



STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF DOWN EAST PARTNERSHIP FOR CHILDREN

ROCKY MOUNT, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2004

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

FINANCIAL STATEMENT AUDIT REPORT OF

DOWN EAST PARTNERSHIP FOR CHILDREN

ROCKY MOUNT, NORTH CAROLINA

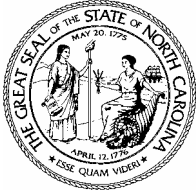
FOR THE YEAR ENDED JUNE 30, 2004

BOARD OF DIRECTORS

ALICE THORP, BOARD CHAIRPERSON

ADMINISTRATIVE OFFICER

HENRIETTA ZALKIND, EXECUTIVE DIRECTOR



Leslie W. Merritt, Jr., CPA, CFP
State Auditor

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AUDITOR'S TRANSMITTAL

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

This report presents the results of our financial statement audit of the Down East Partnership for Children (Down East Partnership) for the year ended June 30, 2004. Our audit was made by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

The accounts and operations of the Down East 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 Down East 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 Down East Partnership is one of these local partnerships. As such, the Down East 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 Down East Partnership's ability to record, process, summarize, and report financial data in the financial statements and present instances of noncompliance or other matters, if any, with laws, regulations, contracts, or grant agreements.

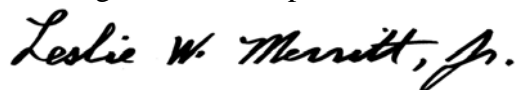
Results - The following condition represents a significant deficiency in internal control or noncompliance or other matters with laws, regulations, contracts, or grant agreements.

Finding

Contract Management and Monitoring Deficiencies

This matter is described in the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters 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.



Leslie W. Merritt, Jr., CPA, CFP
State Auditor

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Down East Partnership for Children
Rocky Mount, North Carolina

We have audited the accompanying Statement of Receipts, Expenditures, and Net Assets – Modified Cash Basis of the Down East Partnership for Children (Down East Partnership) as of June 30, 2004, and the related Statement of Functional Expenditures – Modified Cash Basis for the year then ended. These financial statements are the responsibility of the Down East 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 Down East Partnership for Children as of June 30, 2004, 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 July 8, 2005, on our consideration of the Down East Partnership's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Down East Partnership for Children's basic financial statements. The information in Schedules 1, 3, 4, and 5 is presented for purposes of additional analysis and is not a required part of the basic financial statements. These Schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are 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.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

July 8, 2005

***Down East Partnership for Children
Statement of Receipts, Expenditures, and Net Assets - Modified Cash Basis
For the Year Ended June 30, 2004***

Exhibit A

	Unrestricted Funds		Temporarily Restricted Funds	Total Funds
	Smart Start Fund	Other Funds		
Receipts:				
State Awards (less refunds of \$58,016)	\$ 3,169,865	\$ 609,750	\$ 0	\$ 3,779,615
Federal Awards (less refunds of \$185)		214,050		214,050
Local Awards		10,000		10,000
Private Contributions		325,006	294,639	619,645
Interest and Investment Earnings		18,201		18,201
Sales Tax Refunds		20,873		20,873
Other Receipts		7,044		7,044
Total Receipts	3,169,865	1,204,924	294,639	4,669,428
Net Assets Released from Restrictions:				
Satisfaction of Program Restrictions		112,927	(112,927)	
	3,169,865	1,317,851	181,712	4,669,428
Expenditures:				
Programs:				
Child Care and Education Affordability	1,158,239			1,158,239
Child Care and Education Quality	905,911	412,906		1,318,817
Family Support	724,245	178,320		902,565
Health and Safety	141,783	10,270		152,053
More at Four		583,200		583,200
Support:				
Fund Raising		58,130		58,130
Management and General	269,572	82,945		352,517
Other:				
Sales Tax Paid		17,745		17,745
Total Expenditures	3,199,750	1,343,516		4,543,266
Excess of Receipts Over Expenditures	(29,885)	(25,665)	181,712	126,162
Net Assets at Beginning of Year	57,800	360,787	126,784	545,371
Net Assets at End of Year	\$ 27,915	\$ 335,122	\$ 308,496	\$ 671,533
Net Assets Consisted of:				
Cash and Cash Equivalents	\$ 27,655	\$ 0	\$ 308,496	\$ 336,151
Investments		333,352		333,352
Refunds Due From Contractors	284			284
	27,939	333,352	308,496	669,787
Less: Funds Held for Others	24	(1,770)		(1,746)
	\$ 27,915	\$ 335,122	\$ 308,496	\$ 671,533

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

Down East Partnership for Children
Statement of Functional Expenditures - Modified Cash Basis
For the Year Ended June 30, 2004

Exhibit B

	Total	Personnel	Contracted Services	Supplies and Materials	Other Operating Expenditures	Fixed Charges and Other Expenditures	Property and Equipment Outlay	Indirect Costs	Services/Contracts/Grants	Participant Training Expenditures
Smart Start Fund:										
Programs:										
Child Care and Education Affordability	\$ 1,158,239	\$ 106,222	\$ 13,179	\$ 2,647	\$ 7,989	\$ 2,182	\$ 0	\$ 0	\$ 1,026,020	\$ 0
Child Care and Education Quality	905,911	193,912	14,558	16,958	48,776	10,917	3,146		617,644	
Family Support	724,245	379,740	18,293	23,445	51,292	7,173	19,079		222,983	2,240
Health and Safety	141,783	28,545	897	1,984	4,636	87			105,634	
	<u>2,930,178</u>	<u>708,419</u>	<u>46,927</u>	<u>45,034</u>	<u>112,693</u>	<u>20,359</u>	<u>22,225</u>		<u>1,972,281</u>	<u>2,240</u>
Support:										
Management and General	269,572	208,591	15,763	5,596	33,248	5,801	573			
Total Smart Start Fund Expenditures	\$ 3,199,750	\$ 917,010	\$ 62,690	\$ 50,630	\$ 145,941	\$ 26,160	\$ 22,798	\$ 0	\$ 1,972,281	\$ 2,240
Other Funds:										
Programs:										
Child Care and Education Quality	\$ 412,906	\$ 269,737	\$ 45,391	\$ 13,530	\$ 45,151	\$ 980	\$ 2,041	\$ 19,694	\$ 7,815	8,567
Family Support	178,320	42,578	3,110	5,367	12,718	775	2,496	9,506	101,303	467
Health and Safety	10,270	7,136	425	485	1,269	21		934		
More at Four	583,200							37,267	545,933	
	<u>1,184,696</u>	<u>319,451</u>	<u>48,926</u>	<u>19,382</u>	<u>59,138</u>	<u>1,776</u>	<u>4,537</u>	<u>67,401</u>	<u>655,051</u>	<u>9,034</u>
Support:										
Fund Raising	58,130	30,218	8,936	2,768	13,553	2,655				
Management and General	82,945	136,197		1,080	12,049		905	(67,401)	15	100
	<u>141,075</u>	<u>166,415</u>	<u>8,936</u>	<u>3,848</u>	<u>25,602</u>	<u>2,655</u>	<u>905</u>	<u>(67,401)</u>	<u>15</u>	<u>100</u>
Other:										
Sales Tax Paid	17,745			17,745						
Total Other Funds Expenditures	\$ 1,343,516	\$ 485,866	\$ 57,862	\$ 40,975	\$ 84,740	\$ 4,431	\$ 5,442	\$ 0	\$ 655,066	\$ 9,134

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

DOWN EAST PARTNERSHIP FOR CHILDREN
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2004

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

- A. Organization and Purpose** - The Down East Partnership for Children (Down East Partnership) is a legally separate nonprofit organization incorporated on December 7, 1993. The Down East Partnership was established to develop and provide, through public and private means, early childhood education and developmental services for children and families. The Down East 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 Down East 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 Down East Partnership did not have any permanently restricted net assets at June 30, 2004.

- 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 of North Carolina 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 includes all demand and savings accounts and certificate of deposits or short-term investments with an original maturity of three months or less.
- E. Investments** – This classification includes money market funds, certificates of deposit whose original maturity term exceeds three months, and bonds. Investments are reported at fair market value.
- F. 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.
- G. Funds Held For Others** - Funds held for others includes amounts received that are fiduciary in nature in which the Down East Partnership acts in an agency capacity. The Down East Partnership offers its employees the opportunity to participate in a Flexible Spending Plan (Plan), which is a cafeteria plan as defined by Section 125 of the Internal Revenue Code. A cafeteria plan allows employees to pay for certain employee benefits with pre-tax deductions. For the period June 30, 2004, the Down East Partnership has made payments in excess of the amounts withheld from employees' paychecks for the Plan resulting in a deficit balance in the funds held for others account. The Down East Partnership will collect the amounts advanced from the Plan from employees in the future per the Plan's guidelines.
- H. Property and Equipment** – Under the modified cash basis of accounting, purchases of property and equipment are reported as expenditures in the year occurred. However, Down East Partnership is required by contract regulation to track and maintain property and equipment items as presented in Schedule 4 of this report. The Down East Partnership has a policy to track purchases of property and equipment items with an individual cost of \$500 or more and an estimated useful life greater than one year. Such items are valued at their original purchase price, which may be different from their valuation as of June 30, 2004. Donated items are recorded at estimated fair market value at the date of donation.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- I. 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 that would be due to employees upon termination is reported as a commitment in Note 9.
- J. Use of Estimates** - The preparation of financial statements in conformity with the modified cash basis of accounting used by the Down East Partnership requires management to make estimates and assumptions that affect certain reported amounts and disclosures (such as allocation of joint costs); accordingly, actual results could differ from those estimates. It is management's belief that these estimates are reasonable and fair.

NOTE 2 - DEPOSITS

All funds of the Down East Partnership are deposited with commercial banks and insured by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000 per bank. Deposits over this amount subjects the Down East Partnership to a concentration of credit risk.

The Down East Partnership has an Automated Investment Plan to invest excess balances over an established target amount. The investment is in the bank's repurchase agreements and is not insured by the FDIC. Consequently, the Down East Partnership bank deposits in excess of the FDIC insured limit totaled \$691,645 at June 30, 2004.

NOTE 3 - FUNDING FROM GRANT AWARDS

Smart Start Program - The Down East 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 the State could have an adverse effect on the operations of the Down East Partnership and represents a concentration of credit risk as to the generation of revenue.

Associated with these contracts, the Down East 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 Down East Partnership. These service provider contracts are not reflected on the accompanying financial statements. However, a summary of the service

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

provider contracts entered into by DHHS is presented on Schedule 2 accompanying the financial statements.

The Down East Partnership was awarded and has received \$3,227,665 under a current year Smart Start contract with NCPC. The unexpended balance of this contract is subject to reversion to the State. The Down East Partnership has returned \$27,775 of this contract to the State based on financial status reports submitted to NCPC subsequent to June 30, 2004.

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

More at Four – The Down East Partnership also received revenue and support from the State of North Carolina for the More at Four Program. The Down East Partnership was awarded \$804,996 and received \$585,966 under a current year cost-reimbursement contract. The Down East 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 Down East Partnership are representative of various organizations that benefit from actions taken by the Board. It is the policy of the Down East Partnership that board members not be involved with decisions regarding organizations they represent. During the year, the Down East 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 Down East Partnership's Smart Start Allocation.

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:

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

A. Program Functions

Child Care and Education Affordability - Used to account for service activities including public pre-K classes or child care subsidy programs outside of the Division of Child Development.

Child Care and Education Quality - Used to account for service activities including quality enhancement grants for upgrades, child care resource and referral, kindergarten orientation/transition, the SPARK initiative or health insurance benefits for child care providers.

Family Support - Used to account for service activities including family resource centers, ongoing parenting education, general family support, family crisis intervention, literacy projects, or community outreach information.

Health and Safety - Used to account for service activities including comprehensive health support or special needs – early intervention services/special education.

More at Four – Used to account for development and implementation of More at Four prekindergarten program 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

Fund Raising - Expenditures that are incurred in inducing others to contribute money, securities, time, materials, or facilities for which the contributor will receive no direct economic benefit.

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.

C. Allocation of Joint Costs

The Down East Partnership uses an indirect cost pool to collect administrative expenses that are not directly attributable to the various programs the Partnership operates. Types of costs included in the pool were salaries, contracted services, supplies and materials, other operating expenses, fixed charges and other expenses, property and equipment, and participant training.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Indirect costs are allocated using a percentage of program expenses. The indirect cost rate used for the 2004 fiscal year was 12.77% except for the Family Preservation grant, which had a maximum allowable indirect cost percentage of 10% and the Smart Start administrative contract, which had a maximum allowable amount of \$269,572.

Management and overhead costs totaling \$418,908 were distributed across program activities, including \$269,572 specifically allocated to the Smart Start administrative contract. These costs were initially recorded in the indirect cost pool and then allocated on a monthly basis to the affected programs. An Indirect Cost column has been added to the Statement of Functional Expenditures – Regulatory Basis to indicate how these costs were distributed across programs and to eliminate the charges recorded for distributing the costs. This column allows for a more accurate presentation of costs by program and functional category.

NOTE 6 - OPERATING LEASE OBLIGATIONS

Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2004:

<u>Fiscal Year</u>	<u>Operating Leases</u>
2005	\$ 9,216
2006	389
Total Minimum Lease Payments	<u>\$ 9,605</u>

Rental expense for all operating leases during the year was \$9,451.

NOTE 7 - PENSION PLAN

Deferred Compensation and Supplemental Retirement Income Plans - IRC Section 403(b) Plan - All permanent employees who are at least half time can participate in a tax sheltered annuity plan (Plan) created under Internal Revenue Code Section 403(b). The Plan is a defined contribution plan in which each employee of the Down East Partnership, as a condition of employment, is provided an individual annuity through an outside insurance company. Each employee of the Down East Partnership is provided, as part of the benefit package, an additional 15% of his/her salary to be applied to an individual retirement plan. The Down East Partnership has no liability for any other cost other than the required percentage. The employee's eligible contributions, made through salary reduction agreements, are exempt from

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

federal and State income taxes until the annuity is received or the contributions are withdrawn. These Plans are exclusively for employees of universities and certain charitable and other nonprofit organizations. All costs of administering and funding these Plans are the responsibility of the Plan participants. The Down East Partnership contributed \$75,090 for retirement benefits during the year as part of the benefit package.

NOTE 8 - RISK MANAGEMENT

The Down East 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 Down East Partnership manages these various risks of loss as follows:

<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 Down East Partnership. Settled claims have not exceeded this insurance coverage in any of the past three fiscal years.

NOTE 9 - COMMITMENTS AND CONTINGENCIES

Compensated Absences – As a result of the Down East 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, 2004, is \$68,080. No funds or reservation of net assets has been made for this commitment.

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

NOTE 10 - RESTRICTIONS ON NET ASSETS

A. Temporarily Restricted Net Assets - Temporarily restricted net assets at June 30, 2004, are available for the following purposes:

Purpose	Amount
Project Recovery	\$ 500
Latino Outreach	925
Flood Relief	7,500
Kellogg Foundation	174,950
Child Care Resource and Referral	101,121
Roof Replacement Project	23,500
	<u>\$ 308,496</u>

B. Net Assets Released From Donor Restrictions - Net assets were released from donor restrictions during the fiscal year ended June 30, 2004, by incurring expenditures satisfying the restricted purposes as follows:

Purpose	Amount
Child Care Resource and Referral	<u>\$ 100,000</u>

NOTE 11 - PUBLIC SUPPORT AND FUNDING

The Down East Partnership has received significant funding commitments for future periods through a private organization. A grant commitment totaling \$1,578,385 was received from the W.K. Kellogg Foundation for the purpose of improving learning outcomes for children by strengthening partnerships and their efforts to align early learning resources, services, practices, and policies.

The activity has been identified as the Kellogg SPARK (Supporting Partnerships to Assure Ready Kids) Initiative. The project is scheduled through the 2008 fiscal year.

***Down East Partnership for Children
Schedule of Contract and Grant Expenditures - Modified Cash Basis
For the Year Ended June 30, 2004***

Schedule 1

Organization Name	Smart Start Fund		Other Funds	
	Amount Advanced	Refund Due	Amount Advanced	Refund Due
Benvenue Child Care Center	\$ 0	\$ 0	\$ 55,108	\$ 0
Braswell Memorial Library	* 62,357			
Camelot Child Care Center			11,946	
Carolyn's Child Care Center			57,071	
Communities In Schools of The Rocky Mount Region	* 59,706		40,000	
Community Enrichment Organization			40,000	
Edgecombe County Department of Social Services	*		5,109	
Edgecombe County Health Department	* 105,779	(144)		
Edgecombe County Schools	* 535,075	(140)	163,844	
Fairplay Child Care Center			62,190	
Nash County Department of Social Services	*		7,404	
Nash-Rocky Mount Schools	* 195,841		144,905	
Think and Grow			59,659	
Various Day Care Providers	30,000		7,815	
	<u>988,758</u>	<u>(284)</u>	<u>655,051</u>	
<i>Paid to Individuals:</i>				
Connect the Dots Stipends	4,278			
Insurance Stipends	6,000		15	
Scholarships	973,529			
	<u>983,807</u>		<u>15</u>	
	<u>\$ 1,972,565</u>	<u>\$ (284)</u>	<u>\$ 655,066</u>	<u>\$ 0</u>

* These organizations are represented on the Partnership's Board as described in Note 4 - Service Provider Contracts with Board Member Organizations.

***Down East Partnership for Children
Schedule of State Level Service Provider Contracts
For the Year Ended June 30, 2004***

Schedule 2

Organization Name	DHHS Contracts
Child Care Services Association - WAGE\$ Program	\$ 270,155
Nash/Edgecombe Counties Departments of Social Services	* 140,319
	<u>\$ 410,474</u>

* These organizations are represented on the Partnership's Board as described in Note 4 - Service Provider Contracts with Board Member Organizations.

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.

***Down East Partnership for Children
Schedule of Federal and State Awards - Modified Cash Basis
For the Year Ended June 30, 2004***

Schedule 3

Federal/State Grantor/Pass-through Grantor/Program	Federal CFDA Number	Contract #	Receipts	Expenditures
Federal Awards:				
Department of Justice Pass-through from the North Carolina Department of Crime Control and Public Safety - Division of Governor's Crime Commission Passed-through the City of Rocky Mount Byrne Formula Grant Program (Project Recovery)	16.579	033-1-00-013-362	\$ (185)	\$ 0
Department of Health and Human Services Pass-through from the North Carolina Department of Health and Human Services - Division of Social Services Promoting Safe and Stable Families (Family Preservation - Prior Year)	93.556		3,533	
Promoting Safe and Stable Families (Family Preservation - Current Year)	93.556	01120-04	142,225	144,839
Department of Health and Human Services Pass-through from the North Carolina Department of Health and Human Services - Division of Child Development Child Care Development Block Grant (Prior Year)	93.575	5994	5,807	
Pass-through Halifax-Warren Smart Start Partnership for Children, Inc. Child Care Development Block Grant (Current Year)	93.575	3-34-1-06-701	62,670	61,605
Total Federal Awards			<u>214,050</u>	<u>206,444</u>
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)		Various	(57,800)	
Early Childhood Initiatives Program (Current Year)	*	N/A	3,227,665	3,199,750
Multi-County Accounting and Contracting Grant (Prior Year)		N/A	(216)	
Multi-County Accounting and Contracting Grant (Current Year)		N/A	24,000	24,000
North Carolina Department of Health and Human Services More at Four Pre-Kindergarten Program	*	2090003764	585,966	583,200
Total State Awards			<u>3,779,615</u>	<u>3,806,950</u>
Total Federal and State Awards			<u>\$ 3,993,665</u>	<u>\$ 4,013,394</u>

* 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.

***Down East Partnership for Children
Schedule of Property and Equipment - Modified Cash Basis
For the Year Ended June 30, 2004***

Schedule 4

Furniture and Noncomputer Equipment	\$ 97,286
Computer Equipment/Printers	130,693
Buildings	564,130
Leasehold Improvements	<u>203,178</u>
Total Property and Equipment	<u><u>\$ 995,287</u></u>

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.

***Down East Partnership for Children
Schedule of Qualifying Match (Non-GAAP)
For the Year Ended June 30, 2004***

Schedule 5

Match Provided at the Partnership Level:

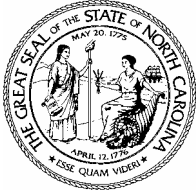
Cash	\$	629,690
In-Kind Goods and Services		<u>5,780</u>
	\$	<u><u>635,470</u></u>

Match Provided at the Contractor Level:

Cash	\$	83,835
In-Kind Goods and Services		<u>111,611</u>
	\$	<u><u>195,446</u></u>

Note: This schedule is presented in accordance with the program match requirement as provided for by North Carolina Session Law 2003-284, Section 10.38(c). The North Carolina Partnership for Children, Inc. and all local partnerships are required to match the total amount budgeted for the Smart Start Program in each fiscal year. The match is comprised of both cash and in-kind amounts. Only in-kind contributions that are verifiable, quantifiable, and related to the Smart Start Program can be applied to the in-kind match requirement, including volunteer services. The law allows for volunteer services to be valued for match purposes, a concept that deviates from generally accepted accounting principles. This schedule identifies those amounts allowable for this partnership in meeting the statewide match requirement.

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Leslie W. Merritt, Jr., CPA, CFP
State Auditor

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

Board of Directors
Down East Partnership for Children
Rocky Mount, North Carolina

We have audited the financial statements of the Down East Partnership for Children (Down East Partnership) as of and for the year ended June 30, 2004, and have issued our report thereon dated July 8, 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Down East 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 an opinion on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. A reportable condition involves a matter coming to our attention relating to a significant deficiency in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Down East Partnership's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. This reportable condition is reported, with responses, in the Audit Findings and Recommendations section of this report:

Finding

Contract Management and Monitoring Deficiencies

A material weakness is a reportable 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 caused by error or fraud 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

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

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 do not believe the reportable condition described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Down East Partnership's 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 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 or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the audit committee, management of the Down East 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.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

July 8, 2005

AUDIT FINDINGS AND RECOMMENDATIONS

Matters Related to Financial Reporting

The following finding and recommendation was identified during the current audit and discusses conditions that represent significant deficiencies in internal control and/or noncompliance with laws, regulations, contracts, or grants.

CONTRACT MANAGEMENT AND MONITORING DEFICIENCIES

During our review of the Down East Partnership's contract management and monitoring system, we identified the following deficiencies:

- More at Four start-up funds totaling \$80,100 were provided to child care facilities that were not included in the Partnership's grant agreements with these child care facilities. In addition, child transportation costs were paid on the Scholarship program that were not part of the authorized grant agreements with reimbursed child care facilities;
- We identified instances where the Partnership failed to follow its established criteria for the Scholarship program. Scholarship criteria required that eligible recipients were to work at least 32 hours per week; however, the Partnership did not maintain documentation to support compliance with this requirement. Test errors for this criteria totaled \$44,400. In addition, we noted where the Partnership granted exceptions to this eligibility requirement that deviated from the program's established guidelines. Test errors for this criteria totaled \$19,600;
- Payments totaling \$22,800 were made for the More at Four program after the June 15th cut-off date identified in the contract;
- Deficiencies were identified in the monitoring procedures for the Scholarship program. The Partnership failed to consistently maintain documentation to support requirements such as the verification of children ages, days of attendance eligible for reimbursement, or required parent education hours.

Recommendation: We recommend that the Down East Partnership enhance its current contract management and monitoring procedures. Grant agreements should be inclusive of all sources of funds, including both cash and noncash awards. The Partnership should also review the established criteria for the Scholarship program to ensure that intended goals are being met and documentation is maintained to support the achievement of those goals.

Partnership's Response: We were aware of these issues, which largely resulted from turnover both in line-staff and supervision of our Scholarship Program. All issues have been addressed and revised policy and procedures implemented after the audit period.

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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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The Honorable Richard H. Moore	State Treasurer
The Honorable Roy A. Cooper, III	Attorney General
Mr. David T. McCoy	State Budget Officer
Mr. Robert L. Powell	State Controller
Ms. Carmen Hooker Odom	Secretary, Department of Health and Human Services
Mr. Ashley Thrift	Chairman, Board of Directors
	The North Carolina Partnership for Children, Inc.
Ms. Karen Ponder	Executive Director
	The North Carolina Partnership for Children, Inc.

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September 16, 2005

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