

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

2013-001 The City lacks adequate internal controls over payments to ensure compliance with state laws and City policies and procedures to safeguard public funds.

Description of Condition

In 2013, the City spent \$1,402,541 on items such as equipment, supplies, petty cash reimbursements and monthly credit card bills for travel and miscellaneous expenses. In the two prior audits, we reported disbursement internal control weaknesses to management. The City has since taken steps to update its municipal code which implemented new purchasing procedures; however, the City has not addressed the following:

- The Mayor or City Council does not approve all purchases prior to incurring the expense as outlined in the Gold Bar Municipal Code (GBMC).
- The City purchases ongoing computer services without a written contract.
- Beginning in 2014, the interim Treasurer returned to perform financial services. However, a new contract was not in place for these services.
- The City keeps its procurement and fuel cards in a locked location; however, the cards are accessible by all City employees on a self-check-out basis using a logbook. Further, the City maintains its fuel cards in envelopes with the PIN access numbers written on each envelope.
- The City updated its municipal code to require monthly replenishment of its petty cash account; however, only one reimbursement was made to replenish the petty cash fund since April 2014. Further, we reviewed the expenditure report for 2013 and found the City had replenished the Petty Cash fund only three times (June, September and December).

Cause of Condition

The City updated its municipal code to align with its current practices; however, the City is not following the procedures outlined in the new code.

Additionally, the City relies on the Finance Committee, composed of two citizens and a Council Member, to review all payments prior to Council approval. This

review process does not ensure expenses are supported in compliance with City code and policies or approved as required.

Effect of Condition

By not following City policies or having effective internal controls, the City cannot be sure public funds are adequately safeguarded. Specifically, City funds could be spent for goods, services, and travel that do not meet City management's financial goals and objectives. Specifically, we found:

- Out of 23 disbursements selected for testing, nine did not have proof of prior approval of either the Council or Mayor as required by City policy and Gold Bar Municipal Code (GBMC) 3.08.010 and 3.08.020. Further, no purchase orders were prepared.
- Two payments made to the Internal Revenue Service (IRS) totaling \$2,321 for interest, late payment fees and failure to file W-2s. By not following IRS rules, the City was required to spend its resources on interest and penalties that could have been used to purchase goods and services. The City has since properly filed all W-2s.
- One \$54 payment to a customer for an over payment. This expenditure did not receive approval from the Council or the Mayor.
- Two instances where the check register did not include approval signatures of all Finance Committee members and Council as required by City policy.
- A \$5,000 imprest fund which has not been approved by Council through a resolution.

In addition, our audit found risk that procurement cards, fuel cards, and petty cash could be misused or misappropriated and not be detected in a timely manner by City management.

Recommendation

We continue to recommend the City evaluate all of its policies and procedures over financial operations to ensure that policies align with the vision of the City and procedures are adequate to ensure compliance and safeguarding of public resources. Specifically, the City should:

- Comply with City codes and policies regarding payments and travel.

- Ensure all professional services procured by the City are supported by written contracts.
- Safeguard procurement and fuel cards, and petty cash.
- Replenish petty cash monthly to the authorized balance, or officially reduce the authorized amount by ordinance, as required.

City's Response

With regard to the statement “. . . Mayor or City Council does not approve all purchases prior to incurring the expense . . .” For 2013, we were not able to correct the deficiency noted in the 2012 audit as those recommendations were delivered by the State Auditor’s Office during the exit conference held in early 2014. Since those recommendations were made, the GBMC was changed removing the requirements for purchase orders and the purchase authorization limits were adjusted, providing greater flexibility to the staff.

With regard to travel request forms, the travel and training policy is in the process of being updated to correct this deficiency.

With regard to computer and financial services contracts, the City is in the process of reviewing the process for obtaining services. It should be noted that the contract for financial services expired on December 31, 2013, which is the period encompassed by this audit. The contract was not renewed until it became obvious that the services would be required through 2015.

With regard to the procurement and fuel cards, the State Auditor’s Office noted that they were in a locked location, which was the recommendation from 2012. Included in the same recommendation was a request to keep the fuel card pin numbers in a location separate from the physical cards themselves. The Mayor and City Council concluded that that action would put an onerous constraint on access to the cards by City staff, particularly during emergencies. The fuel cards were designed to be issued to staff members and the pin numbers were their personal pin numbers. When the City had a misuse of the fuel cards in 2008, the Mayor, with the concurrence of the State Auditor’s Office, placed them all under the custody of the Clerk-Treasurer; defeating the card’s security system. The Auditor’s recommendation still poses an onerous constraint on the efficient operations of the City, particularly during emergencies. The City has the same ability to detect in a timely manner any abuse of the use of procurement and fuel cards that it had before, when the cards were assigned to the employees (See discussion on Finance Committee below). In the eyes of the Auditor, identification of the abusing individual may be more difficult since it is a self-checkout, honor system but, with only three employees needing access to the

cards/pin numbers, a thorough investigation will identify the individual responsible in an expeditious manner.

With regard to the petty cash reimbursement, the availability of procurement cards has reduced but not eliminated the need for petty cash. The petty cash fund is in the hands of a single custodian who is responsible for reimbursing expenditures. It is under double lock and key. The revision of the GBMC in 2014 was done without consideration to the cost of monthly replenishments in relation to the amounts being dispersed. The GBMC will be revised to correct this situation in 2015.

With regard to the Finance Committee, this committee was appointed by the Mayor to act as an independent review group, with no authority to reject payments, for the Mayor and City Council. They ascertain that all vouchers are prepared, with supporting documentation, and noted on the Check Register before going to the Council for approval.

Per GBMC 3.04.020 - Issuance of warrants and checks—Procedure—Auditing officer:

B. Auditing Officer. For the purposes of RCW Chapter 42.24, city staff shall also be the auditing officers without the necessity of a separate appointment.

By practice, each staff member acts as an auditing officer, in accordance with GBMC 3.04.020 (B), verifying that the “expenses are supported in compliance with City code and policies or approved as required.” The final auditing officer is the Clerk-treasurer who prepares each voucher and check, also reviewing each transaction to verify that the “expenses are supported in compliance with City code and policies or approved as required.” The point of disagreement is that signatures are inconsistent and lacking for the State Auditors to absolutely verify compliance. In other words, the City has multiple verifications that the transactions are in compliance. The understaffed city of Gold Bar probably has more checks by designated auditing officers than the city of Everett or any other large entity.

Auditor’s Remarks

We thank the City for its cooperation and assistance during the audit. We will review the corrective action taken during our next regular audit.

Applicable Laws and Regulations

RCW 43.09.200 Local government accounting – Uniform system of accounting.

The state auditor shall formulate, prescribe, and install a system of accounting and reporting for all local governments, which shall be uniform for every public institution, and every public office, and every public account of the same class.

The system shall exhibit true accounts and detailed statements of funds collected, received, and expended for account of the public for any purpose whatever, and by all public officers, employees, or other persons.

The accounts shall show the receipt, use, and disposition of all public property, and the income, if any, derived therefrom; all sources of public income, and the amounts due and received from each source; all receipts, vouchers, and other documents kept, or required to be kept, necessary to isolate and prove the validity of every transaction; all statements and reports made or required to be made, for the internal administration of the office to which they pertain; and all reports published or required to be published, for the information of the people regarding any and all details of the financial administration of public affairs.

Budget Accounting and Reporting System Manual, Accounting, Accounting Principles and General Procedures:

Management and the governing body are responsible for the government's performance, compliance and financial reporting. Therefore, the adequacy of internal control to provide reasonable assurance of achieving these objectives is also the responsibility of management and the governing body. The governing body has ultimate responsibility for ensuring adequate controls to achieve objectives, even though primary responsibility has been delegated to management. Since management and the governing body are assumed to work in harmony, both parties are collectively referred to as "management" throughout the rest of this section.

Internal control should be viewed as an integral or inherent part of the policies, systems and procedures management uses to operate and oversee the organization. This is not to say effective control will never require additional or incremental effort. Rather, controls exist to provide reasonable assurance about the achievement of objectives and so should be integrated into all the organization's fundamental business processes. Controls are normally most

effective when built into the government's infrastructure rather than being treated as supplemental or separate processes. In the same way, implementation and monitoring of internal controls should not be viewed as a singular event, but rather a continuous or iterative process.

Since internal control is as fundamental as the objectives the controls relate to, the need for effective control is applicable to all organizations, regardless of size. While small entities may implement internal controls differently than larger ones, effective internal control is still both necessary and possible.

RCW 42.24.080 - Municipal corporations and political subdivisions - Claims against for contractual purposes - Auditing and payment - Forms - Authentication and certification, states in part:

- (1) All claims presented against any county, city, district or other municipal corporation or political subdivision by persons furnishing materials, rendering services or performing labor, or for any other contractual purpose, shall be audited, before payment, by an auditing officer elected or appointed pursuant to statute or, in the absence of statute, an appropriate charter provision, ordinance or resolution of the municipal corporation or political subdivision. Such claims shall be prepared for audit and payment on a form and in the manner prescribed by the state auditor. The form shall provide for the authentication and certification by such auditing officer that the materials have been furnished, the services rendered, the labor performed as described, or that any advance payment is due and payable pursuant to a contract or is available as an option for full or partial fulfillment of a contractual obligation, and that the claim is a just, due and unpaid obligation against the municipal corporation or political subdivision. No claim shall be paid without such authentication and certification.

City of Gold Bar Municipal Code Chapter 3.04 states in part:

- 3.04.020 Issuance of warrants and checks - Procedure - Auditing officer.

C. Payment Procedure.

1. Warrants or checks in payment of claims or payroll shall not be issued until and after the auditing officer and the

mayor have complied with the contracting, hiring, purchasing and disbursement policies of the city council that implement internal control.

2. At the next regularly scheduled public meeting of the city council, following the issuance of any warrants or checks issued pursuant to this section, the city council shall be presented with the documentation supporting the payment of the claims.
3. The city council shall approve or disapprove all claims paid pursuant to this section and if, upon review, it disapproves some claims, the council must show reasonable cause and render a solution at the time of rejection in order for the city to meet its financial obligations. Once the auditing officer and mayor meet the requirements of the council's solution and the claim is paid, the council will then receive proof of the solution and payment at the following council meeting.

City of Gold Bar Municipal Code Chapter 3.08 states in part:

- 3.08.010 – Expenditure of funds below five hundred dollars.
- Any purchase of supplies, material, equipment or services, except wages for city employees and contract services, when the costs are less than five hundred dollars (\$500.00), excluding tax, may be made by the mayor without council approval; provided, that the purchase is within the department's associated fund's budget and the mayor first obtains a purchase order from the city clerk, which shall not be issued unless sufficient funds are available to cover the purchase.
- For the purposes of this chapter, a purchase may not be broken down into separate items, each less than five hundred dollars (\$500.00) for the purpose of avoiding the requirements of Section 3.08.020. A purchase, no matter how many parts or segments it may consist of, shall be deemed a single purchase when the whole purchase is for a single purpose.
- 3.08.020 - Expenditure of funds of one thousand dollars or more.

- Any purchase of supplies, material, equipment or services except wages for city employees and contract services where the cost thereof is one thousand dollars (\$1000.00) or more, excluding tax, shall not be made by the mayor, or anyone else on behalf of the city, unless the expenditure is first approved by the city council or the expenditure meets the emergency provisions of Section 3.08.030. Provided, however, the mayor may authorize noncapital expenditures from five hundred dollars (\$500.00) to two thousand dollars (\$2,000.00) for items pre-approved in the city's budget. All capital expenditures over one thousand dollars (\$1000.00) shall still require council approval.

City of Gold Bar Municipal Code Chapter 3.36:

- 3.36.010 - Fund created.

There is established and created a fund in the finances of the city to be designated as the "petty cash and change revolving fund" for the purpose of paying for purchases of small items, supplies and other expenses of a minor nature incurred for the city in connection with official business of the city, and for making change for cash payments received by the city.

- 3.36.020 - Custodian.

The custodian of the petty cash and change revolving fund shall be the city treasurer. In order to accomplish audit objectives of segregation of duties for internal control, the mayor or his/her designated officer shall periodically review the petty cash account.

- 3.36.030 - Accounts established.

The city treasurer is authorized and directed to establish the fund at an aggregate total of five hundred dollars (\$500.00) by issuance of a check. The money in this account is not intended to be a budgetary item as such, but to be in the nature of a revolving account for expenditures of a minor nature, which are chargeable to various departments and funds of the city and for making change.

- 3.36.040 - Expenditures.

A. The change revolving account will consist of two hundred dollars (\$200.00) and shall be used only for the purpose of making change for moneys received during the course of business. The petty cash account will consist of three hundred dollars (\$300.00), the maximum disbursement at any one (1) time shall not exceed fifty dollars (\$50.00). Each disbursement from the fund shall be supported by a receipt showing the date, recipient, purpose and amount of each cash disbursement. Reimbursements to the petty cash account should be made at least monthly, and reimbursement vouchers shall have receipts attached thereto. The custodian shall maintain suitable records, showing the expenditures incurred and the departments and funds of the city chargeable for such expenditures.

B. The fund may not be used for personal use or personal cash advances secured by check or other IOU's and any use of the fund for other than expenditures incurred in connection with official city business shall be considered a misappropriation of public funds. Upon termination of the fund, all moneys remaining shall be returned to the city's general fund.

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

2013-002 The City’s financial condition puts it at risk of not being able to meet financial needs.

Background

During the prior three audits, we communicated financial condition concerns to the City. Although the City has taken steps to reduce expenses by decreasing expenditures and staff size, its financial condition has declined for the past several years. The City did not establish a formal financial plan to address cash flow issues, as recommended in our prior audits.

Description of Condition

Financial Position

The City’s General Fund ending cash balance declined significantly from 2009 to 2013:

Fiscal Year	General Fund Ending Balance
2009	\$ 351,028
2010	\$ 59,955
2011	\$ 60,113
2012	\$ 29,909
2013	\$ 141,253

General Fund operating expenditures exceeded revenues in three of the last five years:

	2009	2010	2011	2012	2013
Revenues	\$614,556	\$619,144	\$614,145	\$583,513	\$608,500
Expenditures	\$772,591	\$910,223	\$613,987	\$684,966	\$479,459
Excess/(Deficit)	\$(158,035)	\$(291,079)	\$158	\$(101,453)	\$129,041

The City used a one-time property sale to generate cash flow. In April 2013, the City sold their portion of the Gold Bar Fire District building to the fire district for \$40,000.

Interfund Loans:

The Water Fund lent \$14,000 to the Street Fund in 2011 and \$77,000 to the General Fund in 2012. Although the Council approved resolutions authorizing

the loans, it did not approve repayment schedules. The amount outstanding on December 31, 2013 was \$47,068.

Cost Allocation:

Cities incur costs for central services, such as administration, payroll and purchasing that are shared among funds which benefit from the services. Cities may adopt a fair and equitable method of distributing these shared costs among funds. State law prohibits resources restricted for certain uses, such as utilities, from benefitting other funds (RCW 43.09.210).

The City allocated the costs of salaries and benefits based on estimated percentages to the benefitting funds. In 2013, the City allocated \$227,939 in general government payroll expenditures amongst four restricted and unrestricted funds. The City could not provide sufficient documentation to support the allocation of costs for these funds. The City did not perform a comparison of actual expenditures to determine the reasonableness of the initial allocations and whether the allocations are fair and equitable. Further, the City did not reconcile budgeted amounts to actual costs at year end.

Cause of Condition

Financial Position and Interfund Loans:

The City incurred \$102,252 in litigation costs from January 2013 through December 2, 2014 associated with public records requests and pending public records litigation. Since litigation costs are unpredictable, the City had difficulty budgeting for these costs.

In addition, the City asked voters in November 2012 to approve a property tax levy to cover operating costs in the amount of \$113,000. The levy failed.

Cost Allocation:

The City did not dedicate the time and resources to perform a study to determine if allocated amounts are fair, equitable and representative of the central services provided.

Effect of Condition

Financial Position and Interfund Loans:

If available cash resources in the governmental funds continue to decrease, the City has an increased risk of needing to rely on inter-fund loans to continue operations. The City may not be able to provide services at current levels or meet operating expenses in the future. The City is also at risk for creating a permanent diversion of funds if inter-fund loans are not repaid within the three-year loan period authorized by the City Council.

Cost Allocation:

As a result of the cost allocation conditions identified above, the City is unable to demonstrate how \$227,939 in shared costs allocated in 2013 complied with state laws that prohibit shifting restricted resources to other funds. Further, without support to show how these amounts are fair, equitable and representative of the central services provided, the increased costs to city utilities may result in higher rates.

Recommendation

We continue to recommend the City:

- Establish a long range financial plan to address cash flow issues, monitor and evaluate actual results compared to the plan to ensure its financial condition improves.
- Closely monitor and evaluate financial activities to ensure the City is following the plan and achieving results. Revise the plan if it does not meet planned results.
- Approve a repayment schedule for interfund loans by resolution or ordinance as required by the Budgeting Accounting and Reporting Standards Manual Chapter 4 Section A.
- Develop and follow a policy which documents the rationale for charging shared services to each fund. In addition, the City should retain support of the calculation and actual charges to each fund.
- Periodically review and update the cost allocation policy and plan for charging shared services.

City's Response

Financial Position:

As litigation costs have decreased and revenues, along with the City's economy, have begun to recover, the City's General Fund has been able to improve its ending fund balance so that service reductions over the last several years are beginning to be slowly restored. The City did not establish a formal financial plan as recommended by the State Auditor's office. The current reality does not allow for formal planning due to the unpredictability of litigation costs. A formal financial plan can be developed once the City can establish a more predictable standard which can be managed.

Assisting the City's future financial position and reducing the need to rely on interfund loans to support General Fund operations is the fact that in 2014, the City's liability insurance carrier began to provide legal services as part of the premiums paid by the City for Public Records Acts litigation. This should significantly reduce the City's legal costs and assist the City in increasing reserves and restoring General Fund services to the Community at large.

Interfund Loans:

At issue here is whether the City provided “. . . in the authorization a planned schedule of repayment of the loan principal as well as setting a reasonable rate of interest (based on the external rate available to the municipality) to be paid to the lending fund.” The City Council, while not providing a specific schedule of payment in the resolutions did state therein: “The loan and interest will be repaid no later than three years from issuance.” The administration, through the budgeting process and the annual budget ordinances approved by the City Council, annually appropriated sufficient funds to pay estimated annual debt service based on a monthly debt and interest amortization schedule for each loan and anticipated annual available resources. By practice, the administration was following a monthly repayment schedule while the City Council's original intent was that the loans would be repaid no later than “three years from issuance” leaving the timing and amount of repayment at the administration's discretion. The Street Fund loan was paid off in June of 2014 and adequate funds have been appropriated to retire the General Fund litigation loan by June 2015.

Cost Allocations:

The State Auditor's Office indicates that the “. . . City did not perform a comparison of actual expenditures to determine the reasonableness of the initial allocations and whether the allocations are fair and equitable. Further, the City did not reconcile budgeted amounts to actual costs at year end.” The

recommendation to provide “sufficient documentation to support the allocation of costs for these funds” places an onerous, expensive burden on the City for absolute accuracy in accounting for no public purpose. The 4.4 full time equivalent (FTE) staff members are required to perform multiple short-term activities during the course of the day that “accurate” time keeping would not allow them to complete in order to keep the City functioning. The Auditor’s request is tantamount to the City asking the State Auditors for a breakdown of their billing for the annual audit of the city by time spent auditing each fund and activity. The difficulty in accomplishing this would occur when reviewing Council minutes that cover several activities and funds, each different from the previous one. The time spent to make a determination would result in an increase in the cost of the audit to the City. Or, in order to keep costs down and meet other constraints, the time to actually audit the City would be reduced thereby depriving the City of an accurate and thorough audit. Since the City receives an invoice that is not broken down by activity, RCW 43.09.210 could not be complied with since the City would not have “accurate” data to make the distribution of the annual audit costs as required by RCW 43.09.210. Since no City staff participates in the Audit except to provide requested information, the City has no basis or reference as to the accurate distribution of the cost to each activity or fund. The City’s time would not be an accurate basis to distribute the Audit’s cost equitably to the applicable funds.

Auditor’s Remarks

We thank the City for its cooperation and assistance during the audit. We will review the corrective action taken during our next regular audit.

Applicable Laws and Regulations

RCW 43.09.200 Local government accounting--Uniform system of accounting, states in part:

The state auditor shall formulate, prescribe, and install a system of accounting and reporting for all local governments, which shall be uniform for every public institution, and every public office, and every public account of the same class.

Budgeting, Accounting and Reporting Systems (BARS) Manual, - Interfund Loans states in part:

This section does not attempt to determine which moneys of a municipality may or may not be available for interfund lending, since the special character of some moneys involves commitments

and restrictions which would require individual consideration. As a rule of thumb, however, it may be considered permissible to make interfund loans of those municipal moneys which are clearly inactive or in excess of anticipated cash needs throughout the duration of the loan **and** legally available for investment.

The minimum acceptable procedures for making and accounting for interfund loans are as follows:

The legislative body of a municipality must, by ordinance or resolution, approve all interfund loans, indicating the lending and borrowing funds, and provide in the authorization a planned schedule of repayment of the loan principal as well as setting a reasonable rate of interest (based on the external rate available to the municipality) to be paid to the lending fund. The planned schedule of repayment should specify the due date(s) of payment(s) needed to repay the principal and interest on the loan.

Interest should be charged in all cases, unless:

- a. The borrowing fund has no other source of revenue other than the lending fund; or
- b. The borrowing fund is normally funded by the lending fund.
 1. The borrowing fund must anticipate sufficient revenues to be able over the period of the loan to make the specified principal and interest payments as required in the authorizing ordinance or resolution.
 2. The loan status should be reviewed annually by the legislative body at any open public meeting.
 3. The term of the loan may continue over a period of more than one year, but must be “temporary” in the sense that no permanent diversion of the lending fund results from the failure to repay by the borrowing fund. A loan that continues longer than three years will be scrutinized for a permanent diversion of moneys. (Note: these restrictions and limitations do not apply to those funds which are legally permitted to support one another through appropriations, transfers, advances, etc.)

4. Appropriate accounting records should be maintained to reflect the balances of loans in every fund affected by such transactions.

RCW 43.09.210 Local government accounting – Separate accounts for each fund or activity – Exemption for agency surplus personal property, states in part:

Separate accounts shall be kept for every appropriation or fund of a taxing or legislative body showing date and manner of each payment made therefrom, the name, address, and vocation of each person, organization, corporation, or association to whom paid, and for what purpose paid.

Separate accounts shall be kept for each department, public improvement, undertaking, institution, and public service industry under the jurisdiction of every taxing body.

All service rendered by, or property transferred from, one department, public improvement, undertaking, institution, or public service industry to another, shall be paid for at its true and full value by the department, public improvement, undertaking, institution, or public service industry receiving the same, and no department, public improvement, undertaking, institution, or public service industry shall benefit in any financial manner whatever by an appropriation or fund made for the support of another.