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Board of Finance of the
City Council
City of Burlington
Burlington, Vermont 05401

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This letter is in response to your questions related to the Larkin report (Larkin). This letter includes the questions and our original responses from our letter dated February 7, 2011 with some additional clarification where it was requested and three (3) new questions from after that date.

- Question 1. In the FY07 Management Letter you wrote and dated June 26, 2008, you note only two deficiency under "Accounting Issues," that being "Telecom Fund Salary Allocations" and "Telecom Fund Indebtedness (page 14 and 15) and then under "Telecom Fund", you note three deficiencies, "Capitalization of Service Calls" "Revenue Assurance Auditing," and "Certificate of Public Good Compliance." (Page 19) Did you discuss these deficiencies with the CAO, his staff or BT management in early 2008? If so, what was the response since there is no reference to these items in the City's response to your Management Letter? If you noted that there was no compliance mechanism, you must have seen and been aware of the CPG in 2007-2008. Is that correct? Did you at that time know the City was not in compliance?
- Question 2. Given that you have been the City's Auditor for some time, were you surprised to read in the Larkin Report that BT has not been in compliance with Condition 60 since 2005 (with some gaps when the Koch money and later the CitiCapital money came in?) Was this something you were aware of? If so, did you alert anyone in the City of this and when?
- Question 3. The Larkin Report notes workpaper PP1203 dated January 2008, "cash in pooled account is very negative which (is) a violation of the CPG. No current plans to fund this negative." Can you please explain who from the City you discussed this with and if you did not discuss this with someone, why not?

- Question 5. In FY08's Management Letter dated June 26, 2009, you noted on page 30, the need for a legal opinion on Use of Pooled Cash. Is there a reason why this was not noted as a deficiency in your FY07 Letter dated June 26, 2008 since it appears that since you cited the CPG compliance, it would seem that there must have been concerns about a legal opinion on the use of pooled cash?
- Question 11. On page 27 of the Report, Larkin says that a review of your workpapers for FY07, 08 and 09 shows that you were very concerned about the negative pooled cash position and "the need for BT to have a plan to pay back the negative pooled cash was a significant financial consideration." Would you agree with this statement and did you consider at any time letting the Board of Audit know of your concern?
- Question 12. There are a number of comments taken from your workpapers during the FY08 audit done in 2009. These are highlighted on pages 28 to 36 of the Larkin Report. It seems that you were very concerned about the negative balance and brought those to the attention of the City in 2008 and again in 2009 and 2010. Is that the case?

Response to Questions 1, 2, 3, 5, 11 and 12:

As stated in our contract for services with the City, our responsibility, as described by professional standards, is to express opinions about whether the financial statements prepared or approved by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

We conducted our audits 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 misstatement.

In planning and performing our audit, we considered the City of Burlington, Vermont's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting.

Also, as part of obtaining reasonable assurance about whether the City of Burlington, Vermont's financial statements are free of material misstatement, we are required to determine it's compliance with any provisions of laws, regulations, contracts, and grants that could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions is not an objective of our audit.

Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement. We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

We performed the audits according to the standards as previously communicated to and agreed to by you in our engagement letter.

Two of many specific concerns we had to address as part of our audit of Burlington Telecom (Telecom) were the City's possible violation of the CPG and the ability of Burlington Telecom to replenish the negative balance in the City's pooled cash account.

The Larkin report notes that in a workpaper referenced PP1203 dated January, 2008 and titled "Telecom Planning" that there is a comment that says "Cash in pooled account is very negative which a violation of the CPG is. No current plans to fund this negative". Unfortunately and inaccurately, Larkin chose to add the word "is" before the words "a violation". This was not our intent at this point in the audit. As titled, this is a planning document that was prepared as we began our audit of Telecom.

The comment referenced to by Larkin was included in a list of a number of items that we needed to follow up on or to ask City staff about. There are no conclusions in this workpaper as it is a checklist of planning issues we may need to address in order for us to fulfill our contractual responsibilities under generally accepted auditing standards.

Our first task, as described by professional standards, was to determine if any non-compliance with the CPG could have a direct and material effect on the determination of financial statement amounts. This inquiry was in regards to any and all violations of the CPG from a direct and material financial statement impact. We were not aware that the violation of any specific condition could result in a different amount of financial penalties being imposed.

After discussion with Telecom staff and subsequent confirmation by the City's attorneys, it was believed that the Department of Public Service would not impose fines on the City as this would only have the impact of penalizing the ratepayers. In fact, to date, the Department has not imposed any fines. In addition, we have been informed by the City's attorneys that there are statutory maximum fines for each material violation, which, assuming no further violations are found, could be \$80,000. Even if the maximum fines were imposed, this is not material to Telecom's financial statements and, therefore, we did not need to address this issue again. As it was determined that the violation of the CPG could not have a direct and material effect on the determination of any financial statement amount, we did not need to determine whether the City was, in fact, in violation of the CPG. If we had needed this determination, we would have consulted with the City's attorneys as this is a legal, not an accounting issue.

However, through our inquiries of Telecom staff during the audit as of June 30, 2007, it appeared the City did not have a system to monitor and document compliance. We included this other recommendation in our management letter as of June 30, 2007 and repeated it in our 2008 and 2009 management letters as well.

The more critical issue was Telecom's ability to replenish the negative balance in the City's "pooled" cash account. It was our responsibility to evaluate the City's assertion related to their ability and intent to replenish the account.

For the audits as of June 30, 2005 and 2006, the Telecom Fund had net positive cash balances.

For the audit as of June 30, 2007, as was indicated in that same planning workpaper PP1203, the City refinanced its debt and received more than an additional eleven million dollars subsequent to the end of that year. For the audit as of June 30, 2008, the City again asserted that it had the ability and intent to replenish the pooled cash account. Since there was no subsequent refinancing, we asked the City to specifically confirm that to us, which they did, and we also received a confirmation from Municipal Leasing Consultants, who has placed a number of City leases over the past few years, that they were confident they could secure financing for the project.

For the audit as of June 30, 2009, since the City had rejected the Piper Jaffrey proposal, the City was not able to assert that it had the ability to replenish the pooled cash account. As a result of this, we had to qualify our opinion on the financial statements related to this issue. This is not the result of the violations of the CPG but rather that generally accepted accounting principles require the City to determine if it can repay any due to other funds balance within a reasonable period of time. After consultation with the Governmental Accounting Standards Board, reasonable period can be as long as the useful life of the project being financed. As a result of this, it wasn't until the City rejected the Piper Jaffrey proposal, and was not actively pursuing alternative financing, that it became, and continues to be, unclear as to how or when Burlington Telecom can replenish the pooled cash deficit.

In addition, during our discussion with the CAO related to the City's ability and intent to replenish the pooled cash account for the 2008 audit, he asked that we provide him with a list of any concerns we had and what the accounting implications would be if Telecom cannot replenish the pooled cash account. We provided that letter dated April 3, 2009. As a result of our concern in the letter related to the pooled cash account, we believe he indicated there is some question as to the reimbursement requirements. As a result, we included an other recommendation in the June 30, 2008 management letter that the City obtain a legal determination related to this issue.

We believe the preceding paragraphs address a number of your questions. Once we had the two concerns resolved, we did not need to address them further as it would not be germane to our responsibilities in our contract for services and under generally accepted auditing standards. There may be other agreed upon procedures you would like us to perform, but these are beyond the scope of our current engagement and would have no impact on our opinion on the financial statements.

In regards to your question related to why there was no response to certain of the issues in the management letter, none of the items mentioned in your Question 1 were characterized as deficiencies in internal control but rather as other recommendations. Because of this, there was no requirement that the City respond to any of those issues. The City is now responding to all management letter points.

We met with Christopher Burns, Amber Thibeault and John Van Vught annually during our fieldwork for the Telecom audit including during the June 30, 2007 and 2008 audits. During at least one of our meetings during the June 30, 2007 audit, which would have occurred either at the planning stage of the audit in January 2008 or when Telecom was completely ready for audit when we completed the bulk of the fieldwork in May 2008, we specifically discussed the CPG. We do not have any documentation that they specifically informed us about any violation of condition 60.

We did discuss that they did not have any system to monitor compliance with any of the provisions of the CPG. We would not have known that Telecom had no system to monitor its compliance with the CPG unless we had asked. No one has ever disputed this and this point was included in the management letter for three years in a row until it was finally implemented during fiscal year 2010. We do not know why the City did not implement this recommendation when it was first raised.

We would also have discussed all of the other issues that ended up in the management letter during the course of our fieldwork. This would be true for subsequent years as well. If Telecom staff were aware that they were in violation of condition 60, we have no indication that they informed us of that.

We always issue a draft of our management letters to every one of our clients with the instructions to read them carefully to verify the accuracy of each point. When we did this for the June 30, 2008 management letter, no revisions or clarifications were requested related to our management letter point requesting that the City seek a legal opinion regarding the use of pooled cash. It is routine for the City to request us to correct any inaccuracies or add clarification to our comments as they tend to treat the management letter as a report card although it is not intended for that purpose. We are always happy to make any corrections needed or to add clarification as we want this document to be useful to the users and because we know that the management letter will be circulated and read by State and Federal grantors and by anyone who requests it because it becomes a public document on release.

However, in a response to that management letter dated October 27, 2009, almost three months after that management letter had been released, the City did not say a legal opinion was not needed but did indicate that, "The City has filed for temporary relief from this requirement and is engaged in refinancing Telecom to cure the non-compliance."

We would not have included that request for a legal opinion in our management letter if the City had indicated to us that they had already acknowledged that noncompliance. There would have been no need for that. We cannot explain why we were not advised of this prior to our release of the management letter.

As indicated in our original response, at June 30, 2006, the Telecom fund had net positive cash and, at June 30, 2007, the City had refinanced its debt within sixty days after year end and, therefore, had sufficient cash to replenish the pooled cash deficit within the required sixty day period. If the City did not replenish the pooled cash deficit at that time, it may be that the City did not draw on the available cash in a timely manner. There was sufficient cash within sixty days of each of those year ends to replenish the pooled cash deficit.

However, at June 30, 2008, the City did not have sufficient cash at that date or through subsequent refinancing to eliminate the pooled cash deficit. Because of that, we required the City to assert to us, in writing, in the letter of representation dated June 26, 2009 signed by both Finance and Telecom staff, that "Financing is available for Burlington Telecom so that the negative pooled cash will be repaid to the City."

We also received written confirmation from the City's financing consultant in a letter dated June 12, 2009 that indicated, "This is to confirm that the City of Burlington has engaged Municipal Leasing Consultants for a lease purchase financing for Burlington Telecom's Fiber Optic Project. We are confident we can secure financing for this project."

Even after receiving that assurance, we still encouraged the City to include a footnote in the June 30, 2008 audit, which they agreed to, which read, "Burlington Telecom has negative pooled cash in the amount of \$8,654,981 at June 30, 2008. Subsequent to year-end, that negative balance has increased substantially. The City intends to refinance its debt to include paying back the other City funds. The City believes it has the ability to do this, however, if this does not happen, it could have an adverse impact on the City's cash flow and on the classification of the negative cash resulting in a significant reduction in the City's General Fund fund balance."

We felt that, in spite of the confidence of the City and their financing consultant, the City had an obligation to warn any reader including the Board of Finance and City Council that if, for whatever reason, the refinancing did not happen, it could have a significant adverse impact on the City's General Fund's fund balance.

One thing that's important to remember is that, through all of this, with all that we now know, all of your financial statements and our independent auditors' opinion on them, as they were originally issued, are still accurate. There are no changes that would have been required even if we had all the information that we have today.

Question 4. The Larkin Report found that "BT's accounting records understated the amount of BT's monthly balance in the Pooled Cash account on numerous occasions because of its failure to record in a timely manner cost that it was incurring" (page 9 of Report) thereby distorting what was really owed to pooled cash. Do you agree with this statement? If you do agree, please cite where it is in your Management Letter for FY08 dated June 26, 2009.

Response to Question 4:

The Larkin report indicates that the accounting records have understated the amount of Telecom's monthly balance in the pooled cash account on numerous occasions because of its failure to record in a timely manner costs it was incurring. Our audits are on the financial statements as of the end of each fiscal year. The balances we audited had all the activity recorded. If the balances were inaccurate during the year, the only financial statement impact would be on the calculation of interest charged on the pooled cash deficit but these differences would not be material to the financial statements.

Without auditing month end balances, we do not know if Larkin's statement is accurate, and therefore, we would have had no basis to include this as a management letter comment.

Question 6: On page 11 of the Larkin Report, "Evidence shows that the auditors informed the City of the violation (of Condition 60) prior to November 2008. Moreover, this practice of improper use of the City's pooled cash fund by BT not only violates Condition 60, it places the General Fund and the taxpayers of Burlington at risk." Do you agree with this from a factual point of view?

Response to Question 6:

The Larkin report also indicates that the "... improper use of the City's pooled cash fund by BT not only violates Condition 60, it places the General Fund and the taxpayers of Burlington at risk".

Because of the current uncertainty related to how much or when Telecom can repay the pooled cash deficit, it appears it has, however, we do not know what other alternatives the City had at that point in time. As discussed previously, refinancing the debt may have replenished the pooled cash account but without knowing the terms and conditions of that debt, we could not evaluate whether the taxpayers would still be at risk. Alternatively, the City could have halted construction and/or operation of the Telecom system but may still have been responsible for costs and contractual commitments to date.

As we indicated, we do not know what evidence Larkin is referring to that shows that we informed the City of the violation of condition 60 prior to November 2008. In fact, we believe, because we were asking the City as late as August 2009, when the management letter was released, to obtain a legal opinion on whether or not the use of pooled cash is a violation of the CPG is evidence we were not certain even at that date.

Question 7. On page 13 of the Larkin Report, "Larkin attempted to determine through discovery the amount BT actually borrowed from the City. This determination was complicated by the City's unconventional accounting practices...The general ledgers provided showed only year end balances but did not show year to date balances by month as would be expected in a commercial venture with reasonable and appropriate accounting practices." Would you agree that the City's accounting practices are unconventional or do you feel otherwise?

Response to Question 7:

The Larkin report also indicates, "Larkin attempted to determine through discovery the amount Burlington Telecom actually borrowed from the City. This determination was complicated by the City's unconventional accounting practices... The general ledgers provided showed only year end balances but did not show year to date balances by month as would be expected in a commercial venture with reasonable and appropriate accounting practices". Unfortunately, this statement is inaccurate. The City provides us read only access to the accounting system and we routinely print the reports described by Larkin with monthly balances. We were not asked about this or any other specific accounting issues referred to in the report by Larkin. We do not believe Larkin distributed a draft of their report before it was issued. This would have helped to eliminate any inaccurate statements in the report.

Question 8: Do you agree with the City's practice of Period 13 accounting and have you seen this before?

Response to Question 8:

In response to your question related to period 13 accounting, we know this is a standard feature of the City's Pentamotion software. If used as intended, for year end accruals and adjustments, it has no impact on the year end balances we are provided or our ability to audit them.

Question 9: On page 14 of the Report, it states "The fact that the City is charging interest on the funds owed by BT is a clear indication that the advance constitutes a loan." Would you classify the funds owed as a loan and if so, would it seem to make sense that there should have been some sort of paper trail with typical loan-type paperwork?

Response to Question 9:

The Larkin report also indicates, "The fact that the City is charging interest on the funds owed by BT is a clear indication that the advance constitutes a loan". The City charges or credits other funds of the City who participate in the pooled cash account with interest. This is a standard practice in many municipalities. There is virtually no distinction between a due to/from and an interfund loan other than repayment terms.

It is not typical to have loan type paperwork for a due to other funds liability as the liability is to the same legal entity, the City of Burlington.

Question 10: From your review of the City's and BT's books would you agree that it "cannot be readily determined how much of the \$16.9 million is borrowed and how much is interest?"
(Page 19 of the Report.)

Response to Question 10:

The Larkin report also indicates it "cannot be readily determined how much of the \$16.9 million is borrowed and how much is interest?" The amount of interest charged can be readily determined by the general ledger detail or the pooled cash interest spreadsheets. Every fund that has positive balances has been credited with their interest earnings. We are not sure what Larkin is referring to with this statement.

Question 13: In the Letter of Representation dated June 26, 2009, the City states that "There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices." Do you think that statement is accurate?

Response to Question 13:

As to the statement, in the Letter of Representation dated June 26, 2009, the City states that, "There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices". We are not aware of any communications related to deficiencies in financial reporting practices as of that date; however, it is possible that there was a communication that was not provided to us.

Question 14: In conclusion, do you agree with the conclusions on page 49 of the Larkin Report with regard to Condition 60?

Response to Question 14:

As to Larkin's conclusions regarding condition 60, Larkin indicates that their "... opinion is based on our (Larkin's) interpretation of what Condition No. 60 states". We do not know what their interpretation is or if it coincides with that of the City or the Department of Public Service. As indicated previously, we are not attorneys and do not provide legal interpretations.

Question 15: With regard to its accounting issues as noted on page 50 of the Larkin Report?

Response to Question 15:

As to Larkin's conclusions related to the accounting issues, as indicated previously, some of their criticisms are inaccurate. Others are speculative with very few specific examples to respond to. We would need more information to be able to respond fairly.

Question 16: And lastly, if the City had done a separate and independent audit of BT for FY09, what would the opinion letter to that audit have said with regard to BT as a going concern and with regard to the \$16.9 million debit to pooled cash?

Response to Question 16:

And lastly, the City has contracted with us to prepare a separate audit report for Telecom as of June 30, 2010 and, therefore, we did need to determine if going concern was an issue that had to be addressed. After consultation with the Governmental Accounting Standards Board, it was determined that going concern is a concept at the entity level only and, in fact, the standards specifically indicate we should not address it at the fund or department level.

Therefore, if the City had requested a separate audit report for Telecom as of June 30, 2009, the opinion would have been exactly the same as our opinion on the separate audit report we just issued for Telecom as of June 30, 2010.

Question 17: It is a mystery to me, why, if the audit and all communications are addressed to the Board of Finance and the Mayor, you did not feel a responsibility to notify the Board of Finance. Could you please comment on this.

Response to Question 17:

We do not know what you are asking in Question 17. You are correct that all our reports are addressed to the Mayor and City Council or Board of Finance, so what is your question? We met all our contractual and professional responsibilities. All of your financial statements and our independent auditors' opinions on them, as they were originally issued, are still accurate. There are no changes that would have been required even if we had all the information that we have today. We don't know what specific responsibility you are referring to.

Follow Up to

Question 17: With regard to question 17, you stated that you had conversations with the CAO in 2008 about the debit to pooled cash. To the best of my knowledge you did not meet with nor discuss the audit with the Board of Finance or the City Council at all since the Kiss administration came into office in 2006. My question is once you discussed with anyone at BT or with the CAO the concerns you had with respect to BT regarding either the debit to pooled cash (which you or someone on your staff must have noted in late 2008 since the debit was an issue for you as of June 30, 2008), why you did not feel you needed to notify the Mayor, the City Council and the Board of Finance. Also it appears you discussed CPG and pooled cash issues in the winter of 2008 with the CAO.

Response to Follow Up to Question 17:

First, based on the date of our letter to the CAO, April 3, 2009, we presume we had a discussion in the spring of 2009, not the winter of 2008. Second, the CAO is a member of the Board of Finance. We had no reason to believe that these issues were not known by the Board of Finance. Third, the Mayor, City Council and the Board of Finance were informed of these issues as described previously in this letter through a footnote in the June 30, 2008 audit and a separate recommendation to get a legal opinion whether the City's use of the pooled cash was a violation of the CPG.

Question 18: You stated that in "June 30, 2007, the City had refinanced its debt within sixty days after year end and, therefore, had sufficient cash to replenish the pooled cash deficit within the sixty day period". This would indicate that in early 2008, you knew that about the 60 day rule in Condition 60 of the CPG. In order to ascertain if there was sufficient cash, you needed to know why this would be important. Did you discuss this with anyone?

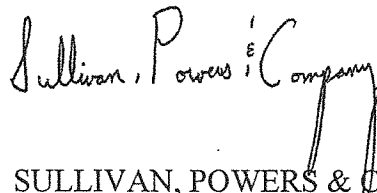
Question 19: It would seem that the timing of the Citi Leasing deal was indeed fortuitous given the sixty day rule. If the financing had been lined up for a closing in September 2007, more than sixty days after June 30, 2007, the pooled cash issue would have come to the full light of day much sooner. Would you agree or am I mistaken?

Response to Questions 18 and 19:

Questions 18 and 19 are both based on false inferences and, therefore, cannot be directly answered. As we indicated on page 4 in paragraphs 2 and 4, our responsibility was to determine if the City had the ability to replenish its pooled cash deficit which they demonstrated by the subsequent refinancing, regardless of when it happened. That was what our responsibility was and we did it. We cannot speculate or answer any other way.

We hope now, after we have publicly met with the Board of Finance to answer their questions and have added the requested clarification in this letter, that you recognize that we have been responsive to your requests. We understand that this process has been complicated by questions that were raised as a result of false inferences that were included in the Larkin Report.

Respectfully submitted,



SULLIVAN, POWERS & CO.
Certified Public Accountants

