



Washington State Auditor's Office

Independence • Respect • Integrity

Federal Single Audit Report

City of Seattle

King County

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

Published September 30, 2015

Republished January 25, 2016

Report No. 1015224





Washington State Auditor's Office

January 25, 2016

Mayor and City Council
City of Seattle
Seattle, Washington

Report on Federal Single Audit

Please find attached our report on the City of Seattle's compliance with requirements applicable to each of its major federal programs in accordance with OMB Circular A-133.

We are issuing this report in order to provide information on specific financial activities of the City.

Sincerely,

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

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FEDERAL SUMMARY

**City of Seattle
King County
January 1, 2014 through December 31, 2014**

The results of our audit of the City of Seattle are summarized below in accordance with U.S. Office of Management and Budget Circular A-133.

Financial Statements

We issued an unmodified opinion on the City's financial statements of the governmental activities, the business-type activities, each major fund and the aggregate discretely presented component units and remaining fund information in our separately issued audit report dated June 29, 2015.

Internal Control Over Financial Reporting:

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

We noted no instances of noncompliance that were material to the financial statements of the City.

Federal Awards

Internal Control Over Major Programs:

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

We issued an unmodified opinion on the City's compliance with requirements applicable to each of its major federal programs.

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

Identification of Major Programs:

The following were major programs during the period under audit:

<u>CFDA No.</u>	<u>Program Title</u>
93.044	Aging Cluster - Special Programs for the Aging - Title III, Part B - Grants for Supportive Services and Senior Centers
93.045	Aging Cluster - Special Programs for the Aging - Title III, Part C - Nutrition Services
93.053	Aging Cluster - Nutrition Services Incentive Program
14.218	CDBG - Entitlement Grants Cluster - Community Development Block Grants/Entitlement Grants
20.500	Federal Transit Cluster - Federal Transit - Capital Investment Grants
20.507	Federal Transit Cluster - Federal Transit - Formula Grants
20.205	Highway Planning and Construction Cluster - Highway Planning and Construction
14.267	Continuum of Care Program
81.128	ARRA-Energy Efficiency and Conservation Block Grant Program
93.568	Low Income Home Energy Assistance
97.067	Homeland Security Grant Program

The dollar threshold used to distinguish between Type A and Type B programs, as prescribed by OMB Circular A-133, was \$3,000,000.

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

SCHEDULE OF FEDERAL AUDIT FINDINGS AND QUESTIONED COSTS

City of Seattle

King County

January 1, 2014 through December 31, 2014

2014-001 City of Seattle's Office of Housing did not have adequate internal controls to ensure compliance with federal requirements for its Homewise program.

CFDA Number and Title:	93.568 Low Income Home Energy Assistance Program (LIHEAP)
Federal Grantor Name:	U.S. Department of Health and Human Services
Federal Award/Contract Number:	009483561
Pass-through Entity Name:	Department of Commerce
Pass-through Award/Contract Number:	F13-43101-404
Questioned Cost Amount:	\$88,784

Description of Condition

City of Seattle's Office of Housing spent \$3.9 million on the Homewise program during fiscal year 2014, of which \$2 million was funded by multiple federal grants through the Washington State Department of Commerce. The objective of the program is to provide weatherization upgrades to low-income individuals.

Federal regulations require that costs charged to the grants are allocable based on benefits received. Therefore, administration costs should be allocated based on percentage of weatherization projects funded. For employees who worked on more than one grant, federal regulations also require a monthly time-and-effort certification detailing the time spent for each grant.

During our review of the Office of Housing's internal controls over cost allocation and time-and-effort requirement, we found the Office of Housing:

- Did not allocate the actual administration costs proportionately based on actual expenditures because of funding restrictions of certain funding sources. As a result, federal grants are paying administration costs that should have been charged to other sources.

- Did not require time-and-effort certifications to include the details of the time and costs charged to each federal grant.

We consider these control deficiencies, collectively, to be a significant deficiency.

Cause of Condition

The Office of Housing had insufficient knowledge of the federal requirements on cost allocation and time and effort requirements.

Effect of Condition and Questioned Costs

Without ensuring that costs are allocated based on actual activities, the Office of Housing is not in compliance with the federal cost principles requirements resulting in questioned costs. The Office of Housing charged an additional \$88,784 in administration costs to the Low Income Home Energy Program that were unallowable to the grant.

Without proper time-and-effort certification, the Office of Housing is not in compliance with federal time and effort requirements. Our audit found that the timesheets for the Homewise program did not include the actual time spent for each grant. However, we were able to determine that all costs charged to the program are for allowable activities. As a result, we are not questioning these costs.

Recommendation

We recommend that Office of Housing staff certify their payroll charges to the Low Income Home Energy Assistance grant on a monthly basis and these certifications reflect actual activity of each employee.

In addition, we recommend that the cost allocation be equitably divided among funding sources, or that unfunded portions be covered with unrestricted sources.

City's Response

The major sources of funding for the HomeWise program include Seattle City Light (SCL) and a variety of state and federal sources that flow through the Washington State Department of Commerce. In 2014, SCL represented approximately half of all HomeWise capital costs. Therefore, in 2014, the Office of Housing (OH) requested that SCL pay for half of HomeWise administrative costs. Unfortunately, SCL capped the administrative amount at less than their pro-rata share, which created this issue.

However, it is important to recognize that SCL dollars directly result in the HomeWise program's ability to generate additional units. SCL capital funds

stretch state and federal dollars further. Often, the combination of SCL capital funds and other grant funds creates a large enough subsidy to incentivize multi-family property owners to participate. Because of this leverage, the Department of Commerce grants are reaching more units than they would otherwise.

In response to the recommendation that the cost allocation be equitably divided, OH will do the following:

- a) OH will continue to request that SCL pays their pro-rata administrative share.*
- b) OH will request unrestricted funds from the City Budget Office for the gap in the event that SCL does not pay equitably. In the period of this audit, OH had a very small amount of City General Fund that was assigned for a specific purpose outside of the HomeWise program. And as of 2017, OH will not have any unrestricted funds. OH is fully funded by restricted sources that cannot be used for the HomeWise program.*
- c) OH will seek to continue to discuss this issue with funders in order to reach an understanding of the definition of an equitable administrative share given the significant leverage they receive.*

In response to the recommendation that OH certifies payroll charges to the LIHEAP grant on a monthly basis instead of quarterly as is the current practice:

Making this change would actually make the distribution of administrative costs less equitable across grants. To illustrate this point, please consider the following scenario.

The HomeWise program used \$1.5 million of capital from Grant A in a given year. Most of this capital was expended in three large segments because it was used for large, multi-family projects. The total HomeWise capital budget in the same year was \$3.2 million, meaning that other grants paid the remaining \$1.7 million in capital. HomeWise administrative, non-capital expenses are a fixed amount of \$130,000 a month, for a total annual amount of \$1.56 million.

The most equitable way to assign administrative costs would be to apply the share on an annual basis. Grant A represents 47% of the capital in a given year, and therefore should cover 47% of the administrative costs that year, or \$731,250. Unfortunately, HomeWise cannot assign administrative expenses on an annual basis because grants in the program have a variety of closing dates that happen throughout the year. We would be unable to charge administrative expenses to a grant after its closing date.

If administrative expenses were assigned on a monthly basis, the distribution would look as follows, and the total amount of administrative expenses paid for that year by Grant A would be \$428,753, far below what it should be, given the amount of capital covered by Grant A:

<i>Month</i>	<i>Amount of Capital Paid for by Grant A</i>	<i>Amount of Capital Paid for by Other Grants</i>	<i>Percentage of Capital Represented by Grant A</i>	<i>Applying this Percentage, Amount of Labor Expenses Paid for By Grant A</i>
<i>January</i>	\$0	\$50,000	0%	\$0
<i>February</i>	\$0	\$100,000	0%	\$0
<i>March</i>	\$700,000	\$0	100%	\$130,000
<i>April</i>	\$0	\$570,000	0%	\$0
<i>May</i>	\$270,000	\$40,000	87%	\$113,226
<i>June</i>	\$10,000	\$320,000	3%	\$3,939
<i>July</i>	\$0	\$250,000	0%	\$0
<i>August</i>	\$0	\$190,000	0%	\$0
<i>September</i>	\$20,000	\$25,000	44%	\$57,778
<i>October</i>	\$500,000	\$25,000	95%	\$123,810
<i>November</i>	\$0	\$60,000	0%	\$0
<i>December</i>	\$0	\$70,000	0%	\$0

Total: \$428,753

Because capital expenditures are incurred in large amounts at isolated points of the year – rather than evenly distributed each month – the quarterly time horizon mitigates these spikes and allows for a more equitable distribution of administrative expenses. If administrative expenses were assigned on a quarterly basis, the distribution would look as follows, and the total amount of administrative expenses paid for that year by Grant A would be \$725,217, much closer to the accurate annualized amount:

<i>Quarter</i>	<i>Amount of Capital Paid for by Grant A</i>	<i>Amount of Capital Paid for by Other Grants</i>	<i>Percentage of Capital Represented by Grant A</i>	<i>Applying this Percentage, Amount of Labor Expenses Paid for By Grant A</i>
<i>1</i>	<i>\$700,000</i>	<i>\$150,000</i>	<i>82%</i>	<i>\$321,176</i>
<i>2</i>	<i>\$280,000</i>	<i>\$930,000</i>	<i>23%</i>	<i>\$90,248</i>
<i>3</i>	<i>\$20,000</i>	<i>\$465,000</i>	<i>4%</i>	<i>\$16,082</i>
<i>4</i>	<i>\$500,000</i>	<i>\$155,000</i>	<i>76%</i>	<i>\$297,710</i>

Total: \$725,217

Therefore, OH will continue to distribute administrative costs on a quarterly basis. Per the recommendation, OH will add the process of completing time and effort certifications on a quarterly basis.

Auditor's Remarks

For employees who worked on more than one grant, federal regulations require a monthly time-and-effort certification detailing the time spent for each grant.

We thank the City for its assistance during the audit and will follow up on corrective actions taken during the 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 Auditee responsibilities.

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 the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

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

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 noncompliance. In the absence of a definition of material noncompliance in the governmental audit requirement a failure to follow compliance requirements or a violation of prohibitions included in the applicable compliance requirements that results in noncompliance that is quantitatively or qualitatively material either individually or when aggregated with other noncompliance to the affected government program.

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.

U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, Attachment A, Section C, states in parts:

- 1) Factors affecting allowability of costs. To be allowable under Federal awards, costs must meet the following general criteria:
 - a. Be necessary and reasonable for proper and efficient performance and administration of Federal awards.

- b. Be allocable to Federal awards under the provisions of this Circular.
- c. Be authorized or not prohibited under State or local laws or regulations.
- d. Conform to any limitations or exclusions set forth in these principles, Federal laws, terms and conditions of the Federal award, or other governing regulations as to types or amounts of cost items.
- e. Be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities of the governmental unit.
- f. Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.
- g. Except as otherwise provided for in this Circular, be determined in accordance with generally accepted accounting principles.
- h. Not be included as a cost or used to meet cost sharing or matching requirements of any other Federal award in either the current or a prior period, except as specifically provided by Federal law or regulation.
- i. Be the net of all applicable credits.
- j. Be adequately documented.

3. Allocable costs.

- a. A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.

- b. All activities which benefit from the governmental unit's indirect cost, including unallowable activities and services donated to the governmental unit by third parties, will receive an appropriate allocation of indirect costs.
- c. Any cost allocable to a particular Federal award or cost objective under the principles provided for in this Circular may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by law or terms of the Federal awards, or for other reasons.
- d. Where an accumulation of indirect costs will ultimately result in charges to a Federal award, a cost allocation plan will be required as described in Attachments C, D, and E.

U.S. Office of Management and Budget Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, Attachment B, Section 8h, states in part:

(4) Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation which meets the standards in subsection (5) unless a statistical sampling system (see subsection (6)) or other substitute system has been approved by the cognizant Federal agency. Such documentary support will be required where employees work on:

- (a) More than one Federal award,
- (b) A Federal award and a non-Federal award,
- (c) An indirect cost activity and a direct cost activity,
- (d) Two or more indirect activities which are allocated using different allocation bases, or
- (e) An unallowable activity and a direct or indirect cost activity.

(5) Personnel activity reports or equivalent documentation must meet the following standards:

- (a) They must reflect an after the fact distribution of the actual activity of each employee,
- (b) They must account for the total activity for which each employee is compensated,
- (c) They must be prepared at least monthly and must coincide with one or more pay periods, and
- (d) They must be signed by the employee.

City's Low Income Home Energy Assistant Program agreement states in part:

Administrative Cost Allocation

Allowable administrative costs actually incurred in operating activities funded under this Grant may be charged to this Grant.

Administrative services shared by other programs shall be assigned to this Grant based on an allocation plan that reflects allowable administrative costs that support services provided under each Grant administered by COMMERCE. An approved current federal indirect cost rate may be applied up to the maximum administrative budget allowed.

Allowable Costs (Performance Measures)

For allowable use of LIHEAP Program funds, refer to the Weatherization Manual for Managing the Low-Income Weatherization Program, as applicable.

Washington State Department of Commerce Weatherization Manual Chapter 6 Section 3.1.2, states

Commerce funds for weatherization must not be used to supplant other funds or programs.

Washington State Department of Commerce Weatherization Manual Chapter 6
Section 6.2A9, states

Authorized Expenditures

OMB (Office of Management and Budget) Circular A-87, Cost Principles for State, Local, and Indian Tribal Governments, and OMB Circular A-122, Cost Principles for Nonprofit Organizations, are used as general guidelines for determining which weatherization costs are allowed.

- a. Exceptions exist where costs conform to specific categories in the applicable contract, policies and procedures, weatherization budget, state law, or local ordinance.
- b. Commerce determines the proper interpretation of the federal or state procedures as they relate to costs allowed or prohibited under this program.

STATUS OF PRIOR FEDERAL AUDIT FINDINGS

This schedule presents the status of federal findings reported in prior audit periods. The status listed below is the representation of the City of Seattle. The State Auditor’s Office has reviewed the status as presented by the City.

Audit Period: 2013	Report Ref. No.: 1012743	Finding Ref. No.: 1	CFDA Numbers: 14.235, 14.267 and 14.218
Federal Program Name and Granting Agency: U. S. Department of Housing and Urban Development: <ul style="list-style-type: none"> Supportive Housing Program Continuum of Care Program Community Development Block Grant 		Pass-Through Agency Name: NA	
Finding Caption: The Seattle Human Services Department does not have adequate internal controls to effectively monitor service providers for grant compliance.			
Background: Audit reported control and compliance issues over activities allowed, allowable costs, eligibility, period of availability, procurement, matching, program income, reporting and subrecipient monitoring compliance areas. Questioned costs were <ul style="list-style-type: none"> Supportive Housing Program \$744,907, Continuum of Care Program \$1,704,044 Community Development Block Grant \$202,752 			
Status of Corrective Action: (check one) <input checked="" type="checkbox"/> Fully Corrected <input type="checkbox"/> Partially Corrected <input type="checkbox"/> No Corrective Action Taken <input type="checkbox"/> Finding is considered no longer valid			
Corrective Action Taken: <i>The City of Seattle, Human Services Department (HSD) created and implemented new standard procedures “<u>Documents Required for Invoice Payment by Contract, Checklist</u>” for invoices, including adequate supporting documentation and monthly status reports, to ensure service providers are complying and meeting the requirements and expectations set forth in contract agreements.</i> <i>These new procedures were vetted with HSD Program Specialists and providers; additionally several trainings were provided to HSD Program Specialists and providers in January and February of 2015.</i> <i>HSD is in the process of developing improved procedures and practices for monitoring providers, contracts and payments.</i>			

Audit Period: 2013	Report Ref. No.: 1012743	Finding Ref. No.: 2	CFDA Number(s): 93.044, 93.045 and 93.053
Federal Program Name and Granting Agency: U.S. Department of Health and Human Services Centers: <ul style="list-style-type: none"> • Special Programs for the Aging – Title III, Part, B – Grants for Supportive Services and Senior Centers • Special Programs for the Aging – Title III, Part C – Nutrition Services • Nutrition Services Incentive Program 		Pass-Through Agency Name: Department of Social and Health Services	
Finding Caption: The City did not comply with all requirements for charging payroll and benefits to the Aging Cluster of programs.			
Background: Audit reported questioned costs of \$72,401 for salaries/wages and related benefits.			
Status of Corrective Action: (check one) <input checked="" type="checkbox"/> Fully Corrected <input type="checkbox"/> Partially Corrected <input type="checkbox"/> No Corrective Action Taken <input type="checkbox"/> Finding is considered no longer valid			
Corrective Action Taken: <i>The Human Services Department's (HSD) Finance and Human Resources units evaluated timesheet entry and approval processes; modifying steps to ensure improvement related to the corrective action. The Director of Finance and Contracts communicated to all HSD staff in December 2014 the new expectations for timesheet entry and approval. As of December 3, 2014, employees are signing timesheets at the end of their shift on the last day of the pay period.</i>			

Audit Period: 2013	Report Ref. No.: 1012743	Finding Ref. No.: 3	CFDA Number(s): 81.128 ARRA
Federal Program Name and Granting Agency: Energy Efficiency and Conservation Block Grant, U.S. Department of Energy		Pass-Through Agency Name: NA	
Finding Caption: The City should improve monitoring of charges between its departments.			
Background: Audit report disclosed control and compliance issues over activities allowed and allowable costs compliance areas. Questioned costs were \$205,622.			
Status of Corrective Action: (check one) <input checked="" type="checkbox"/> Fully Corrected <input type="checkbox"/> Partially Corrected <input type="checkbox"/> No Corrective Action Taken <input type="checkbox"/> Finding is considered no longer valid			

Corrective Action Taken:

OSE took a number of actions to correct deficiencies in three areas. The following identifies actions taken in each.

1) \$114,076 related to interdepartmental charges for HomeWise program support.

OSE requested back-up documentation from the Office of Housing (OH) on their cost-allocation methodology with us, and asked that they send back-up documentation to demonstrate how that methodology was applied to the funds in question. We have reviewed and approved the documentation of the labor expenses, and we certified that the funds were used for grant-eligible activities in a letter to our grantor, US DOE, in February 2015. We will maintain a file of the full documentation for the 10-year file retention period required by City and federal policy.

OSE also communicated to staff the importance of ensuring proper documentation and verification of all charges in contracts and interdepartmental agreements, including both labor and other direct expenses. The message included guidance that all labor and direct expenses must be substantially detailed and explained, with a clear linkage to work performed and/or accomplishments achieved. The message also directed staff to review invoices thoroughly to assure expenses and their relation to the project are clear, and include language about expectations for back-up documentation of expenses in the initial contract or agreement. OSE reminded staff to examine grants carefully for their payment verification requirements, as some differ from standard city requirements. This was communicated in a staff meeting, in a management meeting, and via email.

2) \$78,449 related to transferred payroll costs between Org X1107, Org X1108, and Org X1109.

These transactions relate to staff costs for two Temporary Employment Services (TES) positions that were paid for by multiple funding sources with different grant orgs within OSE. City payroll processes require TES employees to charge time to only one org. In this case, because of restrictions on the grant orgs (X1108 and X1109), OSE was required to charge the full employee's time to OSE's general fund (X1107), and then request reimbursement from the grant sources for allowable grant-related work hours.

OSE now requires that TES employees who cannot charge time directly to a grant on their timesheet, but who are conducting grant-eligible activities, to document their work according to the distribution of their salaries or wages through monthly Time and Effort logs that include a description of the activities conducted under the federal award, reflect actual activity of each employee, and account for the total activity for which an employee is compensated. This documentation is prepared monthly and signed by the employee and supervisor. OSE implemented this requirement in 2014 for all staff charging partial time to the EECBG grant (Org X1109) that had positions assigned to a different home Org (X1107).

3) \$13,097 for labor costs recorded before time was worked.

OSE had a procedure in place to review and control for appropriate expenditures, including:

- *OSE's Director and other management staff also have the ability to correct timesheets after the pay period to reflect actuals (if an employee left early, was sick, etc).*
- *Reimbursement from the grant was sought at least one month after payroll charges occur with adequate time for these corrections to be made.*

However, to correct this action, OSE improved the documentation of this procedure in the OSE employee handbook on October 2014. Additionally, we now send email reminders to employees at the end of every time period, reminding employees to submit their timesheet at the end of the pay period (end of day Tuesday), and reminding supervisors to approve timesheets the day after the pay period ends (Wednesday before noon). This is a step we put in place immediately upon learning of the auditor's finding in September 2014.

Audit Period: 2013	Report Ref. No.: 1012743	Finding Ref. No.: 4	CFDA Number(s): 97.067
Federal Program Name and Granting Agency: Homeland Security Grant Program, U.S. Department of Homeland Security		Pass-Through Agency Name: King County, Military Department, Port of Tacoma, Pierce County	
Finding Caption: The City did not comply with time and effort requirements for payroll costs charged to the Homeland Security Grant Program.			
Background: Audit report disclosed questioned costs of \$51,066 for salaries/wages and related benefits.			
Status of Corrective Action: (check one) <input checked="" type="checkbox"/> Fully Corrected <input type="checkbox"/> Partially Corrected <input type="checkbox"/> No Corrective Action Taken <input type="checkbox"/> Finding is considered no longer valid			
Corrective Action Taken: <i>In 2014, we transferred \$23,297.89 for salaries/benefits from UASI to the Port Security grant (MCOP). Also, after that time, Bill Wolak allocated his hours to other Homeland security grants (MCOP and SHSP), as well as his benefits.</i> <i>Now, Faye Landskov is the new staff in Grants and Contract unit which is advised to allocate her hours to the grants based on the hours that she spends and then her city paid benefits will be allocated to the other homeland security grants based on her salary/wage charges.</i>			

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

**City of Seattle
King County
January 1, 2014 through December 31, 2014**

Mayor and City Council
City of Seattle
Seattle, Washington

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

We have audited the compliance of the City of Seattle, King 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 its major federal programs for the year ended December 31, 2014. The City's major federal programs are identified in the accompanying Federal Summary.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City'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 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 City'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 City's compliance.

Opinion on Each Major Federal Program

In our opinion, the City 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 an instance of noncompliance with those requirements, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying Schedule of Federal Audit Findings and Questioned Costs as Finding 2014-001. Our opinion on each major federal program is not modified with respect to these matters.

Other Matters – Report Reissuance

This report, which replaces a previously issued report, has been reissued to remove a reference to other organizational units of the City as having received a separate audit of their federal awards.

City's Response to Findings

The City's response to the noncompliance findings identified in our audit is described in the accompanying Schedule of Federal Audit Findings and Questioned Costs. The City'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 City 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 City'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 City'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 over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified certain deficiencies in internal control over compliance, as described in the accompanying Schedule of Federal Audit Findings and Questioned Costs as Finding 2014-001 that we consider to be significant deficiencies.

City's Response to Findings

The City's response to the internal control over compliance findings identified in our audit is described in the accompanying Schedule of Federal Audit Findings and Questioned Costs. The City'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 cursive script that reads "Troy X. Kelley".

TROY KELLEY
STATE AUDITOR
OLYMPIA, WA

September 23, 2015

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

**City of Seattle
King 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 City of Seattle.

Finding ref number: 2014-001	Finding caption: City of Seattle’s Office of Housing did not have adequate internal controls to ensure compliance with federal requirements for its Homewise program.
Name, address, and telephone of auditee contact person: Steve Walker, Director, Office of Housing City of Seattle 700 Fifth Avenue, Suite 5700 Seattle, WA 98104 206-684-0338	
Corrective action the auditee plans to take in response to the finding: <i>The major sources of funding for the HomeWise program include Seattle City Light (SCL) and a variety of state and federal sources that flow through the Washington State Department of Commerce. In 2014, SCL represented approximately half of all HomeWise capital costs. Therefore, in 2014, the Office of Housing (OH) requested that SCL pay for half of HomeWise administrative costs. Unfortunately, SCL capped the administrative amount at less than their pro-rata share, which created this issue.</i> <i>However, it is important to recognize that SCL dollars directly result in the HomeWise program’s ability to generate additional units. SCL capital funds stretch state and federal dollars further. Often, the combination of SCL capital funds and other grant funds creates a large enough subsidy to incentivize multi-family property owners to participate. Because of this leverage, the Department of Commerce grants are reaching more units than they would otherwise.</i> <i>In response to the recommendation that the cost allocation be equitably divided, OH will do the following:</i> <i>d) OH will continue to request that SCL pays their pro-rata administrative share.</i> <i>e) OH will request unrestricted funds from the City Budget Office for the gap in the event</i>	

that SCL does not pay equitably. In the period of this audit, OH had a very small amount of City General Fund that was assigned for a specific purpose outside of the HomeWise program. And as of 2017, OH will not have any unrestricted funds. OH is fully funded by restricted sources that cannot be used for the HomeWise program.

- f) OH will seek to continue to discuss this issue with funders in order to reach an understanding of the definition of an equitable administrative share given the significant leverage they receive.*

In response to the recommendation that OH certifies payroll charges to the LIHEAP grant on a monthly basis instead of quarterly as is the current practice:

Making this change would actually make the distribution of administrative costs less equitable across grants. To illustrate this point, please consider the following scenario.

The HomeWise program used \$1.5 million of capital from Grant A in a given year. Most of this capital was expended in three large segments because it was used for large, multi-family projects. The total HomeWise capital budget in the same year was \$3.2 million, meaning that other grants paid the remaining \$1.7 million in capital. HomeWise administrative, non-capital expenses are a fixed amount of \$130,000 a month, for a total annual amount of \$1.56 million.

The most equitable way to assign administrative costs would be to apply the share on an annual basis. Grant A represents 47% of the capital in a given year, and therefore should cover 47% of the administrative costs that year, or \$731,250. Unfortunately, HomeWise cannot assign administrative expenses on an annual basis because grants in the program have a variety of closing dates that happen throughout the year. We would be unable to charge administrative expenses to a grant after its closing date.

If administrative expenses were assigned on a monthly basis, the distribution would look as follows, and the total amount of administrative expenses paid for that year by Grant A would be \$428,753, far below what it should be, given the amount of capital covered by Grant A:

<i>Month</i>	<i>Amount of Capital Paid for by Grant A</i>	<i>Amount of Capital Paid for by Other Grants</i>	<i>Percentage of Capital Represented by Grant A</i>	<i>Applying this Percentage, Amount of Labor Expenses Paid for By Grant A</i>
<i>January</i>	\$0	\$50,000	0%	\$0
<i>February</i>	\$0	\$100,000	0%	\$0
<i>March</i>	\$700,000	\$0	100%	\$130,000
<i>April</i>	\$0	\$570,000	0%	\$0
<i>May</i>	\$270,000	\$40,000	87%	\$113,226
<i>June</i>	\$10,000	\$320,000	3%	\$3,939
<i>July</i>	\$0	\$250,000	0%	\$0
<i>August</i>	\$0	\$190,000	0%	\$0
<i>September</i>	\$20,000	\$25,000	44%	\$57,778
<i>October</i>	\$500,000	\$25,000	95%	\$123,810
<i>November</i>	\$0	\$60,000	0%	\$0
<i>December</i>	\$0	\$70,000	0%	\$0

Total: \$428,753

Because capital expenditures are incurred in large amounts at isolated points of the year – rather than evenly distributed each month – the quarterly time horizon mitigates these spikes and allows for a more equitable distribution of administrative expenses. If administrative expenses were assigned on a quarterly basis, the distribution would look as follows, and the total amount of administrative expenses paid for that year by Grant A would be \$725,217, much closer to the accurate annualized amount:

<i>Quarter</i>	<i>Amount of Capital Paid for by Grant A</i>	<i>Amount of Capital Paid for by Other Grants</i>	<i>Percentage of Capital Represented by Grant A</i>	<i>Applying this Percentage, Amount of Labor Expenses Paid for By Grant A</i>
<i>1</i>	\$700,000	\$150,000	82%	\$321,176
<i>2</i>	\$280,000	\$930,000	23%	\$90,248
<i>3</i>	\$20,000	\$465,000	4%	\$16,082
<i>4</i>	\$500,000	\$155,000	76%	\$297,710

Total: \$725,217

Therefore, OH will continue to distribute administrative costs on a quarterly basis. Per the recommendation, OH will add the process of completing time and effort certifications on a quarterly basis.

Anticipated date to complete the corrective action: NA

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.

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