

November 19, 2020

Management of the Association of Bay Area Governments
C/o Brian Mayhew, Chief Financial Officer
Association of Bay Area Governments
375 Beale Street
San Francisco, California 94105

Management of the Association of Bay Area Governments,

In planning and performing our audit of the financial statements of the business-type activities, the major fund, and the aggregate remaining fund information of the Association of Bay Area Governments ("ABAG") as of and for the year ended June 30, 2020, in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, we considered ABAG's internal control over financial reporting ("internal control") 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 ABAG's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of ABAG's internal control. Matters communicated in this letter are classified as follows.

- Deficiency – A control deficiency 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.
- Significant deficiency – A deficiency, or 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.
- Material weakness – 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.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control 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. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above. However, we identified a certain deficiency in internal control that we are required to or wish to communicate to you.

This communication is intended solely for the information and use of the members of the Executive Board of ABAG, management, and others within the organization, and governmental granting agencies and is not intended to be and should not be used by anyone other than these specified parties.

The purpose of this letter is solely 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 effectiveness of ABAG's internal control over financial reporting or on compliance. This letter is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the ABAG's internal control over financial reporting and compliance. Accordingly, this letter is not suitable for any other purpose.

ABAG's written response to the deficiencies identified in our audit was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Crowe LLP

San Francisco, California
November 19, 2020

Cc: Therese McMillan, Executive Director

Accounting for Grants with Eligible Cost Requirements

Classification:

Deficiency

Applicable Entities:

ABAG

Observation:

The California Department of Housing and Community Development (HCD) administers the Regional Early Action Planning Grant Program (REAP) and awarded state grant funding to ABAG for purposes of enabling jurisdictions to meet the regional housing needs assessment. The grant agreement notes that only approved and eligible costs incurred for work after October 1, 2019 completed during the grant term will be reimbursable.

Generally accepted accounting principles (GAAP) requires that for expenditure-driven grant programs, until the recipient has met the provider's requirements by incurring eligible costs in accordance with the provider's program, no asset (receivable) should be recorded by the recipient. During our audit, we noted that management had recorded a receivable in the amount \$5.89 million and a corresponding unearned revenue. As no related eligible costs were incurred as of fiscal year end, an asset should not have been recorded.

We proposed and management subsequently recorded an adjustment to remove the \$5.89 million receivable and corresponding unearned revenue.

Impact:

As management viewed the REAP award as a government-mandated program, they did not initially view the grant award as contingent upon incurring eligible costs to recognize a receivable from the State. As a result, management inadvertently recorded an asset in advance of incurring eligible costs that was not in accordance with GAAP. It should be noted that the error had no impact on overall net position as the asset recorded was entirely offset by unearned revenue (liability).

Recommendation:

We recommend that management strengthen their process to review all grant terms and conditions to identify requirements on allowable costs and activities of the grant and conditions for reimbursement. When such stipulations exist, receivables and related revenues are recorded only when management has incurred allowable costs under the grant.

Management Response:

The management of the Association of Bay Area Governments (ABAG) concurs with the finding and recommendation. Management reversed the entries and initiated a new process for recognition of grant reimbursements that cross fiscal years.