

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

City of Langley Island County

January 1, 2014 through December 31, 2014

2014-001 The City's internal controls are inadequate to ensure federal expenditures are accurately reported on the Schedule of Expenditures of Federal Awards.

Background

Entity management, the State Legislature, state and federal agencies and bondholders rely on the information included in financial statements and reports to make decisions. City management is responsible for designing and following internal controls that provide reasonable assurance regarding the reliability of financial reporting. The control system must ensure that financial data is reliably authorized, processed and reported.

We identified a material weakness in controls that adversely affects the City's ability to produce a reliable Schedule of Expenditures of Federal Awards (SEFA), which is supplemental information required to be included in the City's financial statements and is part of the audit report required by the federal government. This Schedule is to include all federal program expenditures by the City for each fiscal year.

Description of Condition

Our audit determined internal controls were inadequate to ensure the SEFA accurately reported all federal expenditures. We identified the following internal control deficiencies that, when taken together, represent a material weakness:

- The City procedures for preparing the SEFA are not adequate to ensure all federal program expenditures are identified and reported.

Cause of Condition

The City received a contract award from the Washington Department of Transportation which included both state and federal funding. Due to a lack of communication between the individual overseeing the project and the individual preparing the schedule, the City overlooked the federal portion of this award

when preparing their SEFA. Individuals responsible for reviewing the SEFA did not detect the omission.

Effect of Condition

The City did not report \$388,662 in federal expenditures on the SEFA. Due to this error, we were required to perform additional procedures and audit this program to complete the federal audit. Had our audit not identified this error, the City would not have received an audit of federal programs as required by the Single Audit Act. The omission of the expenditures on the SEFA affected the amount of audit coverage required, and delayed the audit beyond the required nine-month reporting deadline.

If omissions or other errors are made and not identified, the City could not have an audit of federal programs when required, jeopardize future federal funding and report its financial information inaccurately to citizens and other governments.

Recommendation

We recommend the City develop procedures to ensure all federal program expenditures are identified and reported on the Schedule of Expenditures of Federal Awards.

City's Response

The City had both Federal and State grants for a street project. A federal grant payment received by the City was receipted as a state grant payment. In the future, the Finance Director will review all grant receipts to make sure they are coded correctly in the City's financial software.

Auditor's Remarks

We appreciate the steps the City is taking to resolve this issue. We will review the condition during our 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, 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 . . .

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.

Budget Accounting and Reporting System Manual – Supplemental Schedules (Schedule 16), states in part:

4.8.5.20 The purpose of this schedule is to summarize federal grant expenditures as a basis for planning and conducting the single audit. It also serves to provide assurance to those agencies that award financial assistance that their programs or grants were included in the audit. It is important to prepare this schedule carefully to ensure that it is accurate and complete. Any program or grant omitted from this schedule will be considered unaudited. This schedule should be prepared on the same basis of accounting as the financial statements.

4.8.5.30 Include on this schedule all expenditures of federal awards that were received directly from a federal agency and indirectly (pass-through) from a state agency or local government.

4.8.5.130 Use the following guidelines to calculate the value of federal awards expended under loan programs:

- (1) Amount of new loans made or received during the fiscal year, plus
- (2) Balance of loans from previous years for which the federal government imposes continuing compliance requirements, plus
- (3) Any interest subsidy, cash, or administrative cost allowance received.

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 material weaknesses and significant deficiencies 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: . . .

A material weakness is a deficiency, or 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.

A significant deficiency is 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.