



STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF DAVIDSON COUNTY PARTNERSHIP FOR CHILDREN

LEXINGTON, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2003

OFFICE OF THE STATE AUDITOR

RALPH CAMPBELL, JR.

STATE AUDITOR

FINANCIAL STATEMENT AUDIT REPORT OF
DAVIDSON COUNTY PARTNERSHIP FOR CHILDREN
LEXINGTON, NORTH CAROLINA
FOR THE YEAR ENDED JUNE 30, 2003

BOARD OF DIRECTORS

ROBERT LOPP, CHAIRMAN



Ralph Campbell, Jr.
State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Board of Directors, Davidson County Partnership for Children

This report presents the results of our financial statement audit of the Davidson County Partnership for Children (Davidson Partnership) for the year ended June 30, 2003. Our audit was made by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

The accounts and operations of the Davidson Partnership were subject to audit procedures as we considered necessary for us to report on the accompanying financial statements and supplementary information. The audit procedures were conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States.

The audit of the Davidson Partnership was made in conjunction with the Early Childhood Initiatives (Smart Start) program authorized by General Statutes 143B-168.10-.16. These statutes created The North Carolina Partnership for Children, Inc. and required the implementation of local demonstration projects (local partnerships). The Davidson Partnership is one of these local partnerships. As such, the Davidson Partnership is a private nonprofit 501(c)(3) organization and is required by General Statute 143B-168.14(b) to have a financial and compliance audit conducted by the Office of the State Auditor.

The purpose of this report is to present the results of our audit on the accompanying financial statements. A summary of our reporting objectives and audit results are:

- 1. Objective** – To express an opinion on the accompanying financial statements.

Results – The accompanying financial statements present fairly, in all material respects, the amounts and disclosures made in accordance with the modified cash basis of accounting, a comprehensive basis of accounting other than generally accepted accounting principles.

AUDITOR'S TRANSMITTAL (CONCLUDED)

2. **Objective** – To present significant deficiencies, if any, in internal control over financial reporting which could adversely affect the Davidson Partnership's ability to record, process, summarize, and report financial data in the financial statements and present instances of noncompliance, if any, with laws, regulations, contracts, or grants.

Results - The following conditions represent significant deficiencies in internal control or noncompliance with laws, regulations, contracts, or grants.

Finding

1. Control Environment
2. Contract Management and Monitoring

These matters are described in the Independent Auditor's Report on Compliance and on Internal Control over Financial Reporting and the Audit Findings and Recommendations section of this report.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.



Ralph Campbell, Jr.
State Auditor

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Ralph Campbell, Jr.
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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Davidson County Partnership for Children
Lexington, North Carolina

We have audited the accompanying Statement of Receipts, Expenditures, and Net Assets – Modified Cash Basis of the Davidson County Partnership for Children (Davidson Partnership) as of June 30, 2003, and the related Statement of Functional Expenditures – Modified Cash Basis for the year then ended. These financial statements are the responsibility of the Davidson Partnership's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the accompanying financial statements were prepared on the modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of the Davidson County Partnership for Children as of June 30, 2003, and the results of its operations arising from modified cash basis transactions for the year then ended, on the basis of accounting described in Note 1.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 30, 2004 on our consideration of the Davidson Partnership's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with the independent auditor's report in considering the results of our audit.

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

Our audit was made for the purpose of forming an opinion on the basic financial statements of the Davidson County Partnership for Children taken as a whole. The accompanying supplementary schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. The information in Schedules 1, 3, 4, and 5 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. The information in Schedule 2 has not been subjected to the auditing procedures applied in the audit of the basic financial statements and accordingly, we express no opinion on Schedule 2.

This report is intended solely for the information and use of the management of the Partnership, The North Carolina Partnership for Children, Inc., the Governor, and the General Assembly 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 "Ralph Campbell, Jr." in a cursive script.

Ralph Campbell, Jr.
State Auditor

June 30, 2004

Davidson County Partnership for Children**Statement of Receipts, Expenditures, and Net Assets - Modified Cash Basis****For the Year Ended June 30, 2003****Exhibit A**

| | Unrestricted Funds | | Temporarily Restricted Funds | Total Funds |
|---|--------------------|------------------|------------------------------|------------------|
| | Smart Start Fund | Other Funds | | |
| Receipts: | | | | |
| State Awards (less refunds of \$22,259) | \$ 2,081,519 | \$ 448,304 | \$ 0 | \$ 2,529,823 |
| Private Contributions | | 6,473 | | 6,473 |
| Interest and Investment Earnings | | 6,048 | | 6,048 |
| Sales Tax Refunds | | 1,265 | | 1,265 |
| Other Receipts | 4,232 | 1 | | 4,233 |
| Total Receipts | 2,085,751 | 462,091 | | 2,547,842 |
| Net Assets Released from Restrictions: | | | | |
| Satisfaction of Program Restrictions | | 1,090 | (1,090) | |
| | 2,085,751 | 463,181 | (1,090) | 2,547,842 |
| Expenditures: | | | | |
| Programs: | | | | |
| Child Care and Education Quality | 975,414 | 2,564 | | 977,978 |
| Health and Safety | 175,255 | 2,579 | | 177,834 |
| Family Support | 566,574 | 5,387 | | 571,961 |
| More at Four | 24,197 | 439,072 | | 463,269 |
| Support: | | | | |
| Management and General | 292,870 | 10,879 | | 303,749 |
| Program Evaluation | 30,000 | | | 30,000 |
| Other: | | | | |
| Sales Tax Paid | | 1,109 | | 1,109 |
| Refund of Prior Year Grant | | 21,291 | | 21,291 |
| Total Expenditures | 2,064,310 | 482,881 | | 2,547,191 |
| Excess of Receipts Over Expenditures | 21,441 | (19,700) | (1,090) | 651 |
| Net Assets at Beginning of Year | 38,552 | 56,261 | 1,390 | 96,203 |
| Net Assets at End of Year | \$ 59,993 | \$ 36,561 | \$ 300 | \$ 96,854 |
| Net Assets Consisted of: | | | | |
| Cash and Cash Equivalents | \$ 36,331 | \$ 36,561 | \$ 300 | \$ 73,192 |
| Refunds Due From Contractors | 23,973 | | | 23,973 |
| | 60,304 | 36,561 | 300 | 97,165 |
| Less: Funds Held for Others | 311 | | | 311 |
| | \$ 59,993 | \$ 36,561 | \$ 300 | \$ 96,854 |

The accompanying notes to the financial statements are an integral part of this statement.

Davidson County Partnership for Children
Statement of Functional Expenditures - Modified Cash Basis
For the Year Ended June 30, 2003

Exhibit B

| | Total | Personnel | Contracted Services | Supplies and Materials | Other Operating Expenditures | Fixed Charges and Other Expenditures | Property and Equipment Outlay | Services/ Contracts/ Grants | Participant Training Expenditures |
|--|---------------------|-------------------|---------------------|------------------------|------------------------------|--------------------------------------|-------------------------------|-----------------------------|-----------------------------------|
| Smart Start Fund: | | | | | | | | | |
| Programs: | | | | | | | | | |
| Child Care and Education Quality | \$ 975,414 | 213 | | | | | | 975,201 | |
| Health and Safety | \$ 175,255 | | 6,952 | | | | | 168,303 | |
| Family Support | \$ 566,574 | | | | | | | 566,574 | |
| More at Four | \$ 24,197 | | | | | | | 24,197 | |
| | \$ 1,741,440 | \$ 213 | \$ 6,952 | \$ 0 | \$ 0 | \$ 0 | \$ 0 | \$ 1,734,275 | \$ 0 |
| Support: | | | | | | | | | |
| Management and General | \$ 292,870 | 203,353 | 7,864 | 7,945 | 42,212 | 29,951 | 1,545 | | |
| Program Evaluation | \$ 30,000 | | 30,000 | | | | | | |
| | \$ 322,870 | \$ 203,353 | \$ 37,864 | \$ 7,945 | \$ 42,212 | \$ 29,951 | \$ 1,545 | \$ 0 | \$ 0 |
| Total Smart Start Fund Expenditures | \$ 2,064,310 | \$ 203,566 | \$ 44,816 | \$ 7,945 | \$ 42,212 | \$ 29,951 | \$ 1,545 | \$ 1,734,275 | \$ 0 |
| Other Funds: | | | | | | | | | |
| Programs: | | | | | | | | | |
| Child Care and Education Quality | \$ 2,564 | | | | | | | 2,564 | |
| Health and Safety | \$ 2,579 | | | 963 | | | | 1,616 | |
| Family Support | \$ 5,387 | | | 1,154 | 1,580 | | | 2,653 | |
| More at Four | \$ 439,072 | | | | | | | 439,072 | |
| | \$ 449,602 | \$ 0 | \$ 0 | \$ 2,117 | \$ 1,580 | \$ 0 | \$ 0 | \$ 445,905 | \$ 0 |
| Support: | | | | | | | | | |
| Management and General | \$ 10,879 | \$ 1,291 | \$ 8,524 | \$ 505 | \$ 435 | \$ 124 | \$ 0 | \$ 0 | \$ 0 |
| Other: | | | | | | | | | |
| Sales Tax Paid | \$ 1,109 | | | 1,109 | | | | | |
| Refund of Prior Year Grant | \$ 21,291 | | | | | 21,291 | | | |
| | \$ 22,400 | \$ 0 | \$ 0 | \$ 1,109 | \$ 0 | \$ 21,291 | \$ 0 | \$ 0 | \$ 0 |
| Total Other Funds Expenditures | \$ 482,881 | \$ 1,291 | \$ 8,524 | \$ 3,731 | \$ 2,015 | \$ 21,415 | \$ 0 | \$ 445,905 | \$ 0 |
| The accompanying notes to the financial statements are an integral part of this statement. | | | | | | | | | |

DAVIDSON COUNTY PARTNERSHIP FOR CHILDREN
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

- A. Organization and Purpose** - The Davidson County Partnership for Children (Davidson Partnership) is a legally separate nonprofit organization incorporated on February 10, 1994. The Davidson Partnership was established to develop and provide, through public and private means, early childhood education and developmental services for children and families. The Davidson Partnership is tax-exempt as an organization described in Section 501(c)(3) of the Internal Revenue Code.
- B. Basis of Presentation** – The accompanying financial statements present all funds for which the Davidson Partnership's Board of Directors is responsible. Pursuant to the provisions of Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-For-Profit Organizations*, the accompanying financial statements present information according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. As permitted by this Statement, temporarily restricted contributions received and expended in the same year are reported as unrestricted receipts rather than as temporarily restricted receipts.

Contributions that are temporarily restricted and not expended within the year received are reported as an increase in temporarily restricted net assets. When the restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Receipts, Expenditures, and Net Assets as net assets released from restrictions.

The Davidson Partnership did not have any permanently restricted net assets at June 30, 2003.

- C. Basis of Accounting** - The accompanying financial statements were prepared on the modified cash basis of accounting. This basis differs from accounting principles generally accepted in the United States of America primarily because it recognizes long lived assets and other costs which benefit more than one period as expended in the year purchased; it recognizes revenue when received rather than when earned; and it recognizes expenditures when paid rather than when incurred.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

However, unexpended advances to contractors that revert back to the State are recognized as a reduction to expenditures and an increase to net assets. In addition, amounts withheld from employee paychecks or other amounts received in an agency capacity are recorded as funds held for others.

- D. Cash and Cash Equivalents** – This classification appears on the Statement of Receipts, Expenditures, and Net Assets – Modified Cash Basis and consists of cash on deposit with private bank accounts.
- E. Refunds Due From Contractors** - Refunds due from contractors represent the unexpended amount of advances to contractors at year-end that are to be refunded back to the State. As recoveries are collected, the receivable balance is reduced. Payments to the State for the recovered advances are recorded as a reduction to the State awards balance.
- F. Funds Held For Others** - Funds held for others includes amounts received that are fiduciary in nature in which the Partnership acts in an agency capacity. For the year ended, the Davidson Partnership was holding amounts due to former employees.
- G. Compensated Absences** – As a result of the use of the modified cash basis of accounting, liabilities related to accrued compensated absences are not recorded in the financial statements. Expenditures related to compensated absences are recorded when paid. The amount of accrued compensated absences for accumulated, unpaid leave and compensatory time, along with the related employer costs that would be due to employees upon termination is reported as a commitment in Note 9.

NOTE 2 - DEPOSITS

All funds of the Davidson Partnership are deposited with a commercial bank and insured by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000. Deposits over this amount subjects the Davidson Partnership to a concentration of credit risk. At June 30, 2003, the Davidson Partnership's bank deposits in excess of the FDIC insured limit was \$69,398.

NOTE 3 - FUNDING FROM GRANT AWARDS

Smart Start Program - The Davidson Partnership's major source of revenue and support is from the State of North Carolina based on cost-reimbursement contracts with The North Carolina Partnership for Children, Inc. (NCPC) for the Smart Start Program. A significant reduction in the level of funding from

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

the State could have an adverse effect on the operations of the Davidson Partnership and represents a concentration of credit risk as to the generation of revenue.

Associated with these contracts, the Davidson Partnership is responsible for developing a comprehensive, collaborative, long-range plan of services to children and families for the service-delivery area. During the year, the North Carolina Department of Health and Human Services (DHHS) entered into contracts with and made payments to service providers selected by the Davidson Partnership. These service provider contracts are not reflected on the accompanying financial statements. However, a summary of the service provider contracts entered into by DHHS is presented on Schedule 2 accompanying the financial statements.

The Davidson Partnership was awarded and has received \$2,100,485 under a current year Smart Start contract with NCPC. The unexpended balance of this contract is subject to reversion to the State. The Partnership has returned \$35,404 of this contract to the State based on financial status reports submitted to NCPC subsequent to June 30, 2003.

The Partnership expects to receive continued funding through new Smart Start contracts with the State.

More at Four – The Davidson Partnership also received revenue and support from the State of North Carolina for the More at Four Program. The Davidson Partnership was awarded \$470,900 and received \$439,597 under a current year cost-reimbursement contract. The unexpended balance of this contract is subject to reversion to the State. The Partnership expects to receive continued funding through new More at Four contracts with the State.

NOTE 4 - RELATED PARTY TRANSACTIONS

Service Provider Contracts with Board Member Organizations - The board members of the Davidson Partnership are representative of various organizations that benefit from actions taken by the Board. It is the policy of the Davidson Partnership that board members not be involved with decisions regarding organizations they represent. During the year, the Partnership entered into contracts with board member organizations for program activities as identified on Schedule 1 accompanying the financial statements. In addition, Schedule 2 identifies contracts entered into by DHHS with board member organizations for activities funded by the Partnership's Smart Start Allocation.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 5 - FUNCTIONAL EXPENDITURES

The costs of providing the various programs and activities have been summarized on a functional basis in the Statement of Receipts, Expenditures, and Net Assets – Modified Cash Basis. Also, the Statement of Functional Expenditures – Modified Cash Basis, provides detail of the functional costs by their natural classification. Following are the services associated with the functional categories presented in the accompanying financial statements and the methods utilized to allocate joint cost:

A. Program Functions

Child Care and Education Quality - Used to account for service activities including quality enhancement grants for maintenance, child care resource and referral, and professional development.

Health and Safety - Used to account for service activities including child care health consultants, special needs – early intervention services, transportation to health services and developmental screenings.

Family Support - Used to account for service activities including ongoing parenting education, general family support, literacy projects and community outreach information and resources.

More at Four – Used to account for development and implementation of More at Four prekindergarten programs for at-risk four-year-olds who are at risk of failure in kindergarten. The goal is to provide quality prekindergarten services in order to enhance kindergarten readiness.

B. Support Functions

Management and General - Expenditures that are not identifiable with a single program or fund-raising activity but are indispensable to the conduct of those activities and to an organization's existence, including expenditures for the overall direction of the organization, its general board activities, business management, general recordkeeping, budgeting, and related purposes.

Program Evaluation - Expenditures that are incurred to monitor the performance of service providers as to the delivery of services and adherence to the specific terms and conditions of the contracts.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 6 - OPERATING LEASE OBLIGATIONS

Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2003:

| <u>Fiscal Year</u> | <u>Operating Leases</u> |
|------------------------------|-----------------------------|
| 2004 | \$ 23,571 |
| 2005 | 17,170 |
| 2006 | <u>1,736</u> |
| Total Minimum Lease Payments | <u>\$ 42,477</u> |

Rental expense for all operating leases during the year was \$29,157.

NOTE 7 - PENSION PLAN

The Davidson Partnership has a Simplified Employee Pension (SEP) plan covering all employees who have been employed for one year. Each employee of the Davidson Partnership, with more than one year of service, as a condition of employment, is provided an Individual Retirement Account through an outside insurance company. The Davidson Partnership contributed 6% of gross wages for the year ended June 30, 2003. The only exception to this procedure is for Executive Director whose benefit is 20% of his annual salary less the cost for his health and life insurance, with adjustments made quarterly. The Davidson Partnership does not own the accounts nor is liable for any other cost other than the required contribution.

For the year ended June 30, 2003, the Davidson Partnership contributed \$6,270 for pension benefits during the year.

NOTE 8 - RISK MANAGEMENT

The Davidson Partnership is exposed to various risks of loss related to torts, theft of, damage to, or destruction of assets; errors and omissions; injuries to employees; employees' health and life; and natural disasters. The Davidson Partnership manages these various risks of loss as follows:

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

| <u>Type of Loss</u> | <u>Method Managed</u> | <u>Risk of Loss Retained</u> |
|--|--------------------------------|------------------------------|
| Torts, errors and omissions, health and life | Purchased commercial insurance | None |
| Workers Compensation- Employee injuries | Purchased commercial insurance | None |
| Physical property loss and natural disasters | Purchased commercial insurance | None |

Management believes such coverage is sufficient to preclude any significant losses to the Davidson Partnership. Settled claims have not exceeded this insurance coverage in any of the past three fiscal years.

NOTE 9 - COMMITMENTS AND CONTINGENCIES

- A. Compensated Absences** – As a result of the Davidson Partnership’s use of the modified cash basis of accounting, accrued liabilities related to compensated absences (vacation only; sick leave does not vest) and any employer-related costs earned and unpaid, are not reflected in the financial statements. The compensated absences commitment for vacation leave at June 30, 2003, is \$1,819. No funds or reservation of net assets has been made for this commitment.
- B. Other Contingencies Resulting from Uncertainties** - The Davidson Partnership’s deficiencies in managing it’s Smart Start Quality Bonus activity and direct service providers resulted in questioned costs of \$93,878 and an undeterminable amount for those payments not tested. Additional questioned costs of \$5,234 were identified with payments made to a direct service provider. See the Audit Findings and Recommendations section for details. Because of the uncertainty, the amount of contingency that may result from this noncompliance and the disclosure of its effect on future funding from the State is not determinable.

NOTE 10 - RESTRICTIONS ON NET ASSETS

- A. Temporarily Restricted Net Assets** - Temporarily restricted net assets at June 30, 2003 are available for the following purposes:

| <u>Purpose</u> | <u>Amount</u> |
|-------------------|---------------|
| Grandparent’s Day | \$ 300 |

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

- B. Net Assets Released From Donor Restrictions** - Net assets were released from donor restrictions during the fiscal year ended June 30, 2003, by incurring expenditures satisfying the restricted purposes as follows:

| Purpose | Amount |
|----------------------------|-----------------|
| CCR&R Emergency Child Care | \$ 935 |
| Kimberly-Clark Foundation | 155 |
| | <u>\$ 1,090</u> |

Davidson County Partnership for Children
Schedule of Contract and Grant Expenditures - Modified Cash Basis
For the Year Ended June 30, 2003

Schedule 1

| Organization Name | Smart Start Fund | | Other Funds | |
|--|---------------------|--------------------|--------------------|---------------|
| | Amount Advanced | Refund Due | Amount Advanced | Refund Due |
| Barber's Childcare Home | 14,679 | | | |
| Boys & Girls LTD | 19,700 | | | |
| Child Care Connection | 131,503 | (1,249) | 1,200 | |
| Coggins Memorial Baptist Church | * 43,101 | | | |
| Davidson County Community College Child Development Center | * 93,180 | | | |
| Davidson County Area Program for MH/DD/SAS | * 25 | | | |
| Davidson County Department of Social Services | * | | 1,364 | |
| Davidson County Health Department | * 104,371 | (3,564) | 1,616 | |
| Davidson County Public Library | * 134,360 | (111) | | |
| Davidson County Schools | * 438,852 | (1) | 120,906 | |
| Davidson County Transportation | * 12,452 | | | |
| Family Services of Davidson County, Inc. | 55,045 | | | |
| First Reformed UCC Child Development Center | 31,221 | | | |
| First United Methodist Church | | | 2,653 | |
| Fleshman Pratt Education Center | 72,048 | | | |
| Lexington City Schools | * 4,368 | | 80,305 | |
| Northwest Child Development Council, Inc. | 3,925 | | 67,305 | |
| Robert Idol Child Development Center | 87,468 | | | |
| The Learning Place at Thomasville Medical Center | * 86,410 | | 55,626 | |
| Thomasville City Schools | * 6,552 | | 114,930 | |
| Thomasville Head Start | * 25,223 | | | |
| Tiny Tots Day Care, Inc. of Davidson County | 31,212 | | | |
| Tyro Learning Center | 53,424 | | | |
| Various Child Care Centers | 100,096 | (19,048) | | |
| Von's Kids, Inc. | 92,547 | | | |
| Wesleyan Child Development Center | 32,886 | | | |
| | \$ 1,674,648 | \$ (23,973) | \$ 445,905 | \$ 0 |
| Individuals: | | | | |
| Various Individuals-Education for the Stars | 83,600 | | | |
| | \$ 83,600 | \$ 0 | \$ 0 | \$ 0 |
| | \$ 1,758,248 | \$ (23,973) | \$ 445,905 | \$ 0 |
| * These organizations are represented on the Partnership's Board as described in Note 4A - Service Provider Contracts with Board Member Organizations. | | | | |

Davidson County Partnership for Children
Schedule of State Level Service Provider Contracts
For the Year Ended June 30, 2003

Schedule 2

| Organization Name | | DHHS Contracts |
|--|---|---------------------|
| Child Care Services Association - WAGES Program | | 120,000 |
| Davidson County Department of Social Services | * | 1,645,315 |
| | | \$ 1,765,315 |
| <p>* These organizations are represented on the Partnership's Board as described in Note 4 - Service Provider Contracts with Board Member Organizations.</p> | | |
| <p>The information on this schedule provides a listing of service provider contracts entered into by the North Carolina Department of Health and Human Services (DHHS) as described in Note 3 - Funding from Grant Awards.</p> | | |

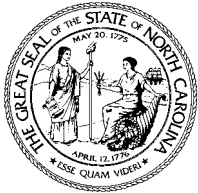
Davidson County Partnership for Children
Schedule of State Awards - Modified Cash Basis
For the Year Ended June 30, 2003

Schedule 3

| State Grantor/Pass-through Grantor/Program | Contract # | Receipts | Expenditures |
|---|----------------|---------------------|---------------------|
| State Awards: | | | |
| North Carolina Department of Health and Human Services | | | |
| Division of Child Development | | | |
| Pass-through from the North Carolina Partnership for Children, Inc. | | | |
| Early Childhood Initiatives Program (Prior Year) | #1-12-1-05-001 | \$ (18,966) | \$ 114 |
| Early Childhood Initiatives Program (Current Year) * | N/A | 2,100,485 | 2,064,196 |
| Multi-County Accounting and Contracting Grant (Prior Year) | N/A | (3,293) | |
| Multi-County Accounting and Contracting Grant (Current Year) | N/A | 12,000 | 10,200 |
| North Carolina Department of Health and Human Services | | | |
| More at Four Pre-Kindergarten Program | #2090002887 | 439,597 | 439,072 |
| Total State Awards | | \$ 2,529,823 | \$ 2,513,582 |
| * Programs with compliance requirements that have a direct and material effect on the financial statements. | | | |
| Note: The More at Four Pre-Kindergarten Program is contracted jointly by the North Carolina Department of Health and Human Services and the Office of the Governor. The allocations for the More at Four program are included in the budget for the North Carolina Department of Health and Human Services; therefore, the above schedule identifies that agency as the State Grantor. The Office of the Governor is responsible for oversight of the More at Four Program. | | | |

| | | | |
|---|--|----|-------------------|
| <i>Davidson County Partnership for Children</i> | | | |
| <i>Schedule of Property and Equipment - Modified Cash Basis</i> | | | |
| <i>For the Year Ended June 30, 2003</i> | | | <i>Schedule 4</i> |
| | | | |
| | | | |
| | Furniture and Non-Computer Equipment | \$ | 23,085 |
| | Computer Equipment/Printers | | 32,866 |
| | Leasehold Improvements | | 966 |
| | | | |
| | Total Property and Equipment | \$ | 56,917 |
| | | | |
| | | | |
| | | | |
| | Note: The information on this schedule provides a summary of property and equipment with acquisition or donated cost of \$500 or more which were held by the Partnership at year end. The valuations represent historical cost. On the modified basis of accounting, these items are expensed in the year of purchase. | | |

| | | |
|--|----|-------------------|
| <i>Davidson County Partnership for Children</i> | | |
| <i>Schedule of Qualifying Match (Non-GAAP)</i> | | |
| <i>For the Year Ended June 30, 2003</i> | | <i>Schedule 5</i> |
| <i>Match Provided at the Partnership Level:</i> | | |
| Cash | \$ | 5,121 |
| In-Kind Goods and Services | | 11,940 |
| | | |
| | \$ | 17,061 |
| <i>Match Provided at the Contractor Level:</i> | | |
| Cash | \$ | 359,610 |
| In-Kind Goods and Services | | 144,751 |
| | | |
| | \$ | 504,361 |
| <p>Note: This schedule is presented in accordance with the program match requirement as provided for by North Carolina Session Law 2001-424, Section 21.72(c). The law allows for volunteer services to be valued for match purposes, a concept that deviates from generally accepted accounting principles.</p> | | |
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Ralph Campbell, Jr.
State Auditor

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**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
THE FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Board of Directors
Davidson County Partnership for Children
Lexington, North Carolina

We have audited the financial statements of the Davidson County Partnership for Children (Davidson Partnership) as of and for the year ended June 30, 2003, and have issued our report thereon dated June 30, 2004. 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 Davidson Partnership's 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 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 Davidson Partnership's internal control over financial reporting in order to determine our auditing procedures for the purposes of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Davidson Partnership's ability to

**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
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GOVERNMENT AUDITING STANDARDS (CONCLUDED)**

record, process, summarize and report financial data consistent with the assertions of management in the financial statements. The reportable conditions noted as a result of our audit are described in the Audit Findings and Recommendations section of this report:

Finding

1. Control Environment
2. Contract Management and Monitoring

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 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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable conditions described above to be material weaknesses.

This report is intended solely for the information and use of the management of the Partnership, The North Carolina Partnership for Children, Inc., the Governor, and the General Assembly and is not intended to be, and should not be, used by anyone other than these specified parties.



Ralph Campbell, Jr.
State Auditor

June 30, 2004

AUDIT FINDINGS AND RECOMMENDATIONS

Matters Related to Financial Reporting

The following findings and recommendations were identified during the current audit and describe conditions that represent significant deficiencies in internal control. Both findings were reported in the previous year report.

1. CONTROL ENVIRONMENT

The control environment sets the tone of an organization, influencing the control consciousness of its personnel. It involves management's and the board of directors' attitude, awareness, and actions concerning internal control. During the previous year, we identified concerns with the Davidson Partnership Board's oversight and monitoring activities associated with its funded partners. We also identified that staff turnover directly affected the Partnership's ability to effectively monitor its contract and grant activities.

This finding is partially resolved. The Davidson Partnership was placed in the Performance Improvement Plan (PIP) by The North Carolina Partnership for Children, Inc. during the current fiscal year. A component of the PIP includes program specific training for both Board members and staff on the oversight and management functions for the Partnership. Another key element is the development and implementation of comprehensive policies and procedures to ensure the establishment of proper internal controls. Most of this activity occurred subsequent to the 2003 fiscal year and is ongoing. In addition, the Davidson Partnership has hired new personnel for both the Executive Director and the Finance Director positions. This should enhance the Partnership's ability to effectively monitor its contract and grant activities.

Recommendation: We recommend that the Davidson Partnership continue with its efforts in the Performance Improvement Plan. The continued development and implementation of comprehensive policies and procedures will provide for the establishment of proper internal control systems and provide direction and accountability for the operations of the Partnership.

Partnership's Response: In the year ended June 30, 2004, we actively participated in the NC Partnership for Children's Performance Improvement Plan and received much needed technical assistance and training. Through the help of their monitoring programs and the advice of their staff we have been able to make significant headway in our resolution of these issues.

The Davidson County Partnership for Children Board of Directors and staff also participated in a high level training provided through the Performance Improvement Plan.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

This training included various topics on Board development, understanding Board roles, and the importance of a strong control environment.

Staff positions have been restructured and the part-time finance position has been replaced with a full-time Finance Director who has a CPA license, as well as seven years of successful Smart Start accounting experience.

Davidson County Partnership for Children Board and staff worked diligently in the fiscal year ended June 30, 2004 to revise all accounting and contracting policies to ensure a strengthened control environment. The Board has played a key role in creating and implementing a process of accountability for all activities. The Partnership's intention is to use appropriate practices to secure maximum effectiveness and efficiency in the use of public dollars.

2. CONTRACT MANAGEMENT AND MONITORING

We reported in the prior year that weaknesses existed in the Davidson Partnership's contract management and monitoring activities. Deficiencies identified included insufficient or unavailable documentation to support changes to established program criteria, eligibility of payments for in-house grant activities, or the Partnership's programmatic monitoring activities.

This finding is unresolved. We continued to note the following deficiencies in the contracting and monitoring processes of the Partnership:

- Formal contracting policies and procedures for the administration of grants were not in place during the 2003 fiscal year.
- Deficiencies continued to be noted in the fiscal and programmatic monitoring activities of the Partnership. Further enhancements are necessary in documenting actual programmatic outcomes and follow-up of identified problem issues.
- We identified that a direct service provider billed and was reimbursed for the payment of employee leave balances. A total of \$5,234 was paid out representing the unused balances for child involvement, sick, and vacation pay leave for employees of the direct service provider. The payout of leave balances is not an allowable policy within the Smart Start program and these charges are considered to be questioned costs.
- The Partnership failed to follow its payment criteria for its Smart Start Quality Bonus activity. The failure to properly calculate its monthly disbursements to daycare providers resulted in overpayments and questioned costs.

AUDIT FINDINGS AND RECOMMENDATIONS (CONTINUED)

- The Smart Start Quality Bonus program was funded at \$761,347 during the 2003 fiscal year. Payment schedules were established for monthly, quarterly, and semiannual reimbursements for services. For the monthly payment schedule, the criteria stated that participating daycares would be reimbursed upon the submission of a payment application and an attached monthly attendance report to substantiate attendance of children.
- We determined that monthly attendance forms were not consistently submitted as per the criteria. Payments were made based upon the previous month attendance sheet and that payment amount continued for the next two months. Actual enrollment documentation to substantiate the payments for the year was limited. We performed recalculations from the limited documentation available and determined that overpayments continued. Our testwork involved 6 centers with total payments of \$244,650. We identified payments totaling \$90,854 that were not substantiated by attendance records. In addition, we identified overpayments totaling \$3,024 for those items tested. As our testwork was not statistically performed, we are unable to project our test results to the total amount of payments. As such, the total amount of over or underpayments could not be determined. Our known questioned costs are \$90,854.

The achievement of the Davidson Partnership's goals is dependent on the effectiveness of its contract management system and its monitoring of contractor performance.

Recommendation: We recommend that the Davidson Partnership enhance its contract management and monitoring procedures to ensure that documentation is maintained to support program criteria, eligibility of grant payments, as well as the Partnership's programmatic monitoring activities. Payments should be made in accordance with established criteria and adequate documentation should be obtained to support payments. In addition, the Davidson Partnership should consult with The North Carolina Partnership for Children, Inc. to resolve the identified questioned costs and the issue of any potential overpayments that may have occurred in the untested centers.

Partnership's Response: In the year ended June 30, 2004, we actively participated in the NC Partnership for Children's Performance Improvement Plan and received much needed technical assistance and training. Through the help of their monitoring programs and the advice of their staff we have been able to make significant headway in our resolution of these issues.

Davidson County Partnership for Children also worked in fiscal year end June 30, 2004 to review, revise, and implement new monitoring, contracting, and grants management policies. Our new monitoring program includes a four-part monitoring series that looks at contract, programmatic, fiscal, and evaluation compliance. Staff positions have also been restructured in this area to ensure monitoring is separate from the program

AUDIT FINDINGS AND RECOMMENDATIONS (CONCLUDED)

management to ensure more independent oversight. We are also working with the Direct Service Provider in question to create a corrective action plan and we will continue to monitor them closely.

We spent a great deal of time in fiscal year end June 30, 2004 reviewing and implementing new contracting and grants management policies. The Smart Start Quality Bonus activity was heavily monitored during the final three quarters of the fiscal year and we do not anticipate issues related to this activity. As of July 1, 2004, Davidson County Partnership for Children is no longer funding the Smart Start Quality Bonus activity.

We appreciate the diligence and professionalism with which this audit was performed and fully accept the recommendations as reported to us. We are determined to respond fully to the recommendations from your team and will continue our efforts for continuous improvement in our organizational effectiveness and compliance.

DISTRIBUTION OF AUDIT REPORT

In accordance with General Statutes 147-64.5 and 147-64.6(c)(14), copies of this report have been distributed to the public officials listed below. Additional copies are provided to other legislators, state officials, the press, and the general public upon request.

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September 8, 2004

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