

Washington State Auditor's Office
Financial Statements Audit Report

City of North Bonneville
Skamania County

Audit Period
January 1, 2009 through December 31, 2010

Report No. 1007203

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February 13, 2012



WASHINGTON
BRIAN SONNTAG
STATE AUDITOR



**Washington State Auditor
Brian Sonntag**

February 13, 2012

Mayor and City Council
City of North Bonneville
North Bonneville, Washington

Report on Financial Statements

Please find attached our report on the City of North Bonneville's financial statements.

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

Sincerely,

BRIAN SONNTAG, CGFM
STATE AUDITOR

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Skamania County
January 1, 2009 through December 31, 2010**

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Schedule of Audit Findings and Responses

**City of North Bonneville
Skamania County
January 1, 2009 through December 31, 2010**

1. The City's internal controls are inadequate to ensure accurate accounting and reliable financial reporting.

Background

City management, the state Legislature, state and federal agencies and bondholders rely on the information included in financial statements and reports to make decisions. It is the responsibility of City management to design and follow internal controls that provide reasonable assurance regarding the reliability of financial reporting. Our audit identified deficiencies in internal controls that adversely affect the City'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 the following deficiencies in internal controls over financial reporting that, when taken together, represent a material weakness:

- The City does not have procedures to ensure bank statements are reconciled in a timely manner. We found the City did no reconciliations of the bank statements to the City's financial records in 2009 or the first half of 2010. While it did reconciliations of activity for the remainder of 2010, at the time of our audit we found it had done no reconciliations in 2011.
- The City does not have policies or procedures to ensure its financial information is accurate, complete, and properly reported.
- The Mayor and City Council review and approve vouchers and warrants but do not review all of the City's financial activity, such as financial statements, bank statement reconciliations, manual payments or other information for accuracy.

Cause of Condition

The City has limited staffing and relies on the Clerk-Treasurer to maintain accurate accounting records and provide information to the Council. No one has been assigned to review or monitor accounting records or reports. The Mayor and City Council have not taken an active role in ensuring the City's financial information is accurate and complete.

Effect of Condition

The City is unable to provide accurate financial information to the Council and citizens. While the City has hired a new Clerk/Treasurer, it has not been able to identify errors in and make corrections to the accounting records. In addition, the City is unable to accurately identify the cash balances for each fund. As a result, we are unable to express an opinion on the financial statements for 2009 and 2010.

In addition, the City's financial condition is declining. Without accurate and complete financial records, the City is unable to effectively monitor its budget and financial condition. The City estimates that several funds, including the General Fund, will end in a negative cash position at the end of 2011. See Finding #2.

These deficiencies in internal controls increase the risk that significant misstatements in the financial information, or misappropriation or misuse of City resources, could occur and not be prevented or detected by the City.

Recommendation

We recommend the City:

- Ensure adequate oversight of financial operations and accounting functions, including reviews of monthly bank reconciliations to ensure they are accurate and complete.
- Establish internal controls procedures to ensure all City activity is recorded in the general ledger accurately and completely.
- Establish internal controls and dedicate the necessary resources to ensure a thorough review of the financial activity of the City is conducted, including financial statements and related schedules to ensure accurate presentation.

City's Response

The city acknowledges the audit findings and recommendations. The city council repeatedly requested better reporting and more detailed information from city staff since 2008. In June 2010 the city hired a new clerk / treasurer who has already addressed many of the findings as detailed below. Those findings not previously addressed were addressed by the end of 2011 as described below and are the subject of continuing efforts by the city council, the mayor and staff to effectively manage operations, improve the city's financial condition, strengthen internal controls and ensure compliance with state laws and regulations.

In the summer of 2010, the clerk/treasurer began drafting a manual of policies and procedures designed to ensure proper controls and processes are followed. The city will continue work in 2012 to ensure better oversight, controls and fiscal responsibility.

While they were inadequate, reconciliations were performed in 2011. The clerk/treasurer delayed completing formal reconciliations to resolve outstanding cash reconciliation issues from 2010. Now that those issues have been resolved, proper reconciliations are being performed.

While requiring the city council to "review all the city's financial activity" would be burdensome, the council needs to review enough activity to ensure that reporting is accurate. The councils during the audit period repeatedly asked for more detailed

financial information, but were unable to obtain it in a timely fashion. The clerk / treasurer began providing more complete information in the summer of 2010, including regular budget-to-actual reports, summaries of non-cash transactions, and summaries of the city's financial position to ensure the council has sufficient information to perform their duties.

The city acknowledges but disagrees with the auditor's finding that the mayor and council have not taken an active role in ensuring the city's financial information is accurate and complete. They have prioritized the city's limited resources on operational and budgetary issues and will continue to strengthen and improve reporting, as well as resolve any remaining accounting issues.

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

RCW 43.09.230 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.

The reports shall be certified as to their correctness by the state auditor, the state auditor's deputies, or other person legally authorized to make such certification.

Their substance shall be published in an annual volume of comparative statistics at the expense of the state as a public document.

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 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 there from; 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.

Budgeting, Accounting and Reporting System Manual - Part 3, Accounting, Chapter 1. Accounting Principles and General Procedures, Section B. Internal Control, 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.

Government Auditing Standards, July 2007 Revision – Section 5.11, provides that auditors should report significant deficiencies and material weaknesses in internal control.

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.

Schedule of Audit Findings and Responses

**City of North Bonneville
Skamania County
January 1, 2009 through December 31, 2010**

- 2. The City has not effectively managed its operations, resulting in a decline in its financial condition.**

Description of Condition

The City's financial position has declined over the past several years. The City's total cash and investment balances were:

Fiscal Year	Total Cash & Investments
2006	\$1,507,560
2007	1,495,257
2008	1,198,771
2009	1,205,111
2010	743,099
October 31, 2011	258,696

The City is unable to determine how much of the total cash and investment balance belongs to each fund and as a result, cannot determine how much of the total is restricted and not available for general spending.

The City is anticipating that at the end of fiscal year 2011 several funds will have a deficit, including the General, Water, and Sewer funds. These funds will require an inter-fund loan from restricted funds in order to continue operations.

Cause of Condition

The Mayor and City Council have not prioritized monitoring of financial information to ensure it is accurate and complete. Without accurate and complete financial information, they have been unable to make informed decisions that affect the City's financial condition.

Effect of Condition

The City is at risk of not being able to meet financial obligations or maintain services at its current levels. This could result in the City needing to take out bank loans or to find alternate funding sources, which would be an additional cost to its ratepayers and taxpayers.

Furthermore, without a feasible plan to cut expenses, the City is at risk of not being able to pay back the inter-fund loans, which would represent an inappropriate permanent diversion of restricted funds.

Recommendation

We recommend the Mayor and City Council develop a written strategy for achieving and maintaining a positive fund balance that meets the current needs and future obligations of the City.

We further recommend the City make it a priority to ensure their financial information and accounting records are accurate and complete to assist with the monitoring of financial operations.

City's Response

The city acknowledges the audit findings and recommendations. The city council repeatedly requested better reporting and more detailed information from city staff since 2008. In June 2010 the city hired a new clerk / treasurer who has already addressed many of the findings as detailed below. Those findings not previously addressed were addressed by the end of 2011 as described below and are the subject of continuing efforts by the city council, the mayor and staff to effectively manage operations, improve the city's financial condition, strengthen internal controls and ensure compliance with state laws and regulations.

The city notes that the decline is particularly pronounced in its General Fund, a trend that began in 2008 with a reduction of about \$231,000. The city further notes that \$259,000 of the reduction in cash position was due to appropriate investments in a new sewer treatment plant. Finally, the city notes that considerable resources were required to resolve a number of personnel matters.

The city has also taken numerous steps to reduce expenses and increase revenues. The 2011 budget decreased expenses from 2009 by \$230,000, and the 2012 budget (passed before the preliminary findings from this audit were released) projects revenue surpluses in every fund. The city has decreased staffing from 7.5 FTEs to 5.75 FTEs and anticipates a further 1 FTE reduction in 2012.

Along with reducing expenses, the city increased revenues by restructuring and raising utility rates for the first time in 10 years and the utility tax rate from 5% to 6%. In 2012 the city will actively explore further cost savings that will improve the city's overall financial condition.

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

SAS No. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, provides guidance on the auditor's evaluation of whether there is substantial doubt about the entity's ability to continue as a going concern. Ordinarily, financial statements of a governmental unit are prepared based on the assumption that the reporting entity will continue as a going concern. SAS No. 59 relates going concern to the entity's ability to continue to meet its obligations as they become due without

substantial disposition of assets outside the ordinary course of business, restructuring of debt, externally forced revisions of its operations, or similar actions.

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.

Part 3, Chapter 4 of the *Budgeting, Accounting and Reporting System* (BARS) manual, states in part, the acceptable procedures for making and accounting for inter-fund loans are as follows:

3. The borrowing fund must anticipate sufficient revenues to be in a position over the period of the loan to make the specified principal and interest payments as required in the authorizing ordinance or resolution.
4. The term of the loan may continue over a period of more than one year, but must be “temporary” in the sense that no permanent diversion of the lending fund results from the failure to repay by the borrowing fund. A loan that continues longer than three years will be scrutinized for a “permanent diversion” of moneys. (Note: these restrictions and limitations do not apply to those funds which are legally permitted to support one another through appropriations, transfers, advances, etc.)

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters in Accordance with *Government Auditing Standards*

**City of North Bonneville
Skamania County
January 1, 2009 through December 31, 2010**

Mayor and City Council
City of North Bonneville
North Bonneville, Washington

We were engaged to audit the financial statements of the City of North Bonneville for the years ended December 31, 2010 and 2009. However, we were not able to obtain financial statements supporting the financial activities of the City for the years ended December 31, 2010 and 2009, nor were we able to satisfy ourselves as to those financial activities by other auditing procedures. Accordingly, we do not express an opinion on the financial activities of the City for 2010 and 2009. In addition, our report includes information about the status of the City's financial condition. This information is more fully described in the Schedule of Audit Findings and Responses, Finding 1.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audits, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Audit Findings and Responses, we identified certain deficiencies in internal control over financial reporting 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 City's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Audit Findings and Responses as Finding 1 to be material weaknesses.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of the City'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 financial statement 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*.

The City's response to the finding identified in our audit is described in the accompanying Schedule of Audit Findings and Responses. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended for the information and use of management and the Mayor and City Council. 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, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

BRIAN SONNTAG, CGFM
STATE AUDITOR

November 14, 2011

Independent Auditor's Report on Financial Statements

City of North Bonneville Skamania County January 1, 2009 through December 31, 2010

Mayor and City Council
City of North Bonneville
North Bonneville, Washington

We were engaged to audit the financial statements of the City of North Bonneville for the years ended December 31, 2010 and 2009. Financial statements are the responsibility of the City's management.

The City did not provide accurate financial statements or supporting schedules for the periods ended December 31, 2010 and 2009, and therefore, representations of the City's financial activities were not available for audit. Further, the City did not retain sufficient documentation in support of transactions to allow us to evaluate the fair statement of revenues and expenditures in the financial statements for the periods ended December 31, 2010 and 2009. The City's records do not permit the application of other auditing procedures to evaluate the fair statement of revenues and expenditures.

As described in Finding 2 in the Schedule of Audit Findings and Responses, the City's declining cash and investment balances and negative balance in the general fund as of December 31, 2010, reflects the significant cash flow challenges that affect City operations. The City's cash flow constraints are expected to continue in the near future. As a result, there exists substantial uncertainty about the City's ability to maintain services at present levels under these conditions.

Since the City did not retain sufficient documentation and we were not able to apply other auditing procedures to satisfy ourselves as to the fair statement of revenues and expenditures, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements. The statements are not included in our report.

In accordance with *Government Auditing Standards*, we have also issued our report on our consideration of the City'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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" written in a larger, more prominent script than the last name "Sonntag".

BRIAN SONNTAG, CGFM
STATE AUDITOR

November 14, 2011



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.

Our mission is to work with our audit clients and citizens as an advocate for government accountability. 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.

The State Auditor's Office employees are located around the state to deliver services effectively and efficiently.

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 and fraud, whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our Web site and through our free, electronic subscription service.

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

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