

SCHEDULE OF FEDERAL AUDIT FINDINGS AND QUESTIONED COSTS

Stevens County January 1, 2014 through December 31, 2014

2014-001 The County did not have adequate internal controls to ensure it complied with time and effort requirements for its Homeland Security Grant Program.

CFDA Number and Title:	97.067 Homeland Security Grant Program
Federal Grantor Name:	U.S. Department of Homeland Security
Federal Award/Contract Number:	NA
Pass-through Entity Name:	Spokane County
Pass-through Award/Contract Number:	SDEM-1018, SDEM-1118, SDEM-1318, E15-010 and E12-247
Questioned Cost Amount:	\$121,025

Description of Condition

During fiscal years 2011, 2012, 2013 and 2014 the County spent \$263,996 in Homeland Security Grant Program funds. The grant expenditures for fiscal years 2011, 2012 and 2013 were not reported on the Schedule of Expenditures of Federal Awards (SEFA) in the applicable fiscal year. These expenditures were included in our audit and reported on the SEFA for fiscal year 2014. We reported internal control deficiencies for financial statement reporting, including the preparation of the SEFA, in Finding 2014-002.

The objective of the program is to improve and significantly enhance the ability of the Nation to prevent, deter, respond to and recover from, threats and incidents of terrorism and to enhance regional preparedness.

We audited the County's internal controls over payroll to determine whether salaries and benefits charged to the grant were supported by time and effort documentation as required by federal regulations. Depending on the number and type of activities employees work, time and effort documentation can be documented on a semi-annual certification or a monthly personnel activity report, such as a timesheet.

Our audit found the County did not obtain monthly time and effort documentation for 14 employees whose positions were partially paid from the Homeland Security Grant Program. However, the County had alternate documentation to support overtime costs charged to the grant, which was approved by an external agency.

We consider this internal control deficiency to be a material weakness.

Cause of Condition

The County does not have a process in place to obtain the required monthly time and effort documentation. The County was unaware it was required to obtain time and effort documentation for employees whose payroll costs are paid by federal funds.

Effect of Condition and Questioned Costs

Without proper time and effort records, the County is unable to substantiate the accuracy of \$168,258 of salary and benefits charged to its Homeland Security Grant Program in the manner required by the grantor. We were able to obtain alternate documentation that was approved by an external agency to support overtime costs of \$47,233 charged to the grant. As a result, we are not questioning these costs. However, we were unable to obtain alternate documentation that supported \$121,025 in payroll costs charged to the program. As a result, we are questioning these costs.

Recommendation

We recommend the County establish and follow time and effort internal controls to ensure it meets federal requirements for documentation of all salary and benefit costs charged to grants.

County's Response

We recognize our shortcomings, have made some personnel changes and will better document all wage and benefit activities should this type of funding become available in the future.

Auditor's Remarks

We wish to thank the County's staff and management for their cooperation and assistance during our audit. We look forward to reviewing the County's corrective action during the next audit.

Applicable Laws and Regulations

U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, Section 300 – Auditee Responsibilities, states in part:

The auditee shall:

(b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

(c) Comply with laws, regulations, and the provisions of contracts or grant agreements related to each of its Federal programs.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in its *Codification of Statements on Auditing Standards*, section 935, as follows:

.11 For purposes of adapting GAAS to a compliance audit, the following terms have the meanings attributed as follows: . . .

Deficiency in 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, noncompliance on a timely basis. A deficiency in *design* exists when (a) a control necessary to meet the control objective is missing, or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in *operation* exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively. . .

Material weakness in internal control over compliance. A deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will

not be prevented, or detected and corrected, on a timely basis. In this section, a reasonable possibility exists when the likelihood of the event is either reasonably possible or probable as defined as follows:

Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.

Remote. The chance of the future event or events occurring is slight.

Probable. The future event or events are likely to occur. . .

Significant deficiency in internal control over compliance. A deficiency, or a combination of deficiencies, in internal control over compliance that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments* (2 CFR Part 225), Attachment B, Section 8(h), states in part:

(1) Charges to Federal awards for salaries and wages, whether treated as direct or indirect costs, will be based on payrolls documented in accordance with generally accepted practice of the governmental unit and approved by a responsible official(s) of the governmental unit.

(4) Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation which meets the standards in subsection (5) unless a statistical sampling system (see subsection (6)) or other substitute system has been approved by the cognizant Federal agency. Such documentary support will be required where employees work on:

- (a) More than one Federal award,
- (b) A Federal award and a non Federal award,
- (c) An indirect cost activity and a direct cost activity,

(d) Two or more indirect activities which are allocated using different allocation bases, or

(e) An unallowable activity and a direct or indirect cost activity.

(5) Personnel activity reports or equivalent documentation must meet the following standards:

(a) They must reflect an after the fact distribution of the actual activity of each employee,

(b) They must account for the total activity for which each employee is compensated,

(c) They must be prepared at least monthly and must coincide with one or more pay periods, and

(d) They must be signed by the employee.

(e) Budget estimates or other distribution percentages determined before the services are performed do not qualify as support for charges to Federal awards but may be used for interim accounting purposes. . .

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

Stevens County January 1, 2014 through December 31, 2014

2014-002 County's internal controls over financial statement preparation are inadequate to ensure accurate reporting.

Background

County elected officials and appointed management are responsible for designing and following internal controls that provide reasonable assurance regarding the reliability of financial reporting. Our audit identified deficiencies in internal controls that adversely affected the County's ability to produce reliable financial statements.

All local governments in Washington that spend federal funds are required to prepare a Schedule of Expenditures of Federal Awards (SEFA) as part of the annual financial report. U.S. Office of Management and Budget (OMB) Circular A-133 requires grantees to identify, in its accounts, all Federal program awards received and expended and to report all Federal awards expended on the SEFA each fiscal year.

The prior five audits identified control deficiencies in the financial statement preparation process that were reported to management.

Description of Condition

Our audit process identified the following deficiencies in internal controls that, when taken together, represent a significant deficiency:

- Employees responsible for preparation of the financial statements lacked the technical knowledge of reporting requirements prescribed in the Budget, Accounting and Reporting System (BARS) manual.
- The County's annual report preparation process did not include controls that ensure amounts reported in the financial statements agree to the underlying accounting records.
- Although the County has a process for reviewing the prepared financial statements, departments did not work collaboratively to ensure the financial statements were accurate in all respects.

- The County's internal control process for preparing and reviewing the Schedule of Expenditures of Federal Awards (SEFA) was not effective.

Cause of Condition

Although the County has taken steps to address some concerns noted during the prior audit, it has not fully developed internal controls to ensure complete and accurate financial statements. The County is required to prepare and submit an annual financial report each year, but has not developed a proper timeline and dedicated resources to ensure the financial statement, notes and supplemental schedules are prepared timely complete and accurate. Although the County's control process provides that the County Treasurer should perform a second review of the financial statements for accuracy, the County Auditor did not provide enough time to ensure this critical control occurred before filing the annual report.

The County's established controls for SEFA preparation assume the grant information provided by departments to the County Auditor is accurate without proper monitoring and review controls. However, some department base reported information on revenues received instead of when the related federal expenditures were incurred as required.

Effect of Condition

Delayed and inaccurate financial reports limit access to financial information used by County officials, the public, state and federal agencies and other interested parties. As a result of the control deficiencies and effects identified below, the County missed its federal single audit deadline. In addition, these conditions delayed the audit process and resulted in increased audit costs. We noted:

- Both the County Auditor and County Treasurer prepared a Schedule of Cash Activity but the schedules did not agree and the differences were not resolved so it could be used as a tool to accurately prepare the annual report.
- The County's Fiduciary Fund Resources and Uses Arising from Cash Transactions submitted for audit included special purpose districts activities causing the statement to be overstated by approximately \$15.8 million.
- Non-operating expenditures were overstated by \$29,696 for Fund 501, Equipment Rental and Revolving Funds due to the County reporting clearing funds.

- The amounts reported on the Schedule of Liabilities were inaccurate overstating four amounts by a total of \$35,574.
- The Notes to the Financial Statements improperly reported operating transfers included an inter-fund loan of \$475,337 and excluding a transfer of \$35,406.
- The County failed to submit its financial statements on time as required by state law, RCW 43.09.230. For the last three years, the statements were submitted more than 30 days late.
- The County submitted a Schedule of Expenditures of Federal Awards based upon revenues, rather than expenditures as required causing it to be understated by \$85,479.
- The County failed to submit the Notes to the Schedule of Expenditures of Federal Awards as required by the BARS manual.

These deficiencies in internal controls make it reasonably possible that material misstatements could continue to occur and not be prevented or detected by the County in a timely manner.

Recommendation

We recommend the County:

- Provide adequate training to employees responsible for financial reporting to ensure compliance with reporting requirements.
- Develop a monitoring control to ensure the financial statements agree to the underlying accounting records
- Ensure departments responsible for financial statement preparation collaborate to produce accurate financial reports.
- Provide adequate time and resources to allow a detailed review of the financial statements by a person knowledgeable of BARS reporting requirements.
- Improve the SEFA preparation process to ensure the schedule is prepared according to OMB and BARS guidance.

County's Response

We recognize our shortcomings and are striving to improve the methods of information gathering and calculations to produce a better product. We recognize

the importance to get proper BARS manual training to help us create an accurate report and will establish a better completion of task deadline schedule so that a proper review is completed in time to meet the filing deadline in the future.

Auditor's Remarks

We wish to thank the County's staff and management for their cooperation and assistance during our audit. We look forward to reviewing the County's corrective action during the next audit.

Applicable Laws and Regulations

U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, Subpart E, Section 500, states in part:

(a) General. The audit shall be conducted in accordance with GAGAS. . .

Subpart B, Section 205, states in part:

(a) Determining Federal awards expended. The determination of when an award is expended should be based on when the activity related to the award occurs. Generally, the activity pertains to events that require the non-Federal entity to comply with laws, regulations, and the provisions of contracts or grant agreements, such as: expenditure/expense transactions associated with grants, cost-reimbursement contracts, cooperative agreements, and direct appropriations; the disbursement of funds passed through to subrecipients; the use of loan proceeds under loan and loan guarantee programs; the receipt of property; the receipt of surplus property; the receipt or use of program income; the distribution or consumption of food commodities; the disbursement of amounts entitling the non-Federal entity to an interest subsidy; and, the period when insurance is in force.

Subpart C, Section 300, states in part:

The auditee shall. . .

(a) Identify, in its accounts, all Federal awards received and expended and the Federal programs under which they were received. Federal program and award identification shall include, as applicable, the CFDA title and number, award

number and year, name of the Federal agency, and name of the pass-through entity.

(b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

(c) Comply with laws, regulations, and the provisions of contracts or grant agreements related to each of its Federal programs.

(d) Prepare appropriate financial statements, including the schedule of expenditures of Federal awards in accordance with §___.310 . . .

Government Auditing Standards, December 2011 Revision, paragraph 4.23 states:

4.23 When performing GAGAS financial audits, auditors should communicate in the report on internal control over financial reporting and compliance, based upon the work performed, (1) significant deficiencies and material weaknesses in internal control; (2) instances of fraud and noncompliance with provisions of laws or regulations that have a material effect on the audit and any other instances that warrant the attention of those charged with governance; (3) noncompliance with provisions of contracts or grant agreements that has a material effect on the audit; and (4) abuse that has a material effect on the audit.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in its *Codification of Statements on Auditing Standards*, section 265, as follows:

.07 For purposes of generally accepted auditing standards, the following terms have the meanings attributed as follows:

Material weakness. A deficiency, or a 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.

Significant deficiency. 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.

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.

RCW 43.09.230 Local government accounting – Annual reports – Comparative statistics, states:

The state auditor shall require from every local government financial reports covering the full period of each fiscal year, in accordance with the forms and methods prescribed by the state auditor, which shall be uniform for all accounts of the same class.

Such reports shall be prepared, certified, and filed with the state auditor within one hundred fifty days after the close of each fiscal year.

The reports shall contain accurate statements, in summarized form, of all collections made, or receipts received, by the officers from all sources; all accounts due the public treasury, but not collected; and all expenditures for every purpose, and by what authority authorized; and also: (1) A statement of all costs of ownership and operation, and of all income, of each and every public service industry owned and operated by a local government; (2) a statement of the entire public debt of every local government, to which power has been delegated by the state to create a public debt, showing the purpose for which each item of the debt was created, and the provisions made for the payment thereof; (3) a classified statement of all receipts and expenditures by any public institution; and (4) a statement of all expenditures for labor relations consultants, with the identification of each consultant, compensation, and the terms and conditions of each agreement or arrangement; together with such other information as may be required by the state auditor.

Budget Accounting and Reporting System (BARS) Manual; Accounting; Accounting Principles and Internal Control; Internal Control states in part:

Purpose and Definition of Internal Controls

Internal control is defined by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), in standards adopted by the American Institute of Certified Public Accountants and by the Federal Office of Management and Budget as follows:

Internal control is a process – affected by those charged with governance, management and other personnel designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations
- Compliance with applicable laws and regulations
- Reliability of financial reporting

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.

Controls over Financial Reporting

This objective refers to fair presentation of financial statements and required schedules in all material respects in accordance with the stated basis of accounting. . .

Preparation of the annual report – Controls should ensure that financial statements and required schedules are properly compiled and prepared from source accounting records. Controls should also ensure correct presentation of statements and schedules. . .

Controls over Financial Reporting:

3.1.3.140 This objective refers to fair presentation of financial statements and required schedules in all material respects in accordance with the stated basis of accounting.

3.1.3.150 In meeting this objective, the government should have controls that accomplish the following key functions:

- Identification of financial events – Controls should ensure financial events and transactions are properly identified and recorded.
- Properly applying accounting standards – Controls should ensure correct criteria and methodology is applied when accounting for financial events. When the correct method of accounting for or reporting a transaction is unclear, the government should seek clarification by performing research, contracting for accounting assistance, or communicating with the State Auditor’s Office or standard setting bodies.
- Correctly accounting for all financial events – Controls should ensure that:
 - Only valid transactions are recorded and reported.
 - All transactions occurred during the period are recorded and reported.
 - Transactions are recorded and reported at properly valued and calculated amounts.
 - Recorded and reported transactions accurately reflect legal rights and obligations.
 - Transactions are recorded and reported in the account and fund to which they apply.
 - Preparation of the annual report – Controls should ensure that financial statements and required schedules are properly compiled and prepared from source accounting records. Controls should also ensure correct presentation of statements and schedules.

3.1.3.160 Controls and processes should generate adequate documentation to demonstrate achievement of objectives. This is not only important for audit, oversight and public records purposes, but also to enable effective monitoring of controls over financial reporting by management.