



Local Agency Formation Commission of Napa County
Subdivision of the State of California

1030 Seminary Street, Suite B
Napa, California 94559
Telephone: (707) 259-8645
Facsimile: (707) 251-1053
www.napa.lafco.ca.gov

We Manage Local Government Boundaries, Evaluate Municipal Services, and Protect Agriculture

August 5, 2013

Agenda Item No. 5b (Consent/Action)

July 29, 2013

TO: Local Agency Formation Commission

FROM: Keene Simonds, Executive Officer

SUBJECT: Authorization to Approve Audit Expenditure

The Commission will consider authorizing the Executive Officer to approve an expenditure in the amount of \$4,725 to Gallina LLP to prepare an independent audit of the agency's financial statements for 2012-2013.

Local Agency Formation Commissions (LAFCOs) are authorized under California Government Code Section 56380 to enter into agreements or contracts with public and private parties for services necessary to fulfill its regulatory and planning responsibilities.

A. Background

It is the practice of LAFCO of Napa County ("Commission") to authorize the Chair to enter into an agreement with a public accounting firm to conduct an independent audit of the agency's financial statements for the prior fiscal year. The purpose of the audit is for a third-party to assess the reliability of the Commission's financial statements by reviewing records and testing transactions to determine their compliance with generally accepted governmental accounting standards. The audit also provides an opportunity for the third-party to identify reporting omissions and to make suggestions for improvements.

B. Discussion

The Commission has received an engagement letter from Gallina, LLP to prepare an independent audit concerning the agency's financial statements for the 2012-2013 fiscal year. Gallina is headquartered in Sacramento, California and is entering the third year of a three-year contract to provide auditing services for the County of Napa. Gallina's proposed cost to prepare the audit for the Commission is \$4,725. This amount equals Gallina's charge to the Commission for preparing an audit for the 2011-2012 fiscal year.

An expanded overview on the County's competitive procurement process for outside auditing services is attached.

Joan Bennett, Commissioner
Councilmember, City of American Canyon

Gregory Pitts, Commissioner
Councilmember, City of St. Helena

Juliana Inman, Alternate Commissioner
Councilmember, City of Napa

Brad Wagenknecht, Chair
County of Napa Supervisor, 1st District

Bill Dodd, Commissioner
County of Napa Supervisor, 4th District

Mark Luce, Alternate Commissioner
County of Napa Supervisor, 2nd District

Brian J. Kelly, Vice Chair
Representative of the General Public

Gregory Rodeno, Alternate Commissioner
Representative of the General Public

Keene Simonds
Executive Officer

C. Analysis

It is generally accepted governmental agencies should prepare annual audits to enhance transparency in the management of public funds. Additionally, as mentioned, the Commission relies on the annual audit process as a performance measure for staff as well as to identify opportunities to improve accounting practices. Accordingly, *while not a requirement*, it is appropriate for the Commission to enter into an agreement with Gallina based on its contractual relationship with the County to prepare an audit on the agency's financial statements for the 2012-2013 fiscal year (emphasis added). Entering the proposed agreement with Gallina requires Commission authorization given the quoted cost – \$4,725 – exceeds the Executive Officer's spending authority under agency policy.¹

D. Recommendation

It is recommended the Commission authorize the Executive Officer to approve an expenditure in the amount of \$4,725 for Gallina to prepare an independent audit for the 2012-2013 fiscal year.

E. Alternatives for Action

The following three alternatives are available to the Commission:

Alternative Action One (Recommended):

Authorize the Executive Officer to approve an expenditure in the amount of \$4,725 for Gallina to prepare an independent audit for the 2012-2013 fiscal year.

Alternative Action Two:

Continue consideration of the item to another meeting while providing appropriate direction to staff with respect to any additional information requests.

Alternative Action Three:

Take no action.

F. Procedures for Consideration

This item has been agendaized as part of the consent calendar. Accordingly, a successful motion to approve the consent calendar will include taking affirmative action on the staff recommendation unless otherwise specified by the Commission.

Respectfully submitted,

Keene Simonds
Executive Officer

Attachments:

- 1) Engagement Letter from Gallina LLP
- 2) Summary of County's Process to Select Audit Firm

¹ Commission policy prohibits the Executive Officer from approving any single or cumulative expense in excess of \$3,000.



June 14, 2013

Ms. Tracy Schulze
Auditor-Controller
County of Napa
1195 Third Street, Room B-10
Napa, CA 94559-3097

Dear Tracy:

We are pleased to confirm our understanding of the services we are to provide County of Napa for the year ending June 30, 2013. We will audit the financial statements of the governmental activities, the business type activities, each major fund, and the aggregate remaining fund information, including the related notes to the financial statements, which collectively comprise the basic financial statements, of the County of Napa as of and for the year ended June 30, 2013. Accounting standards generally accepted in the United States of America provide for certain required supplementary information (RSI), such as management's discussion and analysis (MD&A), to supplement the County of Napa's basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. As part of our engagement, we will apply certain limited procedures to the County of Napa's RSI in accordance with auditing standards generally accepted in the United States of America. These limited procedures will consist of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We will not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance. The following RSI is required by generally accepted accounting principles and will be subjected to certain limited procedures, but will not be audited:

1. Management's discussion and analysis
2. Budgetary comparison schedules
3. Schedule of funding progress

We have also been engaged to report on supplementary information other than RSI that accompanies the County of Napa's financial statements. We will subject the following supplementary information to the auditing procedures applied in our audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America and will provide an opinion on it in relation to the financial statements as a whole.

1. Schedule of expenditures of federal awards
2. Combining and individual fund statements

The following other information accompanying the financial statements will not be subjected to the auditing procedures applied in our audit of the financial statements, and our auditor's report will not provide an opinion or any assurance on that other information.

1. Introductory section
2. Statistical section

Audit Objectives

The objective of our audit is the expression of opinions as to whether your basic financial statements are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles and to report on the fairness of the supplementary information referred to in the second paragraph when considered in relation to the financial statements as a whole. The objective also includes reporting on –

- Internal control related to the financial statements and compliance with the provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the financial statements in accordance with *Government Auditing Standards*.
- Internal control related to major programs and an opinion (or disclaimer of opinion) on compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a direct and material effect on each major program in accordance with the Single Audit Act Amendments of 1996 and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

The reports on internal control and compliance will each include a paragraph that states that the purpose of the report is solely to describe (1) the scope of testing of internal control over financial reporting and compliance and the result of that testing and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance, (2) the scope of testing internal control over compliance for major programs and major program compliance and the result of that testing and to provide an opinion on compliance but not to provide an opinion on the effectiveness of internal control over compliance, and (3) that the report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering internal control over financial reporting and compliance and OMB Circular A-133 in considering internal control over compliance and major program compliance. The paragraph will also state that the report is not suitable for any other purpose.

Our audit will be conducted in accordance with auditing standards generally accepted in the United States of America; the standards for financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; the Single Audit Act Amendments of 1996; and the provisions of OMB Circular A-133, and will include tests of accounting records, a determination of major program(s) in accordance with OMB Circular A-133, and other procedures we consider necessary to enable us to express such opinions and to

render the required reports. We cannot provide assurance that unmodified opinions will be expressed. Circumstances may arise in which it is necessary for us to modify our opinions or add emphasis-of-matter or other-matter paragraphs. If our opinions on the financial statements or the Single Audit compliance opinions are other than unmodified, we will discuss the reasons with you in advance. If, for any reason, we are unable to complete the audit or are unable to form or have not formed opinions, we may decline to express opinions or to issue a report as a result of this engagement.

Management Responsibilities

Management is responsible for the basic financial statements, schedule of expenditures of federal awards, and all accompanying information as well as all representations contained therein. Management is also responsible for identifying government award programs and understanding and complying with the compliance requirements, and for preparation of the schedule of expenditures of federal awards in accordance with the requirements of OMB Circular A-133.

Management is responsible for establishing and maintaining effective internal controls, including internal controls over compliance, and for evaluating and monitoring ongoing activities, to help ensure that appropriate goals and objectives are met and that there is reasonable assurance that government programs are administered in compliance with compliance requirements. You are also responsible for the selection and application of accounting principles; for the fair presentation in the financial statements of the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the County of Napa and the respective changes in financial position and, where applicable, cash flows in conformity with U.S. generally accepted accounting principles; and for compliance with applicable laws and regulations and the provisions of contracts and grant agreements.

Management is also responsible for making all financial records and related information available to us and for ensuring that management is reliable and financial information is reliable and properly recorded. You are also responsible for providing us with (1) access to all information of which you are aware that is relevant to the preparation and fair presentation of the financial statements, (2) additional information that we may request for the purpose of the audit, and (3) unrestricted access to persons within the government from whom we determine it necessary to obtain audit evidence.

Your responsibilities also include identifying significant vendor relationships in which the vendor has responsibility for program compliance and for the accuracy and completeness of that information. Your responsibilities include adjusting the financial statements to correct material misstatements and confirming to us in the written representation letter that the effects of any uncorrected misstatements aggregated by us during the current engagement and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

You are responsible for the design and implementation of programs and controls to prevent and detect fraud, and for informing us about all known or suspected fraud or illegal acts affecting the

government involving (1) management, (2) employees who have significant roles in internal control, and (3) others where the fraud could have a material effect on the financial statements. Your responsibilities include informing us of your knowledge of any allegations of fraud or suspected fraud affecting the government received in communications from employees, former employees, grantors, regulations, or others. In addition, you are responsible for identifying and ensuring that the entity complies with applicable laws, regulations, contracts, agreements, and grants. Additionally, as required by OMB Circular A-133, it is management's responsibility to follow up and take corrective action on reported audit findings and to prepare a summary schedule of prior audit findings and a corrective action plan.

You are responsible for preparation of the schedule of expenditures of federal awards in conformity with OMB Circular A-133. You agree to include our report on the schedule of expenditures of federal awards in any document that contains and indicates that we have reported on the schedule of expenditures of federal awards. You also agree to include the audited financial statements with any presentation of the schedule of expenditures of federal awards that includes our report thereon or make the audited financial statements readily available to intended users of the schedule of expenditures of federal awards no later than the date the schedule of expenditures of federal awards is issued with our report thereon. Your responsibilities include acknowledging to us in the written representation letter that (1) you are responsible for presentation of the schedule of expenditures of federal awards in accordance with OMB Circular A-133; (2) that you believe the schedule of expenditures of federal awards, including its form and content, is fairly presented in accordance with OMB Circular A-133; (3) that the methods of measurement or presentation have not changed from those used in the prior period (or, if they have changed, the reasons for such changes); and (4) you have disclosed to us any significant assumptions or interpretations underlying the measurement or presentation of the schedule of expenditures of federal awards.

You are also responsible for the preparation of the other supplementary information, which we have been engaged to report on, in conformity with U.S. generally accepted accounting principles. You agree to include our report on the supplementary information in any document that contains and indicates that we have reported on the supplementary information. You also agree to include the audited financial statements with any presentation of the supplementary information that includes our report thereon or make the audited financial statements readily available to users of the supplementary information no later than the date the supplementary information is issued with our report thereon. Your responsibilities include acknowledging to us in the written representation letter that (1) you are responsible for presentation of the supplementary information in accordance with GAAP; (2) that you believe the supplementary information, including its form and content, is fairly presented in accordance with GAAP; (3) that the methods of measurement or presentation have not changed from those used in the prior period (or, if they have changed, the reasons for such changes); and (4) you have disclosed to us any significant assumptions or interpretations underlying the measurement or presentation of the supplementary information.

Management is responsible for establishing and maintaining a process for tracking the status of audit findings and recommendations. Management is also responsible for identifying for us previous financial audits, attestation engagements, performance audits, or other studies related to

the objectives discussed in the Audit Objectives section of this letter. This responsibility includes relaying to us corrective actions taken to address significant findings and recommendations resulting from those audits, attestation engagements, performance audits, or studies. You are also responsible for providing management's views on our current findings, conclusions, and recommendations, as well as your planned corrective actions, for the report, and for the timing and format for providing that information.

Audit Procedures – General

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We will plan and perform the audit to obtain reasonable rather than absolute assurance about whether the financial statements are free of material misstatement, whether from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the entity or to acts by management or employees acting on behalf of the entity. Because the determination of abuse is subjective, *Government Auditing Standards* do not expect auditors to provide reasonable assurance of detecting abuse.

Because of the inherent limitations of an audit, combined with the inherent limitations of internal control, and because we will not perform a detailed examination of all transactions, there is a risk that material misstatements or noncompliance may exist and not be detected by us, even though the audit is properly planned and performed in accordance with U.S. generally accepted auditing standards and *Government Auditing Standards*. In addition, an audit is not designed to detect immaterial misstatements or violations of laws or governmental regulations that do not have a direct and material effect on the financial statements or major programs. However, we will inform the appropriate level of management of any material errors or any fraudulent financial reporting or misappropriation of assets that come to our attention. We will also inform the appropriate level of management of any violations of laws or governmental regulations that come to our attention, unless clearly inconsequential, and of any material abuse that comes to our attention. We will include such matters in the reports required for a Single Audit. Our responsibility as auditors is limited to the period covered by our audit and does not extend to any later periods for which we are not engaged as auditors.

Our procedures will include tests of documentary evidence supporting the transactions recorded in the accounts, and may include tests of the physical existence of inventories, and direct confirmation of receivables and certain other assets and liabilities by correspondence with selected individuals, funding sources, creditors, and financial institutions. We will request written representations from your attorneys as part of the engagement, and they may bill you for responding to this inquiry. At the conclusion of our audit, we will require certain written representations from you about the financial statements and related matters.

Audit Procedures – Internal Controls

Our audit will include obtaining an understanding of the entity and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Tests of controls may be performed to test the effectiveness of certain controls that we consider relevant to preventing and detecting errors and fraud that are material to the financial statements and to preventing and detecting misstatements resulting from illegal acts and other noncompliance matters that have a direct and material effect on the financial statements. Our tests, if performed, will be less in scope than would be necessary to render an opinion on internal control and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to *Government Auditing Standards*.

As required by OMB Circular A-133, we will perform tests of controls over compliance to evaluate the effectiveness of the design or operation of controls that we consider relevant to preventing or detecting material noncompliance with compliance requirements applicable to each major federal award program. However, our tests will be less in scope than would be necessary to render an opinion on those controls and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to OMB Circular A-133.

An audit is not designed to provide assurance on internal control or to identify significant deficiencies or material weaknesses. However, during the audit, we will communicate to management and those charged with governance internal control related matters that are required to be communicated under AICPA professional standards, *Government Auditing Standards*, and OMB Circular A-133.

Audit Procedures – Compliance

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we will perform tests of the County of Napa's compliance with provisions of applicable laws, regulations, contracts, and agreements, including grant agreements. However, the objective of those procedures will not be to provide an opinion on overall compliance and we will not express such an opinion in our report on compliance issued pursuant to *Government Auditing Standards*.

OMB Circular A-133 requires that we also plan and perform the audit to obtain reasonable assurance about whether the auditee has complied with applicable laws and regulations and the provisions of contracts and grant agreements applicable to major programs. Our procedures will consist of tests of transactions and other applicable procedures described in the *OMB Circular A-133 Compliance Supplement* for the types of compliance requirements that could have a direct and material effect on each of the County of Napa's major programs. The purpose of these procedures will be to express an opinion on the County of Napa's compliance with requirements applicable to each of its major programs in our report on compliance issued pursuant to OMB Circular A-133.

Engagement Administration, Fees, and Other

We may from time to time, and depending on the circumstances, use third-party service providers in serving your account. We may share confidential information about you with these service providers, but remain committed to maintaining the confidentiality and security of your information. Accordingly, we maintain internal policies, procedures, and safeguards to protect the confidentiality of your personal information. In addition, we will secure confidentiality agreements with all service providers to maintain the confidentiality of your information and we will take reasonable precautions to determine that they have appropriate procedures in place to prevent the unauthorized release of your confidential information to others. In the event that we are unable to secure an appropriate confidentiality agreement, you will be asked to provide your consent prior to the sharing of your confidential information with the third-party service provider. Furthermore, we will remain responsible for the work provided by any such third-party service providers.

We understand that your employees will prepare all cash, accounts receivable, or other confirmations we request and will locate any documents selected by us for testing.

The County of Napa is responsible for providing us with information to determine major federal award programs at least four weeks prior to field work. Sometimes a major program that should have been audited was not because this information was not provided timely as requested or the information provided was not accurate. If for some reason this should occur, GALLINA LLP and the County of Napa will mutually revise the fee to include the additional time and costs needed to audit the missed program.

At the conclusion of the engagement, we will complete the appropriate sections of the Data Collection Form that summarizes our audit findings. It is management's responsibility to submit the reporting package (including financial statements, schedule of expenditures of federal awards, summary schedule of prior audit findings, auditors' reports, and corrective action plan) along with the Data Collection Form to the federal audit clearinghouse. We will coordinate with you the electronic submission and certification. If applicable, we will provide copies of our report for you to include with the reporting package you will submit to pass-through entities. The Data Collection Form and the reporting package must be submitted within the earlier of 30 days after receipt of the auditors' reports or nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audits.

At the conclusion of the engagement, we will provide bound copies, unbound copies and electronic copies in portable document format (PDF) of all reports in the quantities you have designated. However, management is responsible for distribution of the reports and the financial statements. Unless restricted by law or regulation, or containing privileged and confidential information, copies of our reports are to be made available for public inspection.

The audit documentation for this engagement is the property of GALLINA LLP and constitutes confidential information. However, pursuant to authority given by law or regulation, we may be requested to make certain audit documentation available to the State Controller's Office or its designee, a federal agency providing direct or indirect funding, or the U.S. Government

Accountability Office for purposes of a quality review of the audit, to resolve audit findings, or to carry out oversight responsibilities. We will notify you of any such request. If requested, access to such audit documentation will be provided under the supervision of GALLINA LLP personnel. Furthermore, upon request, we may provide copies of selected audit documentation to the aforementioned parties. These parties may intend, or decide, to distribute the copies or information contained therein to others, including other governmental agencies.

The audit documentation for this engagement will be retained for a minimum of seven years after the report release date or for any additional period requested by the State Controller’s Office. If we are aware that a federal awarding agency, pass-through entity, or auditee is contesting an audit finding, we will contact the party(ies) contesting the audit finding for guidance prior to destroying the audit documentation.

The parties agree that any controversy or claim arising out of or relating to the services provided pursuant to this engagement letter agreement shall be determined by arbitration in accordance with the applicable Arbitration Rules for Professional Accounting and Related Services Disputes of the American Arbitration Association; and judgment on the award rendered by the arbitrator(s) may be rendered in any court of competent jurisdiction.

We expect to begin our interim field on August 26, 2013, and to perform year-end field work during the week of October 28, 2013, with the delivery of the reports by December 31, 2013. In order for us to provide you with timely services, it is incumbent upon your accounting staff to have the items listed on the client participation schedule ready for us by the due date indicated on the schedule. If the items are not provided on time, we cannot guarantee an on-time delivery of the reports.

Elba Zuniga is the engagement partner and is responsible for supervising the engagement and signing the reports or authorizing another individual to sign them. Our fee for these services will be as follows:

<i>Task</i>	<i>Cost</i>
Audit of financial statements (CAFR) and schedule of federal award expenditures and major program testing in accordance with Single Audit Act	\$67,250
Appropriations Limit Calculation	-0-
Treasury Oversight Committee compliance review	3,150
Napa TDA Funds	2,100
Napa-Vallejo Waste Management Authority	9,975
Upper Valley Waste Management Authority	3,350
First 5 Napa County	10,250
Napa County Flood Protection and Water Conservation District (including Single Audit)	17,325
Napa County Flood Protection and Watershed Improvement Authority	8,925
Local Agency Formation Commission of Napa County	4,725
In-Home Supportive Services Public Authority	5,250
Napa County Regional Park and Open Space District	5,250
Napa County Housing Authority	10,600
Total	\$148,150

Our invoices for these fees will be rendered each month as work progresses and are payable on presentation. The above fee is based on anticipated cooperation from your personnel and the assumption that unexpected circumstances will not be encountered during the audit. If significant additional time is necessary, we will discuss it with you and arrive at a new fee estimate before we incur the additional costs.

The County of Napa is responsible for providing us with information to prepare addendum letters in response to formal requests from Federal or State agencies to update information in the Single Audit report. If we are asked to prepare an addendum letter, GALLINA LLP and the County of Napa will mutually agree on the fee to include the additional time and costs needed to prepare the addendum letter.

Government Auditing Standards require that we provide you with a copy of our most recent external peer review report and any letter of comment, and any subsequent peer review reports and letters of comment received during the period of the contract. Our 2012 peer review accompanies this letter.

We appreciate the opportunity to be of service to the County of Napa and believe this letter accurately summarizes the significant terms of our engagement. If you have any questions, please let us know. If you agree with the terms of our engagement as described in this letter, please sign the enclosed copy and return it to us.

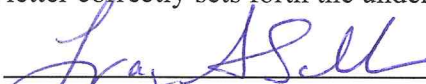
Very truly yours,
GALLINA LLP



M. Elba Zúñiga, CPA
Partner

RESPONSE:

This letter correctly sets forth the understanding of the County of Napa.

By: 

Title: Auditor - Controller

Date: 6/14/13



HANSEN, BARNETT & MAXWELL, P.C.
Certified Public Accountants

SYSTEM REVIEW REPORT

November 29, 2012

To the Partners
Gallina LLP
and the peer review committee of the California Society of CPAs

We have reviewed the system of quality control for the accounting and auditing practice of Gallina LLP (the firm) in effect for the year ended May 31, 2012. Our review was conducted in accordance with the Standards for Performing and Reporting on Peer Reviews established by the Peer Review Board of the American Institute of Certified Public Accountants. As a part of our peer review, we considered reviews by regulatory entities, if applicable, in determining the nature and extent of our procedures. The firm is responsible for designing a system of quality control and complying with it to provide the firm reasonable assurance of performing and reporting in conformity with professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance therewith based on our review. The nature, objectives, scope, limitation of and the procedures performed in a System Review are described in the standards at www.aicpa.org/prsummary.

As required by the standards, engagements selected for review included engagements performed under the *Government Auditing Standards* and audits of employee benefit plans.

In our opinion, the system of quality control for the accounting and auditing practice of Gallina LLP in effect for the year ended May 31, 2012, has been suitably designed and complied with to provide the firm with reasonable assurance of performing and reporting in conformity with applicable professional standards in all material respects. Firms can receive a rating of *pass*, *pass with deficiency(ies)* or *fail*. Gallina LLP has received a peer review rating of *pass*.



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Accounting Oversight Board

5 Trad Center, Suite 750, Salt Lake City, Utah 84180-1128
TEL 801-532-2200 FAX 801-532-7944 www.nbmcps.com

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Auditor-Controller

1195 Third Street · Room B10
Napa, CA 94559
www.countyofnapa.org

Main: (707) 253-4551
Fax: (707) 226-9065

Tracy A. Schulze
Auditor-Controller

MEMO

TO: Board of Supervisors
Nancy Watt, CEO
Minh Tran, County Counsel
Helene Franchi, CEO Principal Analyst

FROM: Tracy Schulze, Auditor-Controller

DATE: January 22, 2013

RE: RFP for Independent Auditor

This memo is in response to Supervisor Dodd's request to ensure that the Board is fulfilling its obligation to the public, regarding due diligence in selecting the County's independent audit firm. The concern results from the fact that Gallina, LLP (Gallina) has been the County's audit firm for several years and there are opinions that indicate it is prudent to rotate audit firms every 3-5 years.

For background information, on April 19th, 2011 I provided an update to the Board on the Request for Proposal (RFP) for Independent Auditors. I have attached the agenda item for the contract awarded on June 7, 2011. For this RFP, I spent several days compiling best practice language and structure, organized an audit committee, created a well-structured, specific grading process, and even spoke to the Grand Jury on several occasions requesting their participation on the audit committee. I worked with the CEO's office and County Counsel's office to ensure that Napa County was producing a comprehensive request.

As stated in the June 7th agenda item, the RFP was mailed to 33 firms and included a pre-proposal conference for questions and answers. Two interested bidders attended the conference in person, one attended by phone. The County received five bids at closing, with one being disqualified for not meeting the minimum requirements. An Audit Committee, consisting of the Auditor-Controller, Assistant Auditor-Controller, Internal Audit Manager, CEO Principal Management Analyst and Deputy County Counsel, thoroughly reviewed each proposal against predetermined criteria. Technical Expertise was valued at 60% and cost was valued at 40%. Overall, the four firms were comparable in expertise, with slight variations, but the three new proposals were much higher in cost. Therefore, the bid was awarded to Gallina for 3 years with a 2 year extension option and included a change in partner assigned to the County's audit as specified in auditing best practices.

I have also attached some recent literature from three highly regarded resources in the accounting profession that provides arguments both for and against auditor rotation. The Public Company Accounting Oversight Board (PCAOB) is a nonprofit corporation established by Congress to protect the interests of investors, overseeing the audits of broker-dealers, including compliance reports filed pursuant to federal securities law. The PCAOB provided a concept paper that examines all sides of the argument with a heavy focus on the ability for private companies to “make deals” with their auditors. (Attachment A). Although they lean towards audit rotation, there is no true evidence that rotation reduces the risk of fraud and in some arguments, rotation is said to increase the potential of fraud. Invited to comment on the PCAOB’s report, the American Institute of Certified Public Accountants (AICPA) submitted a response (Attachment B). The AICPA is the world’s largest member association representing the accounting profession, with nearly 386,000 members in 128 countries, and sets ethical standards for the profession and U.S. auditing standards for private companies, nonprofit organizations, federal, state and local governments. Their position is that mandatory auditor rotation is costly and has the potential to hinder than enhance audit quality. And finally, the third attachment (Attachment C) is the related best practice standard written by the Government Finance Officers Association (GFOA). GFOA is the professional association of state/provincial and local finance officers in the United States and Canada, and has served the public finance profession since 1906. GFOA members, which I am a current member, are dedicated to the sound management of government financial resources. GFOA concluded that best practice is that governmental entities should undertake a full scale competitive process for selection every five years.

Although there are strong arguments both for and against, due diligence lies with putting proper controls and practices in place to ensure the services being provided are in the best interest of the public that the County serves. As an independently elected official, I also share this duty with you and can assure you that continuing to have the firm Gallina as the County’s independent auditor serves the best interest of the public. Gallina knows the County and can actually audit and really dig into specific areas each year instead of trying to learn about the County and spending all their time creating an audit program that simply verifies proper signatures and correct documentation. Furthermore, the learning curve of a new audit firm, not only defers in-depth auditing procedures for the first few years, it also demands a greater amount of County staff time over the period of the audit, making it even more costly.

Overall, I do not agree with changing an audit firm just for the sake of changing firms. Highly regarded industrial publications show that the best practice is to solicit bids every five years to ensure you have the most qualified firm within the market rate. We did this and we will continue to do this. Best practice also states that you should mitigate risks of keeping the same firm by mandatory partner and audit staffing changes which provides the same “new look” as a different firm would have, but at a much less cost to the County and tax payers. With the new contract awarded, we required a partner change and that they rotate their audit staff assignments each year.

I would be happy to meet with you anytime if you have any additional questions or concerns.