

CITY OF SALEM, MASSACHUSETTS

REPORTS ON FEDERAL AWARD PROGRAMS

FISCAL YEAR ENDED JUNE 30, 2005

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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL
CONTROL OVER FINANCIAL REPORTING 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 Salem, Massachusetts

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Salem, Massachusetts, as of and for the fiscal year ended June 30, 2005, which collectively comprise the City of Salem, Massachusetts' basic financial statements and have issued our report thereon dated October 6, 2005. 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.

Compliance

As part of obtaining reasonable assurance about whether the City of Salem, Massachusetts' basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of basic 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 no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Salem, Massachusetts' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have communicated to the management of the City of Salem, Massachusetts, in a separate letter dated October 6, 2005.

This report is intended solely for the information and use of management of the City of Salem, Massachusetts, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Powers + Sullivan". The signature is written in a cursive, flowing style.

October 6, 2005



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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

To the Honorable Mayor
and Members of the City Council
City of Salem, Massachusetts

Compliance

We have audited the compliance of the City of Salem, Massachusetts, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the fiscal year ended June 30, 2005. The City of Salem's major federal programs are identified in the summary of auditors' 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 Salem's management. Our responsibility is to express an opinion on the City of Salem'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 OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance 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 Salem'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 on the City of Salem's compliance with those requirements.

In our opinion, the City of Salem, Massachusetts, complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the fiscal year ended June 30, 2005. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item 05-1.

Internal Control Over Compliance

The management of the City of Salem, Massachusetts, is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City of Salem's internal control over compliance with 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 OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management of the City of Salem, Massachusetts, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, reading "Bowers + Sullivan". The signature is written in a cursive, flowing style.

October 6, 2005



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INDEPENDENT AUDITORS' REPORT ON SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

To the Honorable Mayor
and Members of the City Council
City of Salem, Massachusetts

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Salem, Massachusetts, as of and for the fiscal year ended June 30, 2005, and have issued our report thereon dated October 6, 2005. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City of Salem, Massachusetts' basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of management of the City of Salem, Massachusetts, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

October 6, 2005

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2005

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF AGRICULTURE:		
<u>Passed through State Department of Education:</u>		
Food Distribution	10.550	\$ 134,729
School Breakfast Program	10.553	186,959
National School Lunch Program	10.555	<u>658,716</u>
TOTAL AGRICULTURE		<u>980,404</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:		
<u>Direct Program:</u>		
Community Development Block Grant	14.218	1,609,171
CDBG - Brownfields Economic Devel Initiative	14.246	15,680
<u>Passed through North Shore Home Consortium:</u>		
Home Investment Partnerships Program	14.239	<u>295,158</u>
TOTAL HOUSING		<u>1,920,009</u>
U.S. DEPARTMENT OF JUSTICE:		
<u>Direct Program:</u>		
Grants to Encourage Arrest Policies	16.590	64,671
Law Enforcement Trust Fund	16.592	28,401
Local Law Enforcement Block Grant	16.592	<u>8,723</u>
TOTAL JUSTICE		<u>101,795</u>
U.S. DEPARTMENT OF LABOR:		
<u>Passed through State Commonwealth Corporation:</u>		
Pathways to Success by 21	17.225	215
Best Initiative - Older Youth	17.267	39,792
<u>Passed through State Division of Career Services:</u>		
Work Incentive Disability - Wagner Peyser	17.207	29,642
Unemployment Insurance	17.225	8,734
Workforce Investment Act - Adult Program	17.258	374,700
Workforce Investment Act - Youth Activities	17.259	693,004
Workforce Investment Act - Dislocated Worker	17.260	594,144
Workforce Investment Act - Section 173E	17.260	103,043
Workforce Investment Act - Career Center Seminars	17.260	8,071
National Emergency Grant - Citicorp	17.260	596,288
National Emergency Grant - Airlines	17.260	66,584
Workforce Investment Act - Navigator	17.266	57,699
<u>Passed through Community Transportation Association of America:</u>		
Transportation Access Project	17.261	<u>53,663</u>
TOTAL LABOR		<u>2,625,579</u>
U.S. ENVIRONMENTAL PROTECTION AGENCY:		
<u>Direct Program:</u>		
Brownfield Pilot Project	66.811	<u>131,999</u>

(continued)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2005

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF EDUCATION:		
<u>Direct Program:</u>		
Teaching American History	84.215X	196,701
Smaller Learning Communities	84.215L	158,086
Bilingual Education: Comprehensive School Grants	84.290	515
Foreign Language Assistance	84.293	59,113
Foreign Language Incentive Program	84.294	4,463
<u>Passed through State Department of Education:</u>		
Adult Education - State Grant Program	84.002	11,038
Title I Distribution	84.010	1,190,731
SPED 94 - 142 Allocation	84.027	1,054,163
SPED Professional Development	84.027	18,694
SPED - Corrective Action	84.027	11,000
SPED - Mental Health Support	84.027	1,027
SPED - Specialized Training	84.027	3,365
SPED - Program Improvement	84.027	12,868
Vocational Education	84.048	32,151
Title V	84.151	25,871
Emergency Immigration Act	84.162	208
Eisenhower Professional Development	84.164	1,497
SPED - Early Childhood Allocation	84.173	56,618
Drug Free Schools	84.186	24,429
School Support Program	84.218	12,818
Goals 2000	84.276	123
21st CCLC	84.287	130,580
Enhanced Education Through Technology	84.318	78,554
Project Focus	84.323	5,000
Class Size Reduction	84.340	344
Reading First	84.357	296,053
English Language Acquisition Grant	84.365	84,357
Teacher Quality	84.367	283,618
<u>Passed through Town of Rockport:</u>		
Enhanced Education Through Technology	84.318	17,492
TOTAL EDUCATION		<u>3,771,477</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:		
<u>Passed through North Shore Elder Services, Inc:</u>		
Title IIIB - Special Programs for the Aging	93.044	20,532
Title IIIC - Nutrition Program for the Aging	93.045	62,238
TOTAL HEALTH & HUMAN SERVICES		<u>82,770</u>
CORPORATION FOR NATIONAL AND COMMUNITY SERVICE:		
<u>Passed through State Department of Education:</u>		
Learn and Serve School Based	94.004	5,552
U.S. DEPARTMENT OF HOMELAND SECURITY:		
<u>Direct Program:</u>		
Assistance to Firefighters	83.554	10,010
<u>Passed through Mass Emergency Management Agency:</u>		
Snowstorm Assistance	97.036	166,442
State & Local All Hazards	97.051	10,179
TOTAL HOMELAND SECURITY		<u>186,631</u>
TOTAL		<u>\$ 9,806,216</u>

(concluded)

See notes to schedule of expenditures of federal awards.

Note 1 - Definition of Reporting Entity

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal financial assistance programs of the City of Salem, Massachusetts. All federal financial assistance received directly from federal agencies as well as federal financial assistance passed through other governmental agencies is included on the schedule.

Note 2 - Significant Accounting Policies

The accounting and reporting policies of the City of Salem, Massachusetts are set forth below:

- (a) Basis of Presentation - The accompanying Schedule of Expenditures of Federal Awards is presented on the modified accrual basis of accounting.
- (b) School Lunch Program - Program expenditures represent federal reimbursement for meals provided during the year.

A. Summary of Auditors' Results

1. The auditors' report expresses an unqualified opinion on the basic financial statements of the City of Salem, Massachusetts.
2. No reportable conditions relating to the audit of the financial statements are reported in the Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*.
3. No instances of noncompliance material to the financial statements of the City of Salem, Massachusetts, were disclosed during the audit.
4. No reportable conditions relating to the audit of the major federal award programs is reported in the Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133.
5. The auditors' report on compliance for the major federal award programs for the City of Salem, Massachusetts, expresses an unqualified opinion.
6. There was one audit finding related to federal award programs.
7. The programs tested as major grants include:

<u>Program Title</u>	<u>CFDA Number</u>
Community Development Block Grant	14.218
Workforce Investment Act – Adult Program	17.258
Workforce Investment Act – Youth Activities	17.259
Workforce Investment Act – Dislocated Worker	17.260
Workforce Investment Act – Section 173E	17.260
Workforce Investment Act – Career Center Seminars	17.260
National Emergency Grant – Airlines	17.260
National Emergency Grant – Citicorp	17.260
Teaching American History	84.215X
Smaller Learning Communities	84.215L

8. The threshold for distinguishing Types A and B programs was \$300,000.
9. The City of Salem, Massachusetts, was determined to be a low-risk auditee.

B. Findings-Financial Statements Audit

None.

C. Findings and Questioned Costs-Major Federal Award Programs Audit**U.S. DEPARTMENT OF EDUCATION****05-1**

Teaching American History Grant – CFDA No. 84.215X
Smaller Learning Communities Grant – CFDA No. 84.215L

Condition and Criteria: The City was not in compliance with Federal Regulations for Cash Management, which requires grantees to follow procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and the disbursement of the funds. Additionally, the City was not in compliance with Federal Regulations requiring interest earned on advances by local government grantees to be submitted at least quarterly to the federal agency.

Effect: On the Teaching American History Grant, the City requested and received the entire grant of \$877,472 in the first year of a three year grant program. The cash was pooled with other City funds in interest-bearing bank accounts. Expenditures on the program totaled \$148,853 in year 1 (fiscal year 2004), and \$196,701 in year 2 (fiscal year 2005). Consequently, the City accumulated approximately \$25,500 in interest revenue which it did not report or remit to the federal awarding agency as required.

On the Smaller Learning Communities Grant, the City requested and received \$85,000 in year 1 (fiscal year 2004), and \$175,000 in year 2 (fiscal year 2005), of a 3 year grant. The cash was pooled with other City funds in interest-bearing bank accounts. Expenditures on the program totaled \$44,233 in year 1 and \$158,087 in year 2. Consequently, the City accumulated approximately \$2,000 in interest revenue which it did not report or remit to the federal awarding agency as required

Cause: The City does not have procedures in place to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement of the funds. Specifically, when requesting a draw of funds from the U.S. Treasury, the City is required to certify that the funds will be expended within 3 days of receipt. This certification was required for the transfer to take place. The funds were then not expended within 3 days and were not returned to the grantor.

Questioned Costs: Approximately \$27,500

Auditor's Recommendation: We recommend the City return the unreported interest earnings to the awarding federal agencies. We also recommend the City adopt procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and the use of the funds for program purposes.