



JANET COWELL
TREASURER

NORTH CAROLINA
DEPARTMENT OF STATE TREASURER
STATE AND LOCAL GOVERNMENT FINANCE DIVISION
AND THE LOCAL GOVERNMENT COMMISSION

T. VANCE HOLLOMAN
DEPUTY TREASURER

January 25, 2012

The Honorable Bob Davis, Chairman
Scotland County
P O Box 489
Laurinburg, North Carolina 28353

Dear Chairman Davis:

The State and Local Government Finance Division in its role as staff to the Local Government Commission has analyzed the audited financial statements of Scotland County for the fiscal year ended June 30, 2011. **The County has serious financial problems which the County's governing board must address immediately.** The Board must take corrective action in the following areas to improve your County's financial position.

In the General Fund, the percentage of fund balance available for appropriation relative to expenditures appears to be inadequate to support current operations. As of June 30, 2011, the amount of available fund balance was \$2,702,773 or 6.72% of total fund expenditures. This is a decline from the 9% held at the end of the previous year. Statewide, the average fund balance available for comparably sized units was 24.45% of their total General Fund expenditures. In addition to the demands of General Fund obligations, the General Fund reserves must support the needs of the Public Works Fund and its inability to cover its deficit. This steady decline of the General Fund's fund balance has continued since 2006 to the current level. Allowing expenditures to exceed revenues by large sums year after year is not sustainable. For cash flow purposes, local governments need to maintain adequate amounts of fund balance to finance their operations during periods of declining revenues. Also, fund balance represents a reserve that can be used for emergencies and other unexpected expenditures or to take advantage of financial opportunities that may unexpectedly arise. The County's available fund balance should not be allowed to drop below 8% of total General Fund expenditures, which is equal to one month's average expenditures. The Board should analyze its budget ordinance for the current fiscal year and determine which expenditures can be reduced and/or which revenues can be increased to begin rebuilding General Fund reserves.

The primary reason that the General Fund continued to decline in the 2011 fiscal year is that expenditures exceeded revenues by approximately \$2.3 million. The County's budget

anticipated a revenue shortfall and included an appropriation of fund balance of approximately \$1.7 million which increased through amendments to \$1.86 million at year end. However, because revenues were severely overestimated, the County actually used \$2.3 million in fund balance. Revenues were under-realized by \$3 million. The County actually did a good job of holding down expenditures to make up some of the difference. However, when it is determined that certain revenues will not be realized at the expected amount the Board should amend the budget and reduce revenue estimates and either recognize other revenue it is more sure to receive or reduce appropriations.

The Public Works Fund has multiple financial issues as well. We noted various signs of financial weakness in the Fund indicating that the landfill may not be sustainable in its current form. The Fund reported a net loss on both the full accrual and budgetary basis of reporting, indicating that revenues do not provide sufficient resources to cover the cost of providing services to your customers. Current liabilities exceeded liquid assets, indicating that the Fund may not have sufficient liquid resources to meet its current obligations. There is a deficit fund balance which should be funded immediately according to state statute. In addition, there was only \$170 of cash on hand at year end meaning that the General Fund may have to continue to provide cash flow. The Board must evaluate the performance of this Fund and make the changes necessary to improve financial operations and sustainability. The General Fund does not have the resources to sustain this fund. Rates and rate structures should be evaluated and adjusted to provide better coverage and begin covering the deficit.

We continue to note signs of financial weakness in the Water District Phase II Fund indicating that the water system may not be sustainable in its current form. The Fund reported a net loss on the full accrual basis indicating that revenues do not provide sufficient resources to cover the cost of providing services to your customers. Current liabilities exceeded liquid assets, indicating that the Fund may not have sufficient liquid resources to meet its current obligations. The fund continues to report a deficit fund balance on modified accrual of a negative \$215,645 due to the advance of funds it has received from Water District Phase. The Board must evaluate the performance of this Fund and make the changes necessary to improve financial operations and sustainability. Rates and rate structures should be evaluated and adjusted to provide coverage for at least system operating costs. In fact, if the County is to be eligible for State grant or loan funding for water system expansion or growth, the rate structure must meet certain criteria, one of which is that it provides sufficient resources to meet or exceed operating expenditures plus debt service costs.

The problem areas addressed in this letter require **immediate** corrective action. Because of the serious financial and operational problems that exist, the governing board must develop a financial plan outlining how it intends to control expenditures and operate within its available resources. Because fund balance available for appropriation in the

The Honorable Bob Davis, Chairman
Scotland County
January 25, 2012
Page 2

General Fund is less than 8% of the General Fund's annual expenditures, the governing board should develop and approve a budget amendment that recognizes any revenue sources which may be reasonably increased and/or appropriations that may be reduced in the General Fund. We know from our review of your original 2011-2012 budget ordinance that fund balance was not appropriated in the General Fund in the original version of the budget. Please forward copies of any budget amendments that have been made since the original budget was adopted. Please also include a copy of your most recent interim financial reports as well. A copy of the corrective action plan addressing the items discussed in this letter should be signed by each member of the governing board and submitted to our office within 30 days of receipt of this letter. Our staff is available to help you develop your plan if you require assistance. If you have any questions, please contact me at 919-807-2380.

Sincerely,



Sharon G. Edmundson, CPA
Director, Fiscal Management Section

cc: Joyce McDow, Vice Chairperson
John T. Alford, Commissioner
Guy McCook, Commissioner
Carol McCall, Commissioner
John Cooley, Commissioner
Clarence McPhatter, II, Commissioner
Kevin G. Patterson, County Manager
Charles D. Nichols, Finance Officer
Gustaf C. Lundin & Company, LLP