

# SECTION 7

# AUDIT REQUIREMENTS

- 7.1 Purpose
- 7.2 Legal Requirements
- 7.3 Audit Preparation
- 7.4 Audit Process
- 7.5 Audit Reports
- 7.6 Reporting Requirements

## NAVAJO COUNTY FISCAL POLICY MANUAL

### 7.1 PURPOSE

Arizona Revised Statutes (A.R.S.) §41-1279.21(A) (1) requires the Arizona Office of the Auditor General (OAG) to ensure that counties are audited annually. The OAG may perform the annual audit or may contract with an independent certified public accounting firm to perform the audit. The audits must be conducted in accordance with Generally Accepted Auditing Standards (GAAS) established by the American Institute of Certified Public Accountants (AICPA) and the standards for financial audits contained in *Government Auditing Standards (GAS)* issued by the Comptroller General of the United States. Additionally, counties that expend more than \$500,000 in federal awards during a fiscal year must have an audit to determine compliance with requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. The County's federal grant compliance audit will be conducted in accordance with applicable provisions of GAAS, GAS, and OMB Circular A-133. GAAS require that the audit be planned and performed to obtain reasonable assurance that the financial statements are free of material misstatement. GAS require that the auditor report on the county's internal control over financial reporting and compliance with laws, regulations, contracts, and grant agreements. The *Single Audit Act Amendments of 1996* and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, extends the auditors' responsibilities to include reporting on the Schedule of Expenditures of Federal Awards (SEFA), expressing an opinion on the county's compliance with requirements applicable to major programs, and reporting on the county's internal control over compliance with requirements applicable to major federal programs.

In addition, counties are required to prepare an annual expenditure limitation report (AELR) that also must be audited. The AELR is reported on the basis of accounting prescribed by the uniform expenditure reporting system as required by Arizona law and delineated in the OAG's *Uniform Expenditure Reporting System (UERS)* manual.

The county's basic financial statements (BFS) are the responsibility of county management. The auditors' responsibility is to express an opinion on the BFS based on the audit. County management is responsible for adopting sound accounting policies and for establishing and maintaining internal controls that will help to ensure that financial data is recorded, processed, summarized, and reported consistently with management's assertions embodied in the BFS.

This section discusses audit requirements along with audit preparation, the audit process and reporting requirements.

### 7.2 LEGAL REQUIREMENTS

- A. The legal requirements pertaining to audit requirements are derived from federal laws and regulations and A.R.S. Counties should refer to these sources for additional information.

## NAVAJO COUNTY FISCAL POLICY MANUAL

1. Counties must prepare annual BFS in accordance with U.S. Generally Accepted Accounting Principles (GAAP). In addition, Arizona Constitution, Article IX, §20 requires each county to prepare an AELR. A.R.S §41-1279.07(A) (1).
2. The AELR must be filed with the Auditor General within four (4) months after the close of each fiscal year, unless an extension is granted. A.R.S. §41-1279.07(C).
3. The Board of Supervisors is required to provide to the Auditor General by July 31 of each year the name of the chief fiscal officer (CFO) designated by the county to submit the current fiscal year's AELR. The CFO must certify the AELR's accuracy. A CFO who refuses to file the county's AELR with the Auditor General within the specified time periods, or who intentionally files erroneous reports, is guilty of a Class 1 misdemeanor. A.R.S. §41-1279.07(E) and (G).
4. Each county must provide financial information for inclusion in its annual audit that verifies that Highway User Revenue Fund monies received by the county pursuant to Title 28, Chapter 18, Article 2, and any other dedicated state transportation revenues the county received are being used solely for the authorized transportation purposes. A.R.S. §41-1279.21(A) (1).
5. Counties must provide reasonable and needed facilities, and provide schedules and documents to the Auditor General under oath, upon request. A.R.S. §41- 1279.22(A).
6. The OAG will contact the county in advance to arrange a suitable date to begin audit work and inform the county of the necessary audit requirements. Any person who knowingly fails or refuses to provide documentation or to give information as required is guilty of a Class 5 felony. Any person who otherwise knowingly obstructs or misleads the OAG in the execution of their duties is guilty of a Class 1 misdemeanor. A.R.S. §41-1279.22(B).
7. The OAG is required to report the results of their examinations of the counties to the Joint Legislative Audit Committee and to the Governor as often as required by public interest. A.R.S. §41-1279.21(A) (8).
8. Counties that expend \$500,000 or more of federal awards in a fiscal year must have a single audit conducted in accordance with OMB Circular A-133 §200 and §500.

## NAVAJO COUNTY FISCAL POLICY MANUAL

9. Counties spending less than \$50 million a year in federal awards are not assigned a agency cognizant for audit. Instead, these counties are assigned an oversight agency. This is the agency that provides the predominant amount of direct funding to the county. If there is no direct funding, the federal agency with the predominant amount of indirect funding assumes oversight responsibilities. The oversight agency must provide technical advice to auditors and auditees, as requested, and may assume some or all of the responsibilities performed by the cognizant agency. OMB Circular A-133 §400(b).
10. A federal agency with oversight for a county may reassign oversight responsibility to another federal agency that provides substantial funding and agrees to be the oversight agency. Within 30 days after reassignment, both the old and new oversight agency must notify the county and, if known, the auditor. OMB Circular A-133 §105.

### 7.3 AUDIT PREPARATION

County personnel have a significant role in the audit process. An audit liaison may be assigned to coordinate the accurate and timely preparation of the County's financial statements and supporting schedules. The audit liaison may also be the primary point of contact with the external auditors to help ensure that audit requirements are met.

### 7.4 AUDIT PROCESS

- A. The Engagement Letter. The auditors issue an engagement letter to establish an understanding with the County regarding the nature of the audit including the objectives of the engagement, County management's responsibilities, the auditors' responsibilities pertaining to the audit, and the engagement's limitations.
- B. Audit Test Work. The external auditors will perform a risk assessment of the County to determine the effectiveness of internal controls. Audit procedures and test work are designed based on the results of the risk assessment. The auditor understands of the County and its environment consists of an understanding of the following five aspects:
  1. Industry, regulatory, and other external factors. This includes factors such as the competitive environment, supplier and customer relationships, and technological developments; the regulatory environment encompassing, among other matters, relevant accounting pronouncements, the legal and political environment, and environmental requirements affecting the County; and other external factors, such as general economic conditions.
  2. Nature of the entity. This includes the County's operations, governance, the types of investments that it is making and plans to make, and the County's is structure organizationally and financially.

## NAVAJO COUNTY FISCAL POLICY MANUAL

3. Organizational objectives and strategies and related business risks. This includes objectives and overall plans defined by County's management; strategies or operational approaches; and business risks that result from significant conditions, events, circumstances, actions, or inactions that could adversely affect the county's ability to achieve its objectives and execute its strategies.
  4. Measurement and review of the county's financial performance. This includes the County's performance measures. Performance measures, whether external or internal, can create pressures that may cause improvement in business performance measurers or misstatements in the financial statements.
  5. Internal control. This includes the selection and application of accounting policies consisting of five components: control environment, risk assessment, information and communication, control activities, and monitoring. The County internal control components should provide reasonable assurances regarding the achievement of County objectives in the following categories: reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.
- C. Representation Letter. As part of the audit, the auditors will obtain certain written representations from the County. The representation letter is management's assertions regarding the presentation of the County's financial statements. It includes management's acknowledgment of the County's responsibility for the fair presentation in the financial statements of the County's financial position, results of operations, and cash flows in conformity with GAAP. Other specific representations are made relating to the completeness of the information presented; information on recognition, measurements, and disclosures; and information relating to subsequent events.

### 7.5 AUDIT REPORTS

- A. The County is responsible for fair presentation of the financial statements. The auditors' responsibility is to express an opinion as to whether the financial statements present fairly, in all material respects, the County's financial position of each opinion unit, the respective changes in financial position and, where applicable, cash flows in conformity with GAAP. Based on the results of their audit the auditors will issue an Independent Auditors' Report on the Basic Financial Statements.

## NAVAJO COUNTY FISCAL POLICY MANUAL

### 7.6 REPORTING REQUIREMENTS

- A. Reporting Package. The County is required to submit to the Federal Audit Clearinghouse a reporting package that includes the BFS and federal grant compliance including the SEFA and the auditors' reports. The reporting package should also include, when applicable, a corrective action plan and a summary schedule of prior audit findings that is prepared by the County.
- B. Corrective Action Plan. At the completion of the audit, the County prepares a corrective action plan to address current audit findings. The corrective action plan includes the name of the contact person responsible for corrective action, the anticipated completion date, and the corrective action planned.
- C. Summary Schedule of Prior Audit Findings. The County is responsible for taking corrective action on previously unresolved audit findings. The status of unresolved prior audit findings is disclosed in a summary schedule of prior audit findings including those related to federal awards included in the prior audit's Schedule of Findings and Questioned Costs (SFQC).
- D. Data Collection Form. The County completes and signs certain sections of the federal data collection form that states whether the audit was completed in accordance with OMB Circular A-133 and provides information about the county, its federal programs, and the results of the audit.
- E. Report Submission. The County's audited financial statements, single audit reporting package and data collection form are submitted to the federal audit clearinghouse within the earlier of 30 days after the receipt of the auditors' reports or 9 months after the end of the fiscal year, unless a longer period is agreed to in advance by the oversight agency. The federal audit clearinghouse distributes copies to applicable federal agencies electronically. The County also submits the audited financial statements and single audit reporting package to the State of Arizona and other required governmental entities.