



Washington State Auditor's Office

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Financial Statements and Federal Single Audit Report

Public Utility District No. 1 of Jefferson County

For the period January 1, 2014 through December 31, 2014

Published August 22, 2016

Report No. 1017247





Washington State Auditor's Office

August 22, 2016

Board of Commissioners
Public Utility District No. 1 of Jefferson County
Port Hadlock, Washington

Report on Financial Statements and Federal Single Audit

Please find attached our report on Public Utility District No. 1 of Jefferson County's financial statements and compliance with federal laws and regulations.

We are issuing this report in order to provide information on the District's financial condition.

Sincerely,

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Public Utility District No. 1 of Jefferson County January 1, 2014 through December 31, 2014

SECTION I – SUMMARY OF AUDITOR’S RESULTS

The results of our audit of Public Utility District No. 1 of Jefferson County are summarized below in accordance with U.S. Office of Management and Budget Circular A-133.

Financial Statements

An unmodified opinion was issued on the Schedule of Expenditures of Federal Awards. We were engaged to audit the financial statements and a disclaimer of opinion was issued in a separate report.

Internal Control over Financial Reporting:

- *Significant Deficiencies:* We reported no deficiencies in the design or operation of internal control over financial reporting that we consider to be significant deficiencies related to the financial statements or the Schedule of Expenditures of Federal Awards.
- *Material Weaknesses:* We identified deficiencies that we consider to be material weaknesses related to the Schedule of Expenditures of Federal Awards. We identified deficiencies that we consider to be material weaknesses related to the financial statements, which are included in a separate report.

We noted no instances of noncompliance that were material to the financial statements or Schedule of Expenditures of Federal Awards of the District.

Federal Awards

Internal Control over Major Programs:

- *Significant Deficiencies:* We reported no deficiencies in the design or operation of internal control over major federal programs that we consider to be significant deficiencies.
- *Material Weaknesses:* We identified deficiencies that we consider to be material weaknesses.

We issued an unmodified opinion on the District's compliance with requirements applicable to its major federal program.

We reported findings that are required to be disclosed under section 510(a) of OMB Circular A-133.

Identification of Major Federal Programs:

The following program was selected as a major program in our audit of compliance in accordance with OMB Circular A-133.

<u>CFDA No.</u>	<u>Program or Cluster Title</u>
11.557	ARRA Broadband Technology Opportunities Program (BTOP)

The dollar threshold used to distinguish between Type A and Type B programs, as prescribed by OMB Circular A-133, was \$300,000.

The District did not qualify as a low-risk auditee under OMB Circular A-133.

SECTION II – FINANCIAL STATEMENT FINDINGS

See finding 2014-002. In a separate report dated August 16, 2016, matters related to the financial statements were included in finding 2014-001.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

See finding 2014-003.

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

Public Utility District No. 1 of Jefferson County January 1, 2014 through December 31, 2014

2014-002 The District's internal controls were inadequate to ensure federal expenditures were reported on the Schedule of Expenditures of Federal Awards.

Background

It is the responsibility of District management to design and follow internal controls that provide reasonable assurance regarding the reliability of financial reporting.

Entities that receive federal money are required to prepare a Schedule of Expenditures of Federal Awards (SEFA) as part of their annual financial report. The SEFA should include all federal expenditures made by the District for each fiscal year, and is the basis for determining major programs audited in accordance with U.S. Office of Management and Budget (OMB) Circular A-133.

Description of Condition

Our audit identified the following deficiencies in internal controls that, when taken together, represent a material weakness:

- District personnel responsible for preparation of the SEFA did not have an adequate understanding of the OMB Circular A-133 and State Auditor's *Budgeting, Accounting and Reporting System* (BARS) Manual reporting requirements.
- The District's process for financial statement preparation did not include a reconciliation of reported grant expenditures to accounting records or an effective secondary review capable of detecting significant misstatements.

Cause of Condition

Historically, the District had not received many federal grants. As a result, the District did not design effective internal controls, including providing necessary training to staff, to ensure accurate and complete reporting of federal expenditures.

Effect of Condition

Inaccurate financial reports limit access to financial information used by District officials, the public, state and federal agencies and other interested parties. In addition, these conditions delay the audit process and increase audit costs.

The District did not prepare a SEFA for 2014. However, our audit identified the following federal expenditures which should have been reported:

- \$3,854,114 for the ARRA Broadband Technology Opportunities Program (BTOP) grant (CFDA 11.557), which required audit as a major program.
- \$278,356 for the Capitalization Grants for Drinking Water State Revolving Funds grants (CFDA 66.468).

The District subsequently corrected the misstatements.

Should future omissions or other errors be made and not identified in a timely manner, the District could fail to meet the required audit coverage, miss its federal reporting deadline, jeopardize future federal funding and report its financial information inaccurately to citizens and other government agencies.

Recommendation

We recommend the District establish and follow procedures to ensure:

- Personnel responsible for financial reporting receive adequate training regarding federal reporting requirements as outlined in OMB Circular A-133 and the *Budgeting, Accounting and Reporting System* (BARS) manual.
- The Schedule of Expenditures of Federal Awards is complete and accurate. This includes reconciliation of reported federal grant expenditures to accounting records and a secondary review by an individual knowledgeable of District grant activities and federal reporting requirements.

District's Response

The PUD will ensure that the new Chief Financial Officer and/or the Controller will have the necessary training and/or experience in State and Federal grant accounting and reporting requirements. They will be responsible for implementing and enforcing improved internal controls.

Auditor's Remarks

We thank the District for its assistance throughout the audit, and the steps it is taking to address these issues. We will review the status of the District's corrective action during our next audit.

Applicable Laws and Regulations

Budgeting, Accounting and Reporting System (BARS) Manual – Accounting, Accounting Principles and Internal Control, Internal Control states in part:

3.1.3.20 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

3.1.3.30 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.

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

4.23 When performing GAGAS financial audits, auditors should communicate in the report on internal control over financial reporting and compliance, based on the work performed, (1) significant deficiencies and material weaknesses in internal control;

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 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.

Budget Accounting (BARS) Manual – Supplemental Schedules – Expenditures of Federal Awards (Schedule 16), states in part:

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.

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

Section 200:

(a) Audit required. Non-federal entities that expend \$300,000 (\$500,000 for fiscal years ending after December 31, 2003) or more in a year in Federal awards shall have a single or program-specific audit conducted for that year in accordance with the provisions of this part. Guidance on determining Federal awards expended is provided in §____.205

Section 205:

Basis for determining Federal awards expended.

(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 . . .

Section 300:

(a) The auditee shall:

(b) Identify, in its accounts, all Federal awards received and expended and the Federal programs under which they are 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 the name of the pass-through entity.

(c) 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.

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

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

Section 310:

(b) Schedule of expenditures of federal awards. The auditee shall prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements.

SCHEDULE OF FEDERAL AUDIT FINDINGS AND QUESTIONED COSTS

Public Utility District No. 1 of Jefferson County January 1, 2014 through December 31, 2014

2014-003 The District's internal controls were inadequate to ensure compliance with American Reinvestment and Recovery Act requirements.

CFDA Number and Title: 11.557 ARRA - Broadband
Technology Opportunities Program
(BTOP)

Federal Grantor Name: Department of Commerce National
Telecommunications and Information
Administration

Federal Award/Contract Number: NT10BIX5570047

Pass-through Entity Name: Northwest Open Access Network

**Pass-through Award/Contract
Number:** N/A

Questioned Cost Amount: \$0

Background

Congress enacted the American Recovery and Reinvestment Act (ARRA) of 2009 in response to economic conditions. The Recovery Act requires transparency and accountability regarding the use of this money from the governments that receive it. To meet this objective, recipients must agree to maintain records that identify adequately the source and application of ARRA funding and separately identify how they are spending it on the Schedule of Expenditures of Federal Awards (SEFA).

Description of Condition

Our audit identified the following deficiencies in internal controls that represent material weaknesses:

- The District did not have a process to record or identify the funding source for \$3,854,114 of capital assets funded by ARRA under the Broadband Technology Opportunities Program (BTOP) in its asset management system.

- The District did not report \$3,854,114 of Recovery Act expenditures on the SEFA, because a 2014 SEFA was not prepared.

Cause of Condition

Historically, the District did not receive many federal grants. As a result, staff was unaware of the Recovery Act and other federal reporting requirements.

Effect of Condition and Questioned Costs

By not recording assets or identifying the source of funds in the asset management system, the District did not comply with federal requirements to maintain records that identify, adequately, the source and application of Recovery Act funds.

Grantors use the SEFA as an oversight tool and auditors use them to ensure federal grants receive required audits. By not properly disclosing the use of Recovery Act money, the District did not meet transparency and accountability objectives and could have missed a required audit.

The errors were detected during the financial statement audit, and the BTOP grant was audited as a major program. The District subsequently recorded and identified the funding source of the assets in its asset management system, and reported the expenditures on the SEFA.

Recommendation

We recommend the District establish and follow procedures to ensure:

- Records, including asset management records, adequately identify the source and application of Recovery Act funds.
- The Schedule of Expenditures of Federal Awards is complete, accurate, and presented in accordance with federal requirements, including the requirement to separately identify expenditures of federal awards under the Recovery Act.

District's Response

The PUD has properly identified and recorded funds funded by ARRA under the Broadband Technology Opportunities Program (BTOP) in its asset management system. The Schedule of Expenditures of Federal Awards is now being completed accurately, and is being presented in accordance with federal requirements, including the requirement to separately identify expenditures of federal awards under the Recovery Act.

The PUD has recently hired a District Controller experienced in State and Federal Grant accounting and will ensure District personnel receive continued education on Federal and State Grant Accounting and Reporting. The PUD will continue to develop and follow controls to meet Federal and State requirements. The PUD will hire and contract the necessary personnel to insure the PUD meets Federal and State reporting requirements.

Auditor's Remarks

We thank the District for its assistance throughout the audit, and the steps it is taking to address these issues. We will review the status of the District's corrective action 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*, states in part:

Section .300(b)

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 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.

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 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.

Title 2, Code of Federal Regulations, Section 176.210, states in part:

- (a) To maximize the transparency and accountability of funds authorized under the American Recovery and Reinvestment Act of 2009 (Pub. L. 111-5) (Recovery Act) as required by Congress and in accordance with 2 CFR 215.21 “Uniform Administrative Requirements for Grants and Agreements” and OMB Circular A-102 Common Rules provisions, recipients agree to maintain records that identify adequately the source and application of Recovery Act funds.
- (b) For recipients covered by the Single Audit Act Amendments of 1996 and OMB Circular A-133, “Audits of States, Local Governments, and Non-Profit Organizations,” recipients agree to separately identify the expenditures for Federal awards under the Recovery Act on the Schedule of Expenditures of Federal Awards (SEFA) and the Data Collection Form (SF-SAC) required by OMB Circular A-133...This shall be accomplished by identifying expenditures for Federal awards made under the Recovery Act separately on the SEFA, and as separate rows under Item 9 of Part III on the SF-SAC by CFDA number, and inclusion of the prefix “ARRA-“ in the identifying name of the Federal program on the SEFA and as the first characters in Item 9d of Part III on the SF-SAC....”

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Public Utility District No. 1 of Jefferson County January 1, 2014 through December 31, 2014

This schedule presents the status of federal findings reported in prior audit periods. The status listed below is the representation of Public Utility District No. 1 of Jefferson County. The State Auditor's Office has reviewed the status as presented by the District.

Audit Period: 1/1/2012 – 12/31/2012	Report Ref. No: 1011579	Finding Ref. No: 2012-003	CFDA Number(s): 66.468
Federal Program Name and Granting Agency: Capitalization Grants for Drinking Water State Revolving Funds, Environmental Protection Agency		Pass-Through Agency Name: Department of Commerce	
Finding Caption: The District did not have adequate internal controls to ensure compliance with federal suspension and debarment requirements.			
Background: During 2012, the District paid \$1,614,360 of its loan program funding to four vendors subject to suspension and debarment requirements. The District did not have procedures in place to verify whether the vendors were suspended or debarred prior to entering into the contracts, or inform the vendors of their responsibilities regarding lower-tier covered transactions.			
Status of Corrective Action: (check one) <input checked="" type="checkbox"/> Fully Corrected <input type="checkbox"/> Partially Corrected <input type="checkbox"/> Not Corrected <input type="checkbox"/> Finding is considered no longer valid			
Corrective Action Taken: <i>The PUD is now following procedures to verify whether vendors were suspended or debarred prior to entering into contracts.</i>			

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND
OTHER MATTERS BASED ON AN AUDIT OF THE SCHEDULE OF
EXPENDITURES OF FEDERAL AWARDS PERFORMED IN
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

**Public Utility District No. 1 of Jefferson County
January 1, 2014 through December 31, 2014**

Board of Commissioners
Public Utility District No. 1 of Jefferson County
Port Hadlock, Washington

We have audited, 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, the Schedule of Expenditures of Federal Awards of Public Utility District No. 1 of Jefferson County, Washington, as of and for the year ended December 31, 2014, and have issued our report thereon dated August 16, 2016.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the schedule, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the schedule, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Audit Findings and Responses, we identified certain deficiencies in internal control that we consider to be material weaknesses.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the District's schedule 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. We consider the deficiencies described in the accompanying Schedule of Audit Findings and Responses as Finding 2014-002 to be material weaknesses.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the District's schedule is free from material misstatement, we performed tests of the District's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

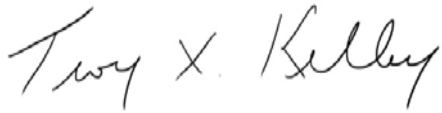
DISTRICT'S RESPONSE TO FINDINGS

The District's response to the findings identified in our audit is described in the accompanying Schedule of Audit Findings and Responses. The District's response was not subjected to the auditing procedures applied in the audit of the schedule and, accordingly, we express no opinion on the response.

PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other

purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink that reads "Troy X. Kelley". The signature is written in a cursive style with a large, stylized 'T' and 'K'.

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

August 16, 2016

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR
EACH MAJOR FEDERAL PROGRAM AND REPORT ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE
WITH OMB CIRCULAR A-133**

**Public Utility District No. 1 of Jefferson County
January 1, 2014 through December 31, 2014**

Board of Commissioners
Public Utility District No. 1 of Jefferson County
Port Hadlock, Washington

**REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL
PROGRAM**

We have audited the compliance of Public Utility District No. 1 of Jefferson County, Jefferson County, Washington, with the types of compliance requirements described in the U.S. *Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the District's major federal programs for the year ended December 31, 2014. The District's major federal programs are identified in the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the District's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about

the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. Our audit does not provide a legal determination on the District's compliance.

Opinion on Each Major Federal Program

In our opinion, the District complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2014.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance with those requirements which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Federal Award Findings and Questioned Costs as Finding 2014-003. Our opinion on each major federal program is not modified with respect to these matters.

District's Response to the Findings

The District's response to the noncompliance findings identified in our audit are described in the accompanying Schedule of Federal Award Findings and Questioned Costs. The District's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

REPORT ON INTERNAL CONTROL OVER COMPLIANCE

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program in order to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal

control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's 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 with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We identified certain deficiencies in internal control over compliance, as described in the accompanying Schedule of Federal Award Findings and Questioned Costs as Finding 2014-003, to be material weaknesses.

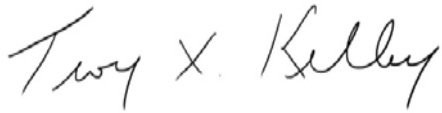
District's Response to Findings

The District's response to the internal control over compliance findings identified in our audit is described in the accompanying Schedule of Federal Award Findings and Questioned Costs. The District's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other

purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink that reads "Troy X. Kelley". The signature is written in a cursive style with a large, stylized 'T' and 'K'.

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

August 16, 2016

INDEPENDENT AUDITOR'S REPORT ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Public Utility District No. 1 of Jefferson County January 1, 2014 through December 31, 2014

Board of Commissioners
Public Utility District No. 1 of Jefferson County
Port Hadlock, Washington

REPORT ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

We have audited the accompanying Schedule of Expenditures of Federal Awards of Public Utility District No. 1 of Jefferson County, Washington, for the year ended December 31, 2014, and the related notes (the schedule).

Management's Responsibility for the Schedule

Management is responsible for the preparation and fair presentation of this schedule in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of a schedule that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on this schedule based on our audit. We conducted our audit 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, and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether the schedule is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the schedule. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the schedule, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant

to the District's preparation and fair presentation of the schedule in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the schedule.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the Schedule of Expenditures of Federal Awards referred to above presents fairly, in all material respects, the expenditures of federal awards of Public Utility District No. 1 of Jefferson County, for the year ended December 31, 2014, in accordance with accounting principles generally accepted in the United States of America.

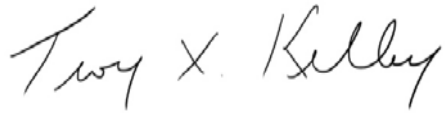
Other Matters

We were engaged to audit the financial statements of Public Utility District No. 1 of Jefferson County as of and for the year ended December 31, 2014, and our report thereon, dated August 16, 2016, expressed a disclaimer of opinion on those financial statements.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated August 16, 2016 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That

report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Troy X. Kelley".

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

August 16, 2016

FINANCIAL SECTION

Public Utility District No. 1 of Jefferson County January 1, 2014 through December 31, 2014

SCHEDULE

Schedule of Expenditures of Federal Awards – 2014

Notes to the Schedule of Expenditures of Federal Awards – 2014

**Public Utility District #1 of Jefferson County
Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2014**

Federal Agency (Pass-Through Agency)	Federal Program	CFDA Number	Other Award Number	Expenditures		Total	Note
				From Pass- Through Awards	From Direct Awards		
Department of Commerce National Telecommunications and Information Administration (Northwest Open Access Network)	ARRA Broadband Technology Opportunities Program (BTOP)	11.557	N/A	3,854,114		3,854,114	1,2,3
Total CFDA 11.557				3,854,114	0	3,854,114	
Environmental Protection Agency Office of Water (WA Department of Commerce)	Capitalization Grants for Drinking Water State Revolving Funds	66.468	DM10-952-018	145,341		145,341	1,2
Environmental Protection Agency Office of Water (WA Department of Commerce)	Capitalization Grants for Drinking Water State Revolving Funds	66.468	DM12-952-091	130,153		130,153	1,2
Total CFDA 66.468				275,494	0	275,494	
Total Federal Awards Expended:				4,129,608	0	4,129,608	

The Notes to the Schedule of Expenditures of Federal Awards is an integral part of this statement

PUBLIC UTILITY DISTRICT NO. 1 OF JEFFERSON COUNTY, WASHINGTON
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2014

Note 1 - Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the federal grant activity of Public Utility District #1 of Jefferson County (the District) under programs of the federal government for the year ended December 31, 2014. The information in this Schedule is presented in accordance with the requirement of the Office of Management and Budget (OMB) Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards. Because the Schedule presents only a selected portion of the operations of the District, it is not intended to and does not present the financial position, changes in net position, or cash flows of the District.

Note 2 - Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

Note 3 - American Recovery and Reinvestments Act (ARRA) of 2009

Expenditures for this program were funded by ARRA.

**CORRECTIVE ACTION PLAN FOR FINDINGS REPORTED
UNDER OMB CIRCULAR A-133**

**Public Utility District No. 1 of Jefferson County
January 1, 2014 through December 31, 2014**

This schedule presents the corrective action planned by the auditee for findings reported in this report in accordance with OMB Circular A-133. The information in this schedule is the representation of the Public Utility District No. 1 of Jefferson County.

Finding ref number: 2014-002	Finding caption: The District's internal controls were inadequate to ensure federal expenditures were reported on the Schedule of Expenditures of Federal Awards.
Name, address, and telephone of auditee contact person: Jim Parker 310 Four Corners Road Port Townsend, WA 98368 (360) 385-8340	
Corrective action the auditee plans to take in response to the finding: <i>The District now understands the requirements for the Schedule of Expenditures of Federal Awards and is complying with the requirement. Additionally, the PUD is hiring a new Controller who will have experience in Federal and State grant reporting and whom the PUD will send to additional training. This individual will develop, implement and enforce improved internal controls for Federal Grant accounting.</i>	
Anticipated date to complete the corrective action: January 2017	
Finding ref number: 2014-003	Finding caption: The District's internal controls were inadequate to ensure compliance with American Reinvestment and Recovery Act requirements.
Name, address, and telephone of auditee contact person: Jim Parker 310 Four Corners Road Port Townsend, WA 98368 (360) 385-8340	
Corrective action the auditee plans to take in response to the finding: <i>The PUD has properly identified and recorded funds funded by ARRA under the Broadband Technology Opportunities Program (BTOP) in its asset management system. The Schedule of</i>	

Expenditures of Federal Awards is now being completed accurately, and is being presented in accordance with federal requirements, including the requirement to separately identify expenditures of federal awards under the Recovery Act.

The PUD has recently hired a District Controller experienced in State and Federal Grant accounting and will ensure District personnel receive continued education on Federal and State Grant Accounting and Reporting. The PUD will continue to develop and follow controls to meet Federal and State requirements. The PUD will hire and contract the necessary personnel to insure the PUD meets Federal and State reporting requirements.

Anticipated date to complete the corrective action: January 2017

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments as well as [fraud](#), state [whistleblower](#) and [citizen hotline](#) investigations.

The results of our work are widely distributed through a variety of reports, which are available on our [website](#) and through our free, electronic [subscription](#) service.

We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

Contact information for the State Auditor's Office	
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