISSION

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**Memorandum #2010-14**

**TO: Local Government Finance Officials and Their Independent Auditors**

**FROM: Sharon Edmundson, Director, Fiscal Management Section**

**SUBJECT: Audit and Reporting Tips for 2009**

**DATE: September 16, 2009**

Based on our reviews of the 2008 audits and questions that are directed to our staff, the following are areas that we believe local government auditors and finance officials should review and which may impact the audit and preparation of financial statements for the fiscal year ended June 30, 2009.

**Changes and Enhancements to Financial Statements**

**Specific Data Gathered for Financial Indicators Website Project**

Most of you are aware that we are working on a financial dashboard project with the School of Government. Once live, this dashboard will allow cities and counties to benchmark against up to five other cities or counties of their choosing, using approximately 20 different financial indicators. To make this project work we are pulling additional data from the audited financial statements and may need your assistance in obtaining some of that data. For example, the note disclosures for capital asset activity and for changes in long-term liabilities under GASB are allowed to be grouped by Activity Group. In order to gather specific data for a Water, Sewer, or Electric Fund, we will be looking for that information to be separated by individual activity either on the statements or in the notes. Most units already provide this level of detail so we don't believe this will require wholesale changes in the way that financial reports are prepared. We also will be looking for the dollar figure for cities and counties' legal debt margin. Again, most units put this figure either in the notes or the MD&A. Look for more information on this dashboard project in the Spring of 2010.

**Other Post-Employment Benefits (OPEB)**

We have elected to treat Carolina County, City of Dogwood, and Carolina County Board of Education as Phase II units for implementation of GASB Statements No. 43 and 45. Therefore, these statements now include note disclosures and statement revisions, as applicable, regarding the funding of OPEB. In the City of Dogwood, we assumed the City chose to continue pay-as-you-go funding for OPEB and have included the appropriate note disclosure for that scenario. Carolina County Board of Education (BOE) pays a monthly percentage of covered payroll into a multiple-employer cost-sharing plan administered

by the State. The BOE's note disclosure references the State CAFR. All LEAs must include this disclosure in their notes for 2009 unless the LEA is a Phase III unit. Those few units can early implement GASB 45 if they choose to do so, since all that is involved is the additional note disclosure. Please note: if your LEA offers additional OPEB, such as supplemental health or other insurance, these must be disclosed as well and are not covered by the standard State plan note. In Carolina County, we assumed partial funding of OPEB through the Department of State Treasurer's OPEB Trust Fund with updates to the note disclosure and pension trust funds. A sample of disclosures for a fully funded OPEB liability using the Department of State Treasurer's OPEB Trust is presented as an appendix to the County's statements.

### **Water and Sewer Fund's Repairs and Maintenance**

As our State as a whole continues to analyze and address the issue of aging infrastructure, we have determined that we are not currently able to see specifically in the financial statements a unit's repairs and maintenance costs for the Water and/or Sewer operation. As a result, we are requesting that all local governments that operate a Water and/or Sewer Fund reflect the amount of repairs and maintenance expenditures separate from their other operating expenditures in their supplementary information. The Schedule of Revenues, Expenditures, and Changes in Fund Balance should reflect a separate line item for repairs and maintenance – this can be within each functional area or as one lump sum. Please note these amounts are not required to be separately stated in the full accrual Statement of Revenues, Expenditures, and Changes in Fund Net Assets. This presentation is not mandatory for 2009 but the information will be helpful to us and we request that you provide it if possible.

### **Debt Disclosures**

In order to facilitate our review of each local government's debt issuance practices, the financial statements should include the following information in their debt disclosures: original issue date, original issue amount, terms of issuance, purpose of debt, and information regarding **the provider of funds**, particularly if funds were loaned by the State Revolving Fund or the US Department of Agriculture.

LGC records of outstanding debt (Form 129) are available online. Go to <http://www.nctreasurer.com>, select "State and Local Government" on the menu bar across the top of the page, then "Fiscal and Debt Management Information", and finally "[Annual Debt Payment Notices with 6-30-08 Balances](#)". An Adobe document will appear and you can use the "Search" function in Adobe Reader to find a specific unit of government. Please be advised that these records may not include all debt issued by a unit of government and will be updated after the fiscal year ends.

### **Risk Management Disclosures**

In order to allow our staff to monitor local unit compliance with the General Statutes, and to confirm that units have adequate amounts of bonding coverage, we are asking local governments to separately disclose in their risk management note **the dollar amount of bonds** they carry on the finance officer position, the tax collector position, and the blanket bond held for individuals who handle or have in their

custody more than \$100 of the unit's funds at anytime or who has access to inventories of the unit. If the unit is not in compliance with G.S. 159-29 for Local Government Finance Officers and G.S. 115C-441(a) for School Finance Officers, a statutory violation note should be added. Please note that the bonding requirement for School Finance Officers increased to a \$50,000 minimum at July 1, 2008.

## **Statement Presentations**

### State 911 Board

Session law 2007-383 repealed Articles 1 and 2 of Chapter 62A and created Article 3 of Chapter 62A that created the State 911 Board. Under the new statutes, revenues received from the State 911 Board are restricted intergovernmental revenues to be held in a Special Revenue Fund called the Emergency Telephone System Fund. Effective January 1, 2008, unspent local 911 wireline fees held by local governments should have been transferred to their General Funds for unrestricted usage. Memoranda #1105, 1091 and 1096 provide more information. In the 2007-2008 Illustrated Financial Statements, the City of Dogwood reflected a transfer of its unspent local 911 revenues into the General Fund. Going forward, it is assumed that only the Article 3 revenue of Chapter 62A is accounted for in the City's Emergency Telephone System Fund.

### Medicaid Hold Harmless

As discussed in Memoranda #1105 and 1091, the State is moving towards absorbing 100% of non-federal Medicaid services expense on behalf of the counties. In return, cities and counties have forgone 1/4 cent of Article 44 sales tax revenue starting on October 1, 2008, with the final 1/4 cent going to the State as of October 1, 2009. Counties also may be entitled to a Medicare Hold Harmless payment to be accounted for with the Local Option Sales Tax revenue in the General Fund. The NCACC's website provides additional helpful information at <http://www.ncacc.org>. For units receiving hold harmless funds, the August payment of those funds is the "settle up" payment for the previous fiscal year. It is not subject to appropriation by the General Assembly and therefore should be accrued in the financial statements. Carolina County Illustrated Financial Statements have been updated to reflect the reduced revenues and expenditures.

## **Other Issues of Interest that May Affect Audited Financial Statements**

### Additional Schedules Requested by USDA

Local governments that have outstanding long-term USDA revenue bonds secured by a specific revenue source will need to ensure that USDA can see the results of operations and the material assets, liabilities, and equity attributable to that revenue source in the financial report. This can present a challenge for units that operate a water and sewer system but have pledged only the water revenue or only the sewer revenue for debt repayment. If this is the case, USDA is requesting that the report include a detailed separate reporting for each function, although the functions may still be reported in the same fund. In the financial statements for the City of Dogwood, we have included in the City's supplementary information three new Schedules - Water and Sewer Fund's Schedule of Net Assets by Function, Schedule of Activities by Function, and Schedule of Cash Flows by Function. Again, this information is only necessary if you have a combined operation but only one revenue stream pledged. Our illustration in

Dogwood is only an example; there are various ways you could present this information if need be. This information is requested for 2009 but will be mandatory for 2010.

#### Pledged Revenues

GASB Statement 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, provides guidance on determining if a transaction is a sale or a collateralized borrowing; states that intra-entity transfers of assets should be reported at carrying value of the transferor; and provides guidance on the required disclosures for all debt that is backed by a specific revenue source when that revenue source is not the entity's predominate source of revenue. The City of Dogwood has issued revenue bonds for the Water and Sewer Fund with the understanding that the debt payments will be paid from water and sewer revenues. The revenue bond note disclosure has been expanded with the additional disclosure required.

#### Payroll Deficiencies

As we have discussed in several memoranda, timely and accurate preparation and recording of payroll expenditures and liabilities continues to be a challenge for some of our local units of government. Units of government with material penalty and interest liabilities or expenditures relating to payroll should expect to see a significant deficiency or material weakness in their internal control reports. Units of government that are not in compliance with IRS regulations regarding the reporting requirements for various personnel (1099 in lieu of W-2 reporting) should expect to see findings in their internal control reports and their stewardship and compliance note disclosures. Please see memorandums #1079, 1083, 1084, and 1089 for a more complete discussion of these issues.

#### Stewardship and Compliance Note Disclosures

In the course of our reviews of local government audits, we continue to see reports that contain findings in the internal control reports that are not disclosed in the notes and vice versa. Statement preparers and auditors should take care that any statutory violations that are noted in the stewardship and compliance note are consistent with the findings in the internal control reports. Conversely, findings in the internal control reports that involve statutory violations should be noted in the stewardship and compliance note disclosures.

On a related topic, we continue to see stewardship violations on the line-item level when the budget note states that the budget is adopted at the department or function level. Legal budgetary violations only exist at the level at which budgetary control was established.

#### Fund Balance Appropriated

We continue to note instances in which a unit budgeted appropriated fund balance in excess of the statutory limitation in both governmental *and enterprise funds*. According to G.S. 159-13(b)(16), appropriated fund balance in a fund shall not exceed the sum of cash and investments minus the sum of liabilities, encumbrances, and deferred revenues arising from cash receipts, as those figures stand at the close of the fiscal year preceding the budget year. Over-appropriation of fund balance is a statutory violation.

**Unit Letters Issued on Reports as Submitted**

Once we receive a complete set of audited financial statements, we analyze the financial condition and compliance with GAAP, North Carolina Statutes, and grant requirements and determine if we have concerns that need to be communicated with the elected governing body. Our analysis and subsequent letter, if issued, is based on the statements as they are presented to us. If our letter is based on information that is subsequently determined to be presented incorrectly, we will not retract our unit letter, although we may issue a second letter.

**LGC Review of Drafts of Audited Financial Statements**

Due to resource limitations, we will review only drafts of audited financial statements that are camera ready Comprehensive Annual Financial Reports, or drafts of audited financial statements for governments that have a scheduled debt sale requiring the preparation of an official statement. A draft should be reviewed by the unit's management prior to submitting it to our office.

**Submission of Audit Reports of Municipalities to the State 911 Board**

As a reminder, municipalities that have participating PSAPs (public safety answering points) should submit an additional copy of their annual audit report to the LGC. We will forward the extra copy to the State 911 Board upon review and approval of the audit. Audit submission requirements for other government types - counties, schools, public authorities, etc., have not changed. Please see Memorandum #1091 for a more complete discussion of this issue.

**Retirement Contribution Rates for TSERS, Firemen's and Rescue Squad Workers**

Below are the retirement funding rates for the fiscal year ended June 30, 2009, for the above mentioned retirement systems. Governments with employees that are members of these retirement systems will need this information for their June 30, 2009, pension note disclosures.

TSERS (Teachers and State Employees Retirement System)

Retirement contribution:	3.36%
Retiree Health Reserve	4.10%
Death Benefit	0.16%
Disability	<u>0.52%</u>
Total	8.14%

Firemen and Rescue Squad Workers Retirement System

Firemen's Retirement	\$272.08
Rescue Squad Workers' Retirement	\$353.16

GASB Statement 40 Note Disclosure Information

STIF	Weighted average maturity of 1.8 years
NCCMT	Term portfolio duration of 0.8 year and rating of AAAM

If you have any questions, please contact members of our staff at 919-807-2381.