

City Audits - The Benefits and the Barriers Establishing Independent Audit Committees and Supporting Independent Performance Auditors

**2005 Financial Management Seminar
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Why establish an Audit Committee?

- To improve oversight over the city's financial and budgetary controls
- To demonstrate leadership in ethics and accountability
- To learn more about how your city is managed

Who is in favor of establishment of strong, independent audit committees?

- Treadway Commission report of 1987 (primarily publicly traded companies)
- Securities and Exchange Commission (companies)
- Government Finance Officers Association (1997) (update: 2006 see attached)
- Sarbanes-Oxley Act of 2002
- AICPA standards and Generally Accepted Government Accounting Standards (GAGAS)

What are the barriers to establishing independent audit committees and independent performance audit functions?

- Group discussion about barriers and strategies to follow presentation

Oversight responsibilities of an audit committee:

A If charged with oversight of the commercial firm providing the annual financial statement audit:

- Selecting the audit firm
- Open communication between the Committee, financial and program management, and the auditors
- Quality and timely financial and compliance reporting
- The annual audit process, including response to management letter concerns
- Examining, supporting, and reporting to the Council regarding:
Internal accounting controls to safeguard assets, ensure compliance and avoid fraud; budgetary and financial matters

B If charged with oversight and support of an independent performance audit function:

- If the City Auditor reports to Council, the audit committee also has responsibilities for the staffing and oversight of the independent performance audit function:
- Recommending or selecting the chief audit executive (City Auditor)
- Recommending salary and budget for staff auditors
- Advice on selection of audits for annual audit plan
- Performance evaluation of City Auditor

Composition and skills of public sector audit committees:

- Five to seven members are recommended
- Ideally, they should be independent of city management (in strong mayor cities, mayor is management; council is governing body/legislative body)

Structure of the audit committee:

Structure of the audit committee should be formally established by charter or legislation. A mix of audit committee structures is often seen; three common structures include:

- The legislative body
- A committee of the legislative body, often the finance or budget committee
- An audit committee including non-legislative members;
 - A citizen-based committee appointed by the legislative body, whose members collectively possess knowledge of government accounting, auditing, and financial reporting practices (generally indicated by professional certifications, such as Certified Public Accountant, Certified Internal Auditor, or Certified Management Accountant) and knowledge of management and business practices. This committee may also include some legislative members, but no executive branch members. – this is the most independent form of an audit committee

- A mix of government and citizen representatives – a representative from the executive branch (e.g., the mayor/city manager or his/her representative); a representative from the legislative body (e.g, the president/chair of the city council or his/her representative); and citizens (often at least three so they hold the majority vote, or executive branch members may be non-voting members)
- An organization-based committee that only includes representatives from the city, usually the mayor/city manager or his/her representative, a representative from the legislative body, and select department heads – this is the least independent form of an audit committee because it includes members who are subject to audit
- If the jurisdiction has an independent audit function on staff, some practitioners advise that the staff chief audit executive attend all audit committee meetings and, in many cases, staff the audit committee.

With thanks to those firms who provided the following reports, which were used in compiling this summary information and may be provided to attendees:

Audit Committee Guide for Public Sector Entities, State and Local Governments and Nonprofit Organizations – McGladrey & Pullen, LLP, Certified Public Accountants

Public Sector Audit Committees Resource Guide – Deloitte & Touche, LLP

Corporate Governance: The Increased Role of the Audit Committee – RBG Public Sector Services Group

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