

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

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

October 26, 2009

To the Honorable Mayor and
Members of Town Council
Town of Chapel Hill, North Carolina

We have audited the basic financial statements of the Town of Chapel Hill, North Carolina for the year ended June 30, 2009, and have issued our report thereon dated October 26, 2009. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility under U.S. Generally Accepted Auditing Standards and OMB Circular A-133

As stated in our engagement letter, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance about whether the basic financial statements are free of material misstatement and are fairly presented in accordance with U.S. generally accepted accounting standards. Because an audit is designed to provide reasonable, but not absolute assurance, and because we did not perform a detailed examination of all transactions, there is a risk that material errors, fraud, or other illegal acts may exist and not be detected by us.

In planning and performing our audit, we considered the Town of Chapel Hill, North Carolina's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal or state program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

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As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the Town of Chapel Hill, North Carolina's compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, the objective of our audit was not to provide an opinion on compliance with those provisions. Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the Town's compliance with the type of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each of its major federal and state programs for the purpose of expressing an opinion on the Town's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the Town's compliance with those requirements.

Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Town of Chapel Hill, North Carolina are described in Note 1 to the basic financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the 2008-2009 fiscal year. We noted no transactions entered into by the Town of Chapel Hill, North Carolina during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the basic financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the basic financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most significant estimates affecting the financial statements were the allowance for doubtful accounts.

Management's estimate of the allowance for doubtful accounts is based on historical loss levels and an analysis of the collectibility of individual accounts. We evaluated the key factors and assumptions used to develop the allowance in determining that it is reasonable in relation to the financial statements taken as a whole.

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Audit Adjustments

For purposes of this letter, professional standards define a significant audit adjustment as a proposed correction of the basic financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the Town's financial reporting process (that is, cause future financial statements to be materially misstated).

There were no uncorrected misstatements of the financial statements.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the basic financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's basic financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management prior to retention as the Town of Chapel Hill, North Carolina's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

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Difficulties Encountered in Performing the Audit

We did not encounter any significant difficulties in dealing with management in performing our audit.

Independence

Amendment No. 3, Independence, to Government Auditing Standards requires that an audit firm document an understanding with the audited entity regarding the objectives of nonaudit services. As part of our audit, we did not perform any nonaudit services.

This information is intended solely for the use of the Members of Town Council and management of the Town of Chapel Hill, North Carolina and should not be used by anyone other than these specified parties.

Martin Starnes & Associates, CPAs, P.A.

Martin Starnes & Associates, CPAs, P.A.
Hickory, NC