

Schedule of Federal Audit Findings and Questioned Costs

Malaga Water District
Chelan County
January 1, 2008 through December 31, 2008

1. The District's controls over financial statement preparation are inadequate to ensure accurate reporting and compliance with federal regulations.

CFDA Number and Title:	10.760 Water and Waste Disposal Systems for Rural Communities
Federal Grantor Name:	Department of Agriculture Rural Development
Federal Award/Contract Number:	9105, 56-004
Pass-through Entity Name:	NA
Pass-through Award/Contract Number:	NA
Questioned Cost Amount:	\$0

Background

District management, the state Legislature, state and federal agencies and bondholders rely on the information included in financial statements and supplemental schedules to make decisions. It is the responsibility of District management to design and follow internal controls that provide reasonable assurance regarding the reliability of financial reporting.

Our audit identified material weaknesses in internal controls over financial reporting that could affect the District's ability to produce reliable financial statements.

Government Auditing Standards, prescribed by the Comptroller General of the United States, require the auditor to communicate material weaknesses, as defined below in the Applicable Laws and Regulations section, as a finding.

Description of Condition

We identified a control deficiency that represents a material weakness in internal controls over financial reporting.

- The District's manager did not have adequate technical knowledge of and experience with the financial reporting requirements detailed in the *Budgeting, Accounting, and Reporting Standards* (BARS) Manual to prepare accurate and complete financial statements and the supporting schedules, such as the Schedule of Expenditures for Federal Awards (SEFA), for audit.

- The Board did not have an oversight process in place to ensure the financial statements and applicable supporting schedules were appropriately prepared for audit.

Cause of Condition

The District has not received large amounts of federal grants in the past, which would require it to prepare financial statements for audit. As a result, it has not designed sufficient controls to ensure that financial statements, including its SEFA, were accurately prepared for audit.

Effect of Condition

The District was unable to prepare accurate financial statements or the SEFA. However, we were able to issue an unqualified opinion on the SEFA after subsequent corrections. Inaccurate information prevents the Board Members and other interested parties from having an independent opinion on the financial results of the District's operations.

The District also did not obtain the required audit of federal grant expenditures and submit a federal single audit report to the Federal Clearinghouse by the September 30, 2009 deadline.

Recommendation

We recommend the District:

- Train appropriate employees regarding the BARS Manual reporting requirements to ensure the required financial statements and schedules are accurately prepared.
- Implement additional internal controls over financial reporting, including detailed review and monitoring of the financial reports, by a knowledgeable person other than the person preparing them, before they are submitted for audit.
- Establish the necessary policies and procedures to identify the District's federal grant expenditures and to ensure compliance with audit requirements.

District's Response

In response to your schedule of audit findings and responses the District makes the following comments.

- *The District is sending its manager to seminars presented by the Washington Financial Officers Association to improve its knowledge of, and the use of forms and schedules required by the Auditor's Office.*
- *If in the future, the District expends federal funds, the District will designate an appropriately trained person to ensure compliance with report requirements.*

Auditor's Remarks

We appreciate the District's timely response and commitment to the resolution of these issues and thank District staff and management for their cooperation and assistance during our audit. We will follow up on these matters in our next audit.

Applicable Laws and Regulations

OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, states in part:

Section 200, Audit requirements.

(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.

(b) Single audit. 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 audit conducted in accordance with §____.500 except when they elect to have a program-specific audit conducted in accordance with paragraph

(c) of this section.

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 . . .

(b) Loan and loan guarantees (loans). Since the Federal Government is at risk for loans until the debt is repaid, the following guidelines shall be used to calculate the value of Federal awards expended under loan programs, except as noted in paragraphs (c) and (d) of this section:

(1) Value 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.

Section 320, Report Submission.

(a) General. The audit shall be completed and the data collection form described in paragraph (b) of this section and reporting package described in paragraph (c) of this section shall be submitted within the earlier of 30 days after receipt of the auditor's report(s), or nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audit

Section 300 outlines the local government's responsibilities.

The auditee shall:

(e) Ensure that the audits required by this part are properly performed and submitted when due.

RCW 43.09.200 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 whatsoever, and by all public officers, employees, and other persons.

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

Statement on Auditing Standards No. 115, issued by the Auditing Standards Board of the American Institute of Certified Public Accountants, defines material weakness and significant deficiency as follows:

a. Material weakness: 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.

b. Significant deficiency: 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.