

CITY OF SALEM, MASSACHUSETTS

REPORTS ON FEDERAL AWARD PROGRAMS

FISCAL YEAR ENDED JUNE 30, 2008

CITY OF SALEM, MASSACHUSETTS
REPORTS ON FEDERAL AWARD PROGRAMS
FISCAL YEAR ENDED JUNE 30, 2008

TABLE OF CONTENTS

Page

| | |
|---|---|
| Report on internal control over financial reporting and on compliance and other matters based on an audit of financial statements performed in accordance with <i>Governmental Auditing Standards</i> | 1 |
| Report on compliance with requirements applicable to each major program and internal control over compliance in accordance with OMB Circular A-133 | 3 |
| Schedule of Expenditures of Federal Awards | 5 |
| Notes to schedule of expenditures of federal awards..... | 7 |
| Schedule of findings and questioned costs | 8 |



100 Quannapowitt Parkway
Suite 101
Wakefield, MA 01880
T. 781-914-1700
F. 781-914-1701
www.powersandsullivan.com

**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 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, 2008, which collectively comprise the City of Salem, Massachusetts' basic financial statements and have issued our report thereon dated December 9, 2008. 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

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 opinions on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City of Salem, Massachusetts' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Salem, Massachusetts' internal control over financial reporting.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City of Salem, Massachusetts' ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City of Salem, Massachusetts' financial statement that is more than inconsequential will not be prevented or detected by the City of Salem, Massachusetts' internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City of Salem, Massachusetts' internal control.

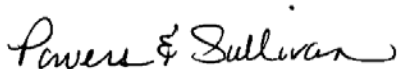
Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses, as defined above. We did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

Compliance and Other Matters

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 grant agreements, 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 instances of noncompliance or other matters that are required to be reported under *Governmental Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as finding 2008-1.

We also noted certain other matters that we reported to management of the City of Salem, Massachusetts in a separate letter dated December 9, 2008.

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 cursive script that reads "Powers & Sullivan".

December 9, 2008



100 Quannapowitt Parkway
Suite 101
Wakefield, MA 01880
T. 781-914-1700
F. 781-914-1701
www.powersandsullivan.com

**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, 2008. 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.

As described in item 2008-2 in the accompanying schedule of findings and questioned costs, the City of Salem, Massachusetts did not perform the sampling and verification of free and reduced price applications for the National School Lunch Program as required by federal regulations. Compliance with such requirements is necessary, in our opinion, for the City of Salem, Massachusetts to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, 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, 2008.

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, 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 Salem's internal control over compliance.

A *control deficiency* in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

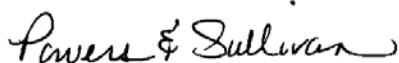
A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

Schedule of Expenditures of Federal 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 City of Salem, Massachusetts, as of and for the fiscal year ended June 30, 2008, and have issued our report thereon dated December 9, 2008. Our audit was performed for the purpose of forming our 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.



December 9, 2008

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

| <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 Elementary and Secondary Education:</u> | | |
| Food Donation | 10.550 | \$ 123,725 |
| School Breakfast Program | 10.553 | 176,218 |
| National School Lunch Program | 10.555 | <u>684,350</u> |
| TOTAL AGRICULTURE | | <u>984,293</u> |
| U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT: | | |
| <u>Direct Program:</u> | | |
| Community Development Block Grant/Entitlement Grants | 14.218 | 1,146,018 |
| Community Development Block Grants/Browning Economic Development Initiative | 14.246 | 1,340 |
| <u>Passed through North Shore Home Consortium:</u> | | |
| HOME Investment Partnerships Program | 14.239 | <u>197,702</u> |
| TOTAL HOUSING | | <u>1,345,060</u> |
| U.S. DEPARTMENT OF THE INTERIOR: | | |
| <u>Passed through State Executive Office of Environmental Affairs:</u> | | |
| Clean Vessel Act | 15.616 | <u>9,428</u> |
| U.S. DEPARTMENT OF JUSTICE: | | |
| <u>Direct Program:</u> | | |
| Grants to Encourage Arrest Policies and Enforcement of Protection Orders | 16.590 | 33,607 |
| Local Law Enforcement Trust Funds Program | 16.592 | 8,672 |
| Bulletproof Vest Partnership Program | 16.607 | 42,540 |
| <u>Passed through Executive Office of Public Safety:</u> | | |
| Public Safety Partnership and Community Policing Grants | 16.710 | 90,114 |
| Gang Resistance Education and Training | 16.737 | 79 |
| Narcotics Assistance Program | 16.738 | <u>48,627</u> |
| TOTAL JUSTICE | | <u>223,639</u> |
| U.S. DEPARTMENT OF LABOR: | | |
| <u>Passed through State Commonwealth Corporation:</u> | | |
| Unemployment Insurance | 17.225 | 11,275 |
| WIA Incentive Grants Section 503 Grants to States | 17.267 | 39,516 |
| <u>Passed through State Division of Career Services:</u> | | |
| Employment Service | 17.207 | 76,535 |
| Workforce Investment Act - Adult Program | 17.258 | 702,307 |
| Workforce Investment Act - Youth Activities | 17.259 | 856,015 |
| Workforce Investment Act - Dislocated Worker | 17.260 | 810,239 |
| Work Incentive Grant | 17.266 | 55,796 |
| <u>Passed through Division of Career Services - Workforce Development:</u> | | |
| Disabled Veterans' Outreach Program (DVOP) | 17.801 | <u>7,964</u> |
| TOTAL LABOR | | <u>2,559,647</u> |
| U.S. DEPARTMENT OF TRANSPORTATION: | | |
| <u>Passed through Executive Office of Public Safety:</u> | | |
| Public Transportation Research | 20.514 | 19,399 |
| National Highway Transportation Safety Administration Discretionary Safety Grants | 20.614 | <u>9,419</u> |
| TOTAL TRANSPORTATION | | <u>28,818</u> |

(continued)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

| <u>Federal Grantor/Program Title</u> | <u>Federal CFDA Number</u> | <u>Expenditures</u> |
|---|------------------------------------|---------------------|
| U.S. ENVIRONMENTAL PROTECTION AGENCY: | | |
| <u>Direct Program:</u> | | |
| Brownfield Pilots Cooperative Agreements | 66.811 | <u>57,295</u> |
| U.S. DEPARTMENT OF EDUCATION: | | |
| <u>Passed through State Department of Elementary and Secondary Education:</u> | | |
| Adult Education State Grant Program | 84.002 | 12,506 |
| Title I Grants to Local Educational Agencies | 84.010 | 781,822 |
| Special Education Grants to States | 84.027 | 1,112,494 |
| Vocational Education Basic Grants to States | 84.048 | 9,037 |
| Safe and Drug Free Schools and Communities State Grants | 84.186 | 14,760 |
| Twenty-First Century Community Learning Centers | 84.287 | 227,697 |
| State Grants for Innovative Programs | 84.298 | 8,419 |
| Education Technology State Grants | 84.318 | 4,496 |
| Reading First State Grants | 84.357 | 234,173 |
| English Language Acquisition Grants | 84.365 | 57,412 |
| Improving Teacher Quality State Grants | 84.367 | 290,894 |
| <u>Passed through State Department of Early Education and Care:</u> | | |
| Special Education Preschool Grants | 84.173 | <u>44,578</u> |
| TOTAL EDUCATION | | <u>2,798,288</u> |
| U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES: | | |
| <u>Passed through North Shore Elder Services, Inc.:</u> | | |
| Special Programs for the Aging Title III, Part B Grants for | | |
| Supportive Services and Senior Centers | 93.044 | 20,575 |
| Special Programs for the Aging Title III, Part C Nutrition Services | 93.045 | 54,830 |
| <u>Passed through Department of Transitional Assistance:</u> | | |
| Temporary Assistance for Needy Families | 93.558 | 20,967 |
| <u>Passed through Executive Office of Health and Human Services:</u> | | |
| National Bioterrorism Hospital Preparedness | 93.889 | 1,857 |
| Bioterrorism Training and Curriculum Development Program | 93.996 | <u>262,539</u> |
| TOTAL HEALTH & HUMAN SERVICES | | <u>360,768</u> |
| CORPORATION FOR NATIONAL AND COMMUNITY SERVICE: | | |
| <u>Passed through State Department of Elementary and Secondary Education:</u> | | |
| Learn and Serve America School and Community Based Programs | 94.004 | <u>3,247</u> |
| U.S. DEPARTMENT OF HOMELAND SECURITY: | | |
| <u>Direct Program:</u> | | |
| Assistance to Firefighters | 97.044 | 46,264 |
| <u>Passed through Mass Emergency Management Agency:</u> | | |
| State Domestic Preparedness Equipment Support Program | 97.004 | <u>26,698</u> |
| TOTAL HOMELAND SECURITY | | <u>72,962</u> |
| TOTAL | | <u>\$ 8,443,445</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) National School Lunch Program and School Breakfast Program - Program expenditures represent federal reimbursement for meals provided during the year.

NOTE 3 – Program Clusters

In accordance with Subpart A §_.105 of OMB Circular No. A-133, *Audits of States, Local Governments and Non Profit Organizations*, certain programs have been clustered in determining major programs. The following represents the clustered programs:

| <u>Name of Cluster/Program</u> | <u>CFDA Number</u> |
|---|------------------------|
| Child Nutrition Cluster | |
| School Breakfast Program | 10.553 |
| National School Lunch Program | 10.555 |
| Summer Food Serve Program for Children | 10.559 |
| CDBG - Entitlement and (HUD-Administered) | |
| Small Cities Cluster | |
| Community Development Block Grants/ Entitlement Grants | 14.218 |
| Community Development Block Grants/ Small Cities Program | 14.219 |
| WIA Cluster | |
| WIA Adult Program | 17.258 |
| WIA Youth Activities | 17.259 |
| WIA Dislocated Workers | 17.260 |
| Special Education Cluster | |
| Special Education Grants to States | 84.027 |
| Special Education Preschool Grants | 84.173 |

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 significant deficiencies relating to the audit of the financial statements are reported in the 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*.
3. One instance of noncompliance material to the financial statements of the City of Salem, Massachusetts, was disclosed during the audit, which is reported as finding 2008-1.
4. No significant deficiencies 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 a qualified 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> |
|---|------------------------|
| School Breakfast Program | 10.553 |
| National School Lunch Program | 10.555 |
| Community Development Block Grants/Entitlement Grants | 14.218 |
| Workforce Investment Act – Adult Program | 17.258 |
| Workforce Investment Act – Youth Activities | 17.259 |
| Workforce Investment Act – Dislocated Workers | 17.260 |
| Title 1 Grants to Local Educational Agencies | 84.010 |
| Special Education Grants to State | 84.027 |
| Special Education Preschool Grants | 84.173 |

8. The threshold for distinguishing Types A and B programs was \$300,000.
9. The City of Salem, Massachusetts, was not determined to be a low-risk auditee.

B. Findings and Questioned Costs-Financial Statements Audit**Finding 2008-1****Internal Control Over Procurement**

Condition and Criteria: The City entered into a contract with North Shore Medical Center to provide Special Education services for the contract period of July 1, 2008 through June 30, 2011. The contract did not follow any purchasing or bidding procedures, as required by the City's internal procurement policies. The contract included \$500,000 of administrative fees allocated over the three year contract. The administrative fees were determined to be a prior year balance owed to North Shore Medical Center.

Cause: The City does not have adequate procedures in place to ensure compliance with the City's purchasing policy in the procurement of special education contractual services or state finance laws.

Additionally, the City does not have procedures in place to ensure that goods and services are paid for in the fiscal year they are purchased.

Effect: The City is not in compliance with their internal purchasing policy in the procurement of special education contractual services; nor state finance laws in which goods and services are required to be paid for in the fiscal year that they are purchased. The City must immediately address the outstanding amount owed to North Shore Medical Center which will impact the fiscal year 2010 budget. The contract to North Shore Medical Center is funded through the City's general education operating budget, and not directly with grant funds.

Questioned Costs: None

Auditors Recommendation: We recommend the City implement procedures to ensure compliance with the City's purchasing policy in the procurement of special education contractual services and state finance laws.

We also recommend that the City raise the outstanding balance owed to North Shore Medical Center for prior year services on the fiscal year 2010 tax recap.

C. Findings and Questioned Costs-Major Federal Award Programs Audit**Finding 2008-2****National School Lunch Program and School Breakfast Program – CFDA No. 10.555**

Condition and Criteria: The City did not perform the sampling and verification of free and reduced price applications as required by federal regulations. Consequently, the required changes to eligibility status based on documentation and other information obtained through the verification process could not be made.

By December 15th of each school year, the City is required to verify the current free and reduced price eligibility of households selected from a sample of applications that are approved for free and reduced price meals, unless they are otherwise exempt from the verification requirement. The verification sample may be done either via a random sample of the approved applications on file on October 31st,

or, by focused sampling, where the sample is selected from applications within a specified range of the income eligibility guidelines for free and reduced price meals or from applications that were approved based on categorical eligibility.

Cause: The City does not have procedures in place to ensure compliance with the grant requirements.

Effect: The City is not in compliance with the grant requirements, and, as a result, the City was unable to make any adjustments to the eligibility for free and reduced price meals that may have been identified had the verification procedures been conducted.

Questioned Costs: Unknown.

Auditors Recommendation: We recommend the City implement procedures to conduct and document the sampling and verification of free and reduced price applications as required by federal regulations for fiscal year 2009, by December 15, 2008.

D. Prior Audit Findings and Questioned Costs – Financial Statement Audit

Finding 2007-1

Material Weaknesses in Internal Control Over Financial Reporting

Status - Resolved

Finding 2007-2

Noncompliance with Certain Provisions of Laws, Regulations, Contracts and Grant Agreements

Status - Resolved

E. Prior Audit Findings and Questioned Costs – Major Federal Award Programs Audit

Finding 2007-3

Fund for the Improvement of Education – CFDA No. 84.215

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

Condition and Criteria: During fiscal year 2007, 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), \$196,701 in year 2 (fiscal year 2005), \$260,608 in year 3 (fiscal year 2006), and \$271,310 in year 4 (fiscal year 2007). The City has received an extension of time to spend the remaining grant funds which expires on September 30, 2007 (fiscal year 2008). Consequently, the City accumulated approximately \$32,500 in interest revenue, of which \$7,100 had not been reported or remitted 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), \$175,000 in year 2 (fiscal year 2005) and \$240,000 in year 3 (fiscal year 2006). The cash was pooled with other City funds in interest-bearing bank accounts. Expenditures on the program totaled \$44,233 in year 1, \$158,087 in year 2, \$240,711 in year 3, and \$56,970 in year 4 (fiscal year 2007). Consequently, the City accumulated approximately \$3,100 in interest revenue, of which, \$1,100 had not been reported or remitted to the federal awarding agency as required.

During fiscal year 2007, the City returned \$27,500 of the interest earned on both programs through fiscal year 2005 to the Massachusetts Department of Education. In September, 2007, the City returned \$6,600 of interest earned on both programs through fiscal year 2006 to the Massachusetts Department of Education, and in February, 2007, placed all remaining unspent funds in a non interest bearing bank account. In fiscal year 2009, the City returned \$1,600 of interest earned in fiscal year 2007.

Status - This matter is considered resolved. In September 2009, the City has returned the unreported interest earnings to the awarding federal agency. New procedures have been implemented to minimize the time elapsing between transfers of funds. Procedures include setting up account numbers before anticipated revenues and expenditures are incurred, forwarding copies of award letters and memos with the corresponding account numbers listed to the Treasurer and Finance Director's offices. It is the responsibility of the grant administrator to process requests for funds on a regular basis with reconciliations being done on a monthly and quarterly basis with copies and support forwarded to the Treasurer's and Finance Director's offices for review.

Finding 2007-4

Fund for the Improvement of Education – CFDA No. 84.215

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

Condition and Criteria: In fiscal year 2007, we tested \$276,294 in total grant expenditures recorded on the City's general ledger for the Teaching American History and Smaller Learning Communities Grants and found the following:

- \$7,129 of invoices charges to these grants was found to be ineligible. These expenses have been reported as part of the schedule of federal awards in fiscal year 2007.
- The last entry made to the ledger at the close of the Small Learning Communities Grant was a journal entry for \$30,159 that charged the grant for the exact amount of unspent funds and reduced general fund expenses. The new School Business Manager explained that the charge was for a portion of the salary of the housemaster of the freshman house. We were not satisfied that sufficient documentation was available to support this charge and we are questioning the charge. These expenses have been reported as part of the schedule of federal awards in fiscal year 2007.

- In December 2006, a journal entry was made that charged both grants \$4,000 for administration costs for a total of \$8,000. In January 2007, a journal entry was made that charged \$8,462 to the Smaller Learning Communities Grant for administration. In March 2007, a journal entry was made that charged \$20,000 to the Teaching American History Grant for administration cost. The School did not have a cost allocation plan to determine the costs. Per discussion with the grants administrator he agreed that the charges were based on which grants had funds remaining and that he spent very little time on these 2 grants. The entire \$36,462, which is over ½ of his annual salary, is a questioned cost. The City and School agreed that these charges should not have been charged and the amounts have been removed from the schedule of federal awards. However the final reports for these grants had not been amended and unspent grant funds had not been returned to the granting agency.
- In fiscal year 2007 the last entry made on the ledger at the close of the Teaching American History Grant was a journal entry that charged this grant for \$44,325 which was the exact amount of unspent grant funds and reduced general fund expenses. There was no supporting documentation for this charge and we have determined that the entry is without merit. The City and School agreed that this entry was not proper and the amount was not included in the fiscal year 2007 schedule of expenditures of federal awards.

Effect: The City and School had a material weakness in internal control over financial reporting and compliance with major federal awards in fiscal year 2007. A minimum of \$118,075 in ineligible costs were recorded as grant expenditures because of a lack of procedures to verify that all expenditures charged to the grant were for allowable purposes which increased the risk that additional ineligible expenditures will be recorded against the grant. Consequently, the City was not in compliance with the grant agreement in fiscal year 2007.

Status - This matter is considered resolved. The City has disputed \$30,159 of the Smaller Learning Communities Grant because this amount was paid to the freshman housemaster that was created by the grant and the amount is now being paid out of the school's operating budget. The City has also refunded checks in the amount of \$19,591 to the awarding agencies and implemented new procedures to ensure expenditures charged against grants are for allowable purposes.