

COMPLIANCE SECTION



MARTIN ♦ STARNES & ASSOCIATES, CPAs, P.A.

"A Professional Association of Certified Public Accountants and Management Consultants"

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

Independent Auditor's Report

To the Honorable Mayor and
Members of the City Council
City of Lexington, North Carolina

We have audited, in accordance with the 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, the accompanying 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 Lexington, North Carolina, as of and for the year ended June 30, 2016, and the related notes to the financial statements which collectively comprise the City of Lexington's basic financial statements, and have issued our report thereon dated October 24, 2016. Our report includes a reference to other auditors who audited the financial statements of the City of Lexington ABC Board, as described in our report on the City of Lexington's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported separately by those auditors. The financial statements of the City of Lexington ABC Board and the Lexington Tourism Authority were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of Lexington's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City of Lexington's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

A deficiency in internal control 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 and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not

identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Lexington's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, non-compliance 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 non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Martin Starnes & Associates, CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
Hickory, North Carolina
October 24, 2016

MARTIN ♦ STARNES & ASSOCIATES, CPAs, P.A.

"A Professional Association of Certified Public Accountants and Management Consultants"

Report On Compliance For Each Major Federal Program; Report On Internal Control Over Compliance; In Accordance With OMB Uniform Guidance and the State Single Audit Implementation Act

Independent Auditor's Report

To the Honorable Mayor and
Members of the City Council
City of Lexington, North Carolina

Report on Compliance for Each Major Federal Program

We have audited the City of Lexington, North Carolina's compliance with the types of compliance requirements described in the OMB *Compliance Supplement* and the *Audit Manual for Governmental Auditors in North Carolina*, issued by the Local Government Commission, that could have a direct and material effect on each of the City of Lexington's major federal programs for the year ended June 30, 2016. The City of Lexington's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for the compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City of Lexington's major federal programs based on our audit of the types of compliance requirements referred to above. 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 the audit requirements of *Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) and the State Single Audit Implementation Act. Those standards, the Uniform Guidance, and the State Single Audit Implementation Act require that we plan and perform the audit to obtain reasonable assurance about whether non-compliance 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 Lexington'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 on compliance for each major federal program. However, our audit does not provide a legal determination of the City of Lexington's compliance.

Opinion on Each Major Federal Program

In our opinion, the City of Lexington complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

Report on Internal Control Over Compliance

Management of the City of Lexington is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City of Lexington's internal control over compliance with the types of requirements that could have a direct and material effect on a major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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 Lexington's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, non-compliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material non-compliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Martin Starnes & Associates, CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
Hickory, North Carolina
October 24, 2016

MARTIN ♦ STARNES & ASSOCIATES, CPAs, P.A.

"A Professional Association of Certified Public Accountants and Management Consultants"

Report On Compliance For Each Major State Program; Report On Internal Control Over Compliance; In Accordance With OMB Uniform Guidance; And The State Single Audit Implementation Act

Independent Auditor's Report

To the Honorable Mayor and
Members of the City Council
City of Lexington, North Carolina

Report on Compliance for Each Major State Program

We have audited the City of Lexington, North Carolina's, compliance with the types of compliance requirements described in the *Audit Manual for Governmental Auditors in North Carolina*, issued by the Local Government Commission, that could have a direct and material effect on each of the City of Lexington's major State programs for the year ended June 30, 2016. The City of Lexington's major State programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major State programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City of Lexington's major State programs based on our audit of the types of compliance requirements referred to above. 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 applicable sections of *Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), as described in the *Audit Manual for Governmental Auditors in North Carolina*, and the State Single Audit Implementation Act. Those standards, the Uniform Guidance, and the State Single Audit Implementation Act require that we plan and perform the audit to obtain reasonable assurance about whether non-compliance with the types of compliance requirements referred to above that could have a direct and material effect on a major State program occurred. An audit includes examining, on a test basis, evidence about the City of Lexington'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 on compliance for each major State program. However, our audit does not provide a legal determination of the City of Lexington's compliance.

Opinion on Each Major State Program

In our opinion, the City of Lexington complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major State programs for the year ended June 30, 2016.

Report on Internal Control Over Compliance

Management of the City of Lexington is responsible for establishing and maintaining effective internal control over compliance with the types of requirements referred to above. In planning and performing our audit, we considered the City of Lexington's internal control over compliance with the requirements that could have a direct and material effect on a major State program to determine our auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on compliance for each major State program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, non-compliance with a type of compliance requirement of a State program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material non-compliance with a type of compliance requirement of a State program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or combination of deficiencies, in internal over compliance with a type of compliance requirement of a State program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Martin Starnes & Associates, CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
Hickory, North Carolina
October 24, 2016

City of Lexington, North Carolina
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2016

Exhibit G-1

Part 1. Findings and Questioned Costs

Section I. Summary of Auditors' Results

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance to GAAP: Unmodified

Internal control over financial reporting:

Material weakness(es) identified? Yes No

Significant Deficiency(s) identified? Yes None reported

Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major federal programs:

Material weakness(es) identified? Yes No

Significant Deficiency(s) identified? Yes None reported

Type of auditor's report issued on compliance for major federal programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? Yes No

Identification of major federal programs:

<u>CFDA No(s).</u>	<u>Names of Federal Program or Cluster</u>
14.228	CDBG - State's Program and Non-Entitlement Grants in Hawaii
20.205	Highway Planning and Construction Cluster

Dollar threshold used to distinguish between Type A and Type B programs: \$ 750,000

Auditee qualified as low-risk auditee? Yes No

State Awards

Internal control over major State programs:

Material weakness(es) identified? Yes No

Significant Deficiency(s) identified? Yes None reported

Type of auditor's report issued on compliance for major State programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with the State Single Audit Implementation Act? Yes No

Identification of major State programs:

<u>Program Name</u>
Powell Bill

Continued on next page.

City of Lexington, North Carolina
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2016

Exhibit G-1
continued

Section II. Financial Statement Findings

None reported

Section III. Federal Award Findings and Questioned Costs

None reported

Section IV. State Award Findings and Questioned Costs

None reported

Part 2. Summary Schedule of Prior Year Audit Findings

None reported

City of Lexington, North Carolina
Schedule of Expenditures of Federal and State Awards
For the Year Ended June 30, 2016

Exhibit G-2

Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Grantor's Number	Federal (Direct & Pass-through) Expenditures	State Expenditures	Pass-through to Subrecipients	Local Expenditures
Federal Grants						
Cash Programs						
<i>U.S. Department of Housing and Urban Development</i>						
Passed-through N.C. Department of Commerce						
CDBG - State's Program and Non-Entitlement Grants in Hawaii						
Scattered Site Housing Program	14.228	12-C-2436	\$ 204,400	\$ -	\$ -	\$ -
Community Development Block Program/Economic Development	14.228	10-D-2672	253,597	-	-	253,597
Community Development Block Program/Economic Development	14.228	14-E-2674	750,000	-	-	750,000
<i>U.S. Department of Justice</i>						
Direct Programs						
Bulletproof Vest Partnership Program	16.607	2013BUBX13065274	1,235	-	-	1,235
Bulletproof Vest Partnership Program	16.607	2014BUBX14072639	2,249	-	-	2,249
Federal Equitable Sharing Program	16.922	NC0290100	12,479	-	-	-
Passed-through N.C. Department of Public Safety						
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2014-DJ-BX-1148	13,401	-	-	-
<i>U.S. Department of Transportation</i>						
Direct Programs						
National Infrastructure Investments Program (TIGER II Discretionary Grants)	20.933	FR-TII-0005-11-01-00	14,591	-	-	-
Passed-through N.C. Department of Transportation						
<i>Highway Planning and Construction Cluster</i>						
Highway Planning and Construction Program	20.205	C-5208	289,449	-	-	72,363
<i>Total Highway Planning and Construction Cluster</i>						
			289,449	-	-	72,363
Total assistance - federal programs			1,541,401	-	-	1,079,444

Continued on next page.

City of Lexington, North Carolina
Schedule of Expenditures of Federal and State Awards
For the Year Ended June 30, 2016

Exhibit G-2
continued

<u>Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Grantor's Number</u>	<u>Federal (Direct & Pass-through) Expenditures</u>	<u>State Expenditures</u>	<u>Pass-through to Subrecipients</u>	<u>Local Expenditures</u>
State Grants						
Cash Programs						
<i>N.C. Department of Environment and Natural Resources</i>						
Direct Program						
Parks and Recreation Trust Fund		817	\$ -	\$ 164,107	\$ -	\$ 164,107
<i>N.C. Department of Public Safety</i>						
Direct Program						
Governor's Crime Commission		PROJ011723	-	11,215	-	25,585
<i>N.C. Department of Transportation</i>						
Direct Program						
Powell Bill, DOT-4		32570	-	368,985	-	-
<i>N.C. Department of Revenue</i>						
Direct Program						
Unauthorized Substance Tax			-	60,993	-	-
Total assistance - state programs			<u>-</u>	<u>605,300</u>	<u>-</u>	<u>189,692</u>
Total assistance			<u>\$ 1,541,401</u>	<u>\$ 605,300</u>	<u>\$ -</u>	<u>\$ 1,269,136</u>

Notes to the Schedule of Expenditures of Federal and State Awards

1. Basis of Presentation

The accompanying schedule of expenditures of federal and state awards (SEFSA) includes the federal and state grant activity of the City of Lexington under the programs of the federal government and the State of North Carolina for the year ended June 30, 2016. The information in this SEFSA is presented in accordance with the requirements of Title 2 US Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards and the State Single Audit Implementation Act. Because the Schedule presents only a selected portion of the operations of the City of Lexington, it is not intended to and does not present the financial position, changes in net position, or cash flows of the City of Lexington.

Continued on next page.

City of Lexington, North Carolina
Schedule of Expenditures of Federal and State Awards
For the Year Ended June 30, 2016

Exhibit G-2
continued

2. Summary of Significant Accounting Policies

Expenditures reported in the SEFSA are reported on the modified accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

City of Lexington has elected not to use the 10-percent de minimis indirect cost rate as allowed under the Uniform Guidance.