

Independent Audit Oversight

AB 229

Assembly Member Ricardo Lara (D-Southgate)

Under current law, the State Controller generally has authority to audit local agencies over their handling of state or federal funds. Audits of how local agencies spend local funds are included within annual reports issued by independent auditors that are selected by the agency and can be contracted with for an unlimited amount of time. The audits prepared by independent auditors only are submitted to the Controller for review if the local agency spends more than \$500,000 a year in federal funds. While all counties and most cities are required by current law to submit audits for review, some cities and many special districts are not.

The Controller can initiate a quality control review of the work papers of an independent auditor when there is suspicion that the work performed by the independent auditor is inadequate, such as in the County of Modoc and the City of Bell. However, that only applies to audits sent to the Controller.

The Controller has the authority to develop and issue audit guidelines for use by independent auditors of special districts, but does not have such authority for independent audits of cities and counties.

This bill would:

Require that financial, state compliance and single audits of all local governments, including special districts, be submitted to the Controller's Office for review to ensure compliance with the audit guide.

Findings in the financial, state compliance and single audits would be distributed to the state agency charged with oversight of state and federal pass through programs. In addition, the results of SCO's oversight activity, including the results of quality control work paper reviews will be included in an annual report to the legislature.

Authorize the Controller's Office to perform quality control reviews of the independent auditor's local government audit working papers.

Audits will be selected for a review based on a variety of criteria to ensure that this effort is focused on the highest potential problems and the greatest coverage. Criteria under consideration include: 1) disciplinary actions by the State Board of Accountancy; 2) financial reports that are rejected as incomplete or unacceptable by the Controller after a desk review; 3) whether the same firm consistently reports no adverse findings in the report; 4) the number of local government clients the independent auditor has; 5) the firm's experience in performing local government audits; 6) the complexity of state and federal programs administered by the local government; 7) requests or leads about wrongdoing from other sources, such as citizen

groups or the media; and, 8) the extent of actions the local government can take without state approvals, such as charter cities, which do not have to comply with certain state laws, such as compensation caps for officials and employees.

Specify the process the Controller's Office must take to develop and issue audit guidelines for independent audits of cities and counties.

The audit guidelines will promote accountability and transparency and will be developed in consultation with audit firms and representatives from the cities and counties. This process will be modeled after the one used by the Controller's Office to develop audit guidelines for local education agencies.

Require the Controller's Office to prepare and publish a list of independent auditors that are acceptable for local government audits, and prepare a report of findings to be distributed to the Legislature, including the results of quality control work paper reviews that were performed.

Specifically, the Controller's Office will publish a list of approved independent audit firms that cities, counties, and special districts may select to perform their audits.

Require that local governments include in their contracts with independent auditors a provision that allows the Controller's Office to access work papers.

This will ensure easy access to these materials during a quality control review. The quality control review of the annual audits of Bell performed by its independent auditor found that the firm had failed to follow or fully comply with many fieldwork audit standard, federal compliance audit requirements and state redevelopment compliance audit requirements. Had they done so, some, if not all, of the problems the Controller's auditors found in Bell could have been identified earlier.

Prohibit a local government from using the same independent auditor/audit firm for more than five continuous years, unless approved by the Controller's Office for exceptions.

This limit is contained in audit procurement guidelines developed by the Government Finance Officers Association to promote auditor independence.