



**Washington State Auditor's Office**

**Troy Kelley**

**Integrity • Respect • Independence**

## **Accountability Audit Report**

# **City of Arlington**

**Snohomish County**

**For the period January 1, 2013 through December 31, 2013**

**Published March 23, 2015**

**Report No. 1013812**





## Washington State Auditor Troy Kelley

March 23, 2015

Mayor and City Council  
City of Arlington  
Arlington, Washington

### Report on Accountability

Thank you for the opportunity to work with you to promote accountability, integrity and openness in government. The State Auditor's Office takes seriously our role of providing state and local governments with assurance and accountability as the independent auditor of public accounts. In this way, we strive to help government work better, cost less, deliver higher value and earn greater public trust.

Independent audits provide essential accountability and transparency for City operations. This information is valuable to management, the governing body and public stakeholders when assessing the government's stewardship of public resources.

The attached comprises our report on the City's compliance and safeguarding of public resources. Our independent audit report describes the overall results and conclusions for areas we examined. We appreciate the opportunity to work with your staff and we value your cooperation during the audit.

Sincerely,

TROY KELLEY  
STATE AUDITOR  
OLYMPIA, WA

## TABLE OF CONTENTS

Audit Summary .....	4
Schedule Of Audit Findings And Responses .....	6
Related Reports .....	15
Information About The City .....	16
About The State Auditor's Office .....	17

## AUDIT SUMMARY

### Results in brief

In most areas we audited, City operations complied with applicable requirements and provided adequate safeguarding of public resources. The City also complied with state laws and regulations and its own policies and procedures in the areas we examined.

However, we identified areas in which the City could make improvements.

We recommended the City:

- Ensures it establishes contracts for all City property leased. The City should develop procedures to ensure contracts are established prior to the use of its property.
- Ensure there are procedures in place to monitor compliance with lease requirements, City policy, City Municipal Code and state law.
- Work with its legal counsel to ensure lease contracts are signed in accordance with its Municipal Code.
- Implement a plan to ensure a consistent method is used when allocating shared costs to all City funds.
- Ensures the Airport Fund is compensated from the General Fund for leased office space at the airport.

These recommendations were included in our report as a finding.

We also noted certain matters that we communicated to City management in a letter dated March 16, 2015, related to conflict of interest, payroll and cash receipting. We appreciate the City's commitment to resolving those matters.

### About the audit

This report contains the results of our independent accountability audit of the City of Arlington from January 1, 2013 through December 31, 2013.

Management is responsible for ensuring compliance and adequate safeguarding of public resources from fraud, loss or abuse. This includes the design, implementation and maintenance of internal controls relevant to these objectives.

Our audit involved performing procedures to obtain evidence about the City's uses of public resources, compliance with state laws and regulations and its own policies and procedures, and internal controls over such matters.

In keeping with general auditing practices, we do not examine every transaction, activity or area. Instead, the areas examined were those representing the highest risk of fraud, loss, abuse, or noncompliance. The following areas were examined during this audit period:

- Cash receipting
- Airport contracts
- Citations
- Financial condition
- Procurement
- Payroll
- Conflict of interest
- State grants

## SCHEDULE OF AUDIT FINDINGS AND RESPONSES

### **2013-001    The City of Arlington lacks adequate internal controls over Airport financial activities.**

#### ***Background***

In 1959 the City of Arlington took over operations of the Arlington Airport from the United States General Services Administration. The Airport leases property and buildings to private parties for general aviation uses. During 2013, the Airport had operating revenues of \$3,266,708 of which \$2,865,274 is from leasing activities.

State law prohibits resources restricted for certain uses such as airports from benefitting other funds (RCW 43.09.210). This includes the City's allocation of central services such as administration; payroll and purchasing that benefit multiple funds where it must adopt a fair and equitable method of distributing these shared costs among all the funds that benefit.

#### ***Description of Condition***

We reviewed the internal controls over leasing activities and cost allocations at the Airport. Our audit found:

- The City does not have contracts in place for all space leased at the Airport.
- The City has a relationship with a non-profit to provide services and to lease space from the City that mutually benefits both parties; however, the City does not have an agreement with the non-profit to define the mutual benefits received by both parties.
- The City does not bill for Airport leases and rentals timely; therefore, the Airport Fund loses the use of revenue for a short period of time by not receiving all funds owed for lease and rental revenue on time.
- The City does not ensure compliance with all written contract terms and City Municipal Code when in conflict.
- The City does not have an adequate review process to ensure the completion of the public safety survey in order to consistently apply shared costs of Police, Fire and Emergency Medical Services (EMS) to the Airport Fund.

- The City uses Airport facilities to provide office space for a department that performs general government services. The City's General Fund is benefitting from the use of Airport facilities without compensation, in violation of state law.

### *Cause of Condition*

The City has not made it a priority to provide ongoing training and education to Airport employees. Airport staff has primarily focused on maintaining compliance with federal requirements and have not applied the same attention to state requirements.

The City has experienced turnover in its Airport Supervisor and Airport Manager positions at the Airport.

In addition, the City was not aware it needed to have a comprehensive agreement to define the mutual benefits received by the City and a non-profit.

### *Effect of Condition*

Without adequate oversight and internal controls over operations at the Airport, the City cannot ensure it is receiving all funds owed and that the City is adequately and fairly allocating costs to the Airport for services received. Specifically, we found:

#### Airport Leases

- The City allowed a private business to operate and use additional Airport property without a signed lease modification since May 1, 2013. Although the business did make lease payments of \$512 for the months of May and June, the City did not properly bill for these amounts. Further, the City recorded the payments made to the wrong account.
- A non-profit organization has a lease for storage on Airport property that expired in 2006; however, the organization still stores equipment in the space. Although the lease expired in 2006, the non-profit still makes annual lease payments of \$941 for use of the space. The City did not update the amount of the lease payments, due to mutual benefits received by the City and the non-profit.
- The City also leases space to the non-profit organization to hold an aviation event each year. The contract, signed in 2001, requires the City to annually negotiate services in writing from the Arlington Fire Department, Police Department, and the City Planning Department for the event. In

2007, the City amended its Municipal Code to require all special event services to be negotiated during the permit application process, rather than through individual agreements. Although the City was able to demonstrate that the aviation services were approved through the permit process, the 2001 contract was not updated to agree to the City's Municipal Code. The contract also requires that all fees and charges totaling \$15,102 for the use of the site be paid on or before July 31st each year. The City did not bill for the fees timely and as a result, the payment was not received until October 1, 2014.

#### Use of Restricted Funds

- The City allocates costs to the Airport Fund for Police, Fire and EMS services. The City uses a survey of police hours spent patrolling on and around the Airport property to determine an allocation percentage for the services provided to the Airport. The City does have a written memo outlining the procedures to apply the survey to allocate the costs. However, the 2012 survey was not completed until 2013, which prevented the City's ability to correctly allocate costs for that year. As a result, 2012 costs were incorrectly allocated using the 2010 survey.
- The City moved its Community Planning and Development Department, part of the General Fund, to the Airport building in November 2013. The Airport Fund is not reimbursed for the Department's use of its space. Although this department does provide services to the Airport, the City did not have supporting documentation to demonstrate that the General Fund was not benefitting at the expense of the Airport Fund.

#### ***Recommendation***

We recommend the City:

Establish adequate internal controls, including oversight, over Airport financial activities to ensure the safeguards of public resources.

- Ensure it establishes contracts for all City property leased. The City should develop procedures to ensure contracts are established prior to the use of its property.
- Ensure there are procedures in place to monitor compliance with lease requirements, City policy, City Municipal code, and state law.

- Establish a mutual benefit agreement with the non-profit to outline the services to be provided by both parties. The City should periodically review this agreement and ensure the benefit of this arrangement outweighs any costs incurred by the City.
- Ensure an adequate review is performed over costs allocated to restricted funds to ensure costs are allocated in accordance with City approved plans, are consistently applied, and are supported.
- Analyze and review the services provided by the Community Planning and Development Department to the Airport Fund and ensure the Airport Fund is compensated by the General Fund for leased office space as appropriate.

### ***City's Response***

*The City is aware of its responsibility to maintain internal controls over Airport financial activities, and appreciates that our partners at the State Auditors' Office (SAO) have conducted a thorough review of the procedures at the Airport. With the diversity of businesses located at the airport, there is a labyrinth of regulation in everything from setting lease rates to taxes. Federal, state, county and local regulators include the Federal Aviation Administration, the state of Washington, Snohomish County, and the Arlington Municipal Code. It is challenging to determine which policies, procedures and practices prevail when they conflict.*

*In the specific examples raised by the SAO, the City points out that no loss of revenue to the airport occurred. All payments were received from the leaseholders, and the amounts represent just 0.6 percent of the total amount of revenue received from leasing activities.*

*Beginning in the fall of 2013, the Airport staff began a thorough review of all 200 Airport leases to ensure that they were all up to date. During this review, we discovered a number of leases that were out of date and began the process of bringing updated leases to the Airport Commission for approval. Also during this time the Airport Director retired and the Airport Manager departed for another job in a different state. An experienced Airport Manager was hired in August 2014 and has continued the lease review and updates. The new manager has also instituted a number of changes to improve the Airport's internal controls and tracking of financial activities. While the City does not believe it has had, or is having a loss of Airport revenue, it acknowledges that the procedures that have been put in place will more quickly identify a potential issue.*

*Prior to 2007, special events were reviewed inconsistently across the city. In an effort to bring consistency to the process, the City amended its Municipal Code to include a Special Event Permit process. During the review process, the*

*departments take into account any additional services required or costs incurred for the event. Permits for events are issued after this review has occurred and an agreement has been reached on additional services and costs. We find the special event issue to be inconsistent with prior Auditor comments about the precedence that the Municipal Code takes over all other documents, policies, and procedures that the City may have. The City believes the special event permitting process contained in the Municipal Code supersedes any prior agreements and individual department processes and procedures. The City will, however, update any outstanding agreements to clarify the proper process for review of special events is contained in the Municipal Code.*

*With respect to the biennial survey for allocating costs to the Airport Fund for Police, Fire, and EMS services, the City notes that the Memorandum of Understanding with the Federal Aviation Administration has been followed since its adoption in 1999. The only exception to this occurred in 2012, when the survey was performed a year late. The survey should have been completed and implemented for the 2013 budget, but due to staffing shortages in the Police Department, a lower priority was placed on the survey and it was not completed until 2013. The City does call attention to the fact that there was no loss of revenue to the Airport during that year.*

*As the Auditor is well aware, the City faced a significant fiscal crisis in the General Fund during the economic downturn. In an effort to be efficient with the taxpayer's dollars, the City deemed there were economies of scale to combine staff, office equipment and office space. All staff at the Airport Office perform duties for both the Airport and Community & Economic Development. The services provided to the Airport by Community & Economic Development staff are paid for by the Airport fund. In addition, all supplies, materials and equipment used by the staff are segregated and paid for out of the appropriate funds. The cost of all shared office equipment is split between funds. The City achieved a high level of cross training and integration of the Airport office staff into the Community & Economic Development Department with this consolidation, serving both the airport tenants and the taxpayers, and allowed the City to focus on rebuilding its reserves. In addition, the City believed there should be no charge for the space used by the Community & Economic Development staff as the Airport would not be able to lease the internal office space to any other business. The City will, however, review this usage to determine if any cost allocations to the Airport need to be made.*

*The City recognizes the importance of maintaining adequate internal controls, and appreciates the input from the SAO to assist with better safeguarding of public assets. We look forward to completing the update of our procedures,*

*tightening our airport leasing controls, which will continue to create an environment that draws aviators and businesses to our wonderful facility.*

### ***Auditor's Remarks***

We appreciate the City's cooperation and willingness to take corrective action to address the issues identified with airport operations during the current audit. We provide the following points of clarification to the City's response:

- We were unable to confirm the City's assertion that no revenue was lost as a result of the issues identified above. The absence of contracts for all space leased, continued use of expired contracts and delay in billing tenants timely increases the risk that the City is not receiving all amounts owed to it or current market rates for the space leased.
- It is City management's responsibility to ensure it complies with all legally binding documents, including contracts and municipal codes. The City was unable to demonstrate how municipal codes take precedence over previously executed contracts.
- Although the City stated that no revenues were lost due to the untimely completion of the 2012 biennial survey of public safety expenditures, the audit concern is focused on the City allocating estimated costs to the restricted Airport Fund rather than actual expenditure amounts. The completion of the survey has no impact on revenues.

The State Auditor's Office will review the City's corrective action taken during our next audit.

### ***Applicable Laws and Regulations***

RCW 43.09.210 Local Government Accounting – Separate accounts for each fund or activity – Exemption for agency surplus personal property

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.

All unexpended balances of appropriations shall be transferred to the fund from which appropriated, whenever the account with an appropriation is closed.

This section does not apply to agency surplus personal property handled under \*RCW 43.19.1919(5).

RCW 43.09.200 – Local government accounting – Uniform System of Accounting, states:

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 therefore; 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 (BARS) manual - Accounting, Accounting Principles and General Procedures, Internal Control*, states in part:

Internal control is a management process for keeping an entity on course in achieving its business objectives, as adopted by the governing body. This management control system should ensure

that resources are guarded against waste, loss and misuse; that reliable data is obtained, maintained, and fairly disclosed in financial statement and other reports; and resource use is consistent with laws, regulations and policies. Each entity is responsible for establishing and maintaining an effective system of internal control throughout their government.

Chapter 3.1.3.30 of the *Budgeting, Accounting, and Reporting System* (BARS) manual states in part:

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.

#### City of Arlington Municipal Code

##### 2.44.030 - Commission powers and duties.

The commission established in Section 2.44.010 is granted authority to construct, enlarge, improve, maintain, equip, operate and regulate said airport and airport facilities, but remain in all these things accountable to the city council. So long as decisions of the airport commission are consistent with the approved airport master plan, the Arlington comprehensive plan, all other provisions of the Arlington Municipal Code and applicable federal regulations, the annual airport budget, the airport capital improvement plan, and approved lease policies, the airport commission may exercise the following powers and responsibilities without formal review or ratification by the city council, except when formal review is deemed appropriate by the airport manager:

- (1) Leasing and development of airport property, including amendments or modifications to leases and the granting or requests for subordination of leasehold interests or other security interests for financing purposes;

(2) Capital improvements to airport properties, including, when appropriate, the application for federal or state grants to finance the same; and

(3) Amendments to airport leasing and operational policies, rules and requirements.

## RELATED REPORTS

### **Financial**

Our opinion on the City's financial statements and compliance with federal grant program requirements is provided in a separate report, which includes the City's financial statements.

### **Federal grant programs**

We evaluated internal controls and tested compliance with the federal program requirements, as applicable, for the City's major federal program, which is listed in the Federal Summary section of the financial statement and single audit report.

## INFORMATION ABOUT THE CITY

The City of Arlington was incorporated in 1903. Located in Snohomish County, the City has a population of approximately 18,300 citizens. The City provides a full range of services including police, fire, emergency medical services, water distribution, sewage collection and treatment, street maintenance, parks maintenance, planning, a municipal cemetery and a municipal airport.

An elected, seven-member City Council and a separately elected Mayor govern the City. The City Council appoints a City Administrator to oversee the City's daily operations as well as its approximately 125 full-time employees. For the year ended December 31, 2013, the City operated on an annual budget of approximately \$52 million, including capital projects.

Contact information related to this report	
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*Information current as of report publish date.*

### Audit history

You can find current and past audit reports for the City of Arlington at <http://portal.sao.wa.gov/ReportSearch>.

## 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.

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