



**BUSINESS OF THE CITY COUNCIL
CITY OF MERCER ISLAND**

**AB 6469
May 21, 2024
Special Business**

AGENDA BILL INFORMATION

TITLE:	AB 6469: 2022 Financial, Accountability, and Federal Audit Exit Conference	<input checked="" type="checkbox"/> Discussion Only <input type="checkbox"/> Action Needed: <input type="checkbox"/> Motion <input type="checkbox"/> Ordinance <input type="checkbox"/> Resolution
RECOMMENDED ACTION:	Receive report. No action necessary.	

DEPARTMENT:	Finance
STAFF:	Matt Mornick, Finance Director LaJuan Tuttle, Deputy Finance Director
COUNCIL LIAISON:	n/a
EXHIBITS:	1. 2022 Audit Engagement Letter 2. 2022 Audit Exit Conference Report
CITY COUNCIL PRIORITY:	n/a

AMOUNT OF EXPENDITURE	\$ n/a
AMOUNT BUDGETED	\$ n/a
APPROPRIATION REQUIRED	\$ n/a

EXECUTIVE SUMMARY

Representatives of the Washington State Auditor’s Office (SAO) will lead an Exit Conference to report on the results of the Financial and Accountability Audits for the fiscal year ending December 31, 2022 (see Exhibit 1).

- The purpose of the Exit Conference is for the audit team to report audit results to management prior to publication of the audited financial statements (see Exhibit 2).
- After the Exit Conference, the SAO will publish the audit reports, audited financial statements, notes to the financial statement, and required supplementary information on the SAO website.

BACKGROUND

The City of Mercer Island is audited on an annual basis. The SAO regularly performs two types of audits each year: a Financial Audit and an Accountability Audit, resulting in an audit report for both types. Additional information regarding the scope and limitations of each audit type can be found in the audit representation letter included as Exhibit 1.

A financial audit provides an independent opinion on a local government’s financial statements and the results of its operations and cash flows. In other words, a financial audit determines whether the financial statements present a reliable, accurate picture of a government’s finances.

An accountability audit evaluates whether a local government has adhered to applicable state laws, regulations, and its own policies and procedures. Auditors review records to ensure public funds are accounted for and controls are in place to protect public resources from misappropriation and misuse.

A federal attestation examination is a review of compliance over federal funding programs. Federal guidelines require a Federal Single Audit when expenditures for federal programs exceed \$750,000 in a fiscal year. New with American Rescue Plan Act (ARPA) of 2021/ Coronavirus State and Local Fiscal Recovery Funds (CSLFRF) program dollars is the option for an Alternative Compliance Engagement if the recipient was both a non-entitlement unit of local government (less than 50,000 residents) and only exceeded the \$750K threshold because of ARPA/CSLFRF dollars. The City qualified for the alternative engagement for 2022 federal expenditures, which allowed for a more streamlined and cost-effective federal program audit.

ISSUE/DISCUSSION

The financial audit report identifies a material weakness (finding) relating to the recognition of revenues received in advance from the CSLFRF, which is a program funded through ARPA. The audit report further clarifies that financial reporting under Generally Accepted Accounting Principles (GAAP) requires revenue recognition for grants received in advance to be limited to eligible expenditures incurred. Stated more clearly, earned revenue cannot exceed eligible expenditures in the reporting period.

The reported finding does not represent any misuse of public funds. Rather, it represents a classification error involving how the federal funds received were reported on the audited financial statements.

Absent specific direction from the SAO, staff elected to recognize earned revenue as ARPA funds were committed for eligible uses by the City Council. The decision to recognize earned revenue as ARPA funds were committed was discussed in length with the SAO audit team during the 2021 annual financial audit. The audit team gave no indication the City's revenue recognition determination was non-compliant with GAAP. Given fiscal year 2021 audit results, the City used the same revenue recognition criteria in the 2022 annual financial statements.

Staff acknowledges that the City's interpretation of the revenue recognition criteria for ARPA funds was inconsistent with that of the SAO. However, the City believes adequate controls and procedures are in place and disagrees with the assessment of a material weakness in internal controls. Once advised of the appropriate revenue recognition criteria for ARPA funds, the City corrected amounts reported in earned and unearned revenue classifications in the 2022 financial statements.

RECOMMENDED ACTION

Receive and review the 2022 Audit Exit Conference report from the Washington State Auditor's Office.