



State of North Carolina

Department of State Treasurer

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TREASURER

*State and Local Government Finance Division
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DEPUTY TREASURER

Memorandum No. 1096

April 15, 2008

TO: Local Government Officials and Certified Public Accountants

FROM: Sharon Edmundson, Director
Fiscal Management Section

SUBJECT: Contract to Audit Accounts (Form LGC-205) and Approval of Interim and Final Invoices

As the audit process begins for the 2007-2008 fiscal year, we offer our summary review of changes in professional education requirements, current Single Audit requirements and recently issued accounting and auditing standards. This presentation differs somewhat from prior years in that this memorandum presents only a brief summary of the changes in auditing standards, compliance audit requirements, and accounting standards. A separate, more detailed memorandum will follow that will discuss each of these areas in full. Also presented here are the procedures for the approval of audit contracts and invoices. Local Government Commission (LGC) approval is required for all contracts and invoices for audit services, including special audits and agreed-upon procedures, for local governments, public authorities, and charter schools.

The 2008 contract has only two substantive changes from the 2007 version. Item #2 on the contract is amended to make all parties to the contract aware that both the audit and the workpapers are subject to review by Federal and State Agencies including the LGC and the Office of State Auditor (OSA.) The Local Government Commission (LGC) believes that the authority to conduct these reviews already exists in the various laws and standards regarding governmental audits in North Carolina. Because of this, auditors and units of government that submitted 2008 auditing contracts on the 2007 audit contract form should be aware that they also may be subject to the review referred to in Item #2. The second change is that units that have participating PSAPs (public safety answering point) must submit an additional copy of the annual audit for the LGC to forward to the State 911 Board. We will have a list available of those units if there is a question regarding a particular unit.

As is our practice, contract forms dated 1/1/2007 and 1/1/2008 may be used to contract for audits of the June 30, 2008, fiscal year. A copy of the Contract to Audit Accounts can be downloaded from the North Carolina Department of State Treasurer's website at www.nctreasurer.com. A sample Request for Audit Proposals (RFP) for Audit Services modified for GASB 34 and the revised GAO Independence Standards also are available on the website under Auditing and Reporting Resources.

To provide for a more efficient processing of the audit contract, we have included at the end of this memorandum a checklist of items for your review. We recommend that parties to the contract review the list before submission of the contract to our office in order to avoid delays in processing due to avoidable errors. We also have included a form to be completed if your contact information has changed from the prior year. **It is not necessary to complete and submit that form unless your contact data has changed.**

Below is a brief summary of the changes in auditing standards that will be effective for 2008 audits and beyond. As stated earlier, a more detailed discussion of these standards will follow in a subsequent memorandum. Please note that the changes required by these standards are pervasive and will change the way all government audits are conducted going forward. Auditors of local governments in North Carolina are required to conduct their audits in accordance with these and all generally accepted auditing standards.

Recently Issued Auditing Standards and Interpretations

Risk Based Reporting Standards

Previously, the Auditing Standards Board (ASB) issued Statement on Auditing Standards (SAS) No. 102 *Defining Professional Requirements in Statements of Auditing Standards*, No. 103, *Audit Documentation*, and No. 112 *Communicating Internal Control Related Matters Identified in an Audit*. These SASs already have been in effect for at least a year and are required to be used in order to implement the risk based auditing standards found in SAS 104 through 111 discussed below. The auditor must have knowledge of the requirements of these two standards to properly apply the new risk based auditing standards. The LGC has issued two memoranda, LGC Memo #1088 on issues concerning *Audit Documentation* and LGC Memo #1077 on *Communicating Internal Control Related Matters Identified in an Audit*. Units of government also should be familiar with the requirements of these two SASs in order to better understand the results of their annual audit. Look for another memorandum from the LGC staff on SAS 112 later this year.

Statement on Auditing Standards No. 104 – No. 111

The AICPA Auditing Standards Board has issued eight Statements on Auditing Standards (SAS) collectively referred to as the “Risk Assessment Standards.” These new Risk Assessment Standards are effective for audits of financial statements for periods beginning on or after December 15, 2006. Any fiscal year end of December 31, 2007 or later is affected by these new standards. Most local government audits in North Carolina will first fall under these new standards for the fiscal year end of June 30, 2008.

The new risk assessment auditing standards are:

- 104 – Amendment to Statement on Auditing Standards and procedures
- (“Due Professional Care in the Performance of Work”)
- 105 – Amendment to SAS No. 95, Generally Accepted Auditing Standards
- 106 – Audit Evidence
- 107 – Audit Risk and Materiality in Conducting an Audit
- 108 – Planning and Supervision
- 109 – Understanding the Entity and its Environment and Assessing the Risks of Material Misstatement
- 110 – Performing Audit Procedures in Response to Assessed Risks and Evaluating the Audit Evidence Obtained
- 111 – Amends SAS 39, Audit Sampling

These new standards require that the auditor gain a more in-depth understanding of the control environment of the local unit. The auditor will have to understand not only the governmental sector in general, he or she also will have to understand the regulatory environment relative to the government, and will have to understand the economic environment in which the government exists. The auditor will need to gain an understanding of the structure of the unit and determine which operating or business cycles are significant to the unit. There will be more emphasis by the auditor on testing the processes and procedures that the local unit uses to monitor itself and its financial records and assets, particularly those that are a part of the operating cycles that are significant to the

unit. The new requirements dictate that the auditor place more emphasis also on testing the disclosures found in the annual financial report. The auditor also will have to maintain a thorough understanding of the accounting policies and procedures followed by the unit.

The effect of these new standards on the local governmental unit will be substantial. More audit work will be done earlier in the audit cycle than before. Under previous standards, the auditor had the option to not rely on and controls that may have been in place in the government and increase substantive testing in lieu of relying on those controls. Since the controls were not being relied upon, little documentation of them was required. Under these new standards, this will no longer be an option. The control environment must be documented in detail regardless of the intent of the auditor to rely or not rely on those controls. It is essential that the unit and the auditor determine at the beginning of the audit process which accounting or business cycles are critical.

GAO Issues July 2007 Revision of Yellow Book

The Government Accountability Office (GAO) has issued the July 2007 revision of the Government Auditing Standards, commonly known as the "Yellow Book." These revised standards have adopted the terminology and definitions found in the SAS No. 112. Therefore significant deficiencies that would be reported in a SAS No. 112 report are expected to be reported in the Yellow Book as well. The LGC believes that it is not necessary to issue a SAS No. 112 unless the auditor includes other comments or cites deficiencies that are not considered significant deficiencies.

The July 2007 revision of *Government Auditing Standards* supersedes the 2003 revision and is the final revision for 2007. This revision contains the January 2007 revisions plus updated quality control and peer review sections in chapter 3. The July 2007 revision is the version that should be used by government auditors until further updates and revisions are made.

The effective date for the 2007 revisions is for financial audits and attestation engagements for periods beginning on or after January 1, 2008, which is for the fiscal year ending June 30, 2009, for most governmental units in North Carolina. Early implementation is permissible and encouraged. For financial statement audits performed under GAGAS, the effective dates of AICPA auditing standards SAS 102, 103, and 112 will apply. **Until the 2007 GAGAS standards become effective, auditors should adopt terminology and definitions in the SAS No. 112 when reporting on internal control deficiencies and other significant deficiencies in order to promote consistency in communicating and reporting on such internal control deficiencies.**

The July 2007 revision is available only in electronic format and can be downloaded from the GAO Yellow Book Web Page: <http://www.gao.gov/govaud/ybk01.htm>. The printed version can be ordered through the [Government Printing Office \(GPO\)](#) online or by calling 202-512-1800 or 1-866-512-1800 toll free.

Highlights to the Contract to Audit Accounts

The following are items to be considered in planning for audit engagements.

1. **Acceptable contract forms** - For 2007-2008 fiscal year audits, only contract forms with revision dates of 1/1/2007 or 1/1/2008 may be used. Contracts with revision dates prior to 1/1/2007 will not be approved. (See the top left corner of the Contract to Audit Accounts for the revision date.)
2. **Units with outstanding revenue bonds** - Item #1 of the contract states that the auditor will audit all required legal disclosures of the governmental unit. Those auditors working with local governmental

units that have outstanding revenue bonds should be aware that any bond compliance statements or additional reports required in the authorizing bond documents need to be submitted to the LGC simultaneously with the local government's audited financial statements unless otherwise specified in the bond documents.

3. **Significant Deficiencies and Material Weaknesses** - Item #7 of the contract states that all matters defined as *significant deficiencies or material weaknesses* in AU 325 of the AICPA Professional Standards [Statements on Auditing Standards (SAS) No. 112] will be communicated to the Governing Board in writing. Further, a copy of any written communications concerning matters that the auditor believes will benefit management, whether or not required by AU 325, must be sent to this office. This includes the SAS No. 112 report, *Communicating Internal Control Related Matters Identified in an Audit*; the SAS No. 114 report, *The Auditor's Communication With Those Charged with Governance*; and any other letters written to management concerning their fiscal policies. **If, at a minimum, a management letter is not issued for a local government, then the auditor must submit a signed statement to this office indicating that a management letter was not issued.** Final invoices will not be approved by the LGC until the management and governance letter(s) or a statement that 'no management letter was issued,' is received by our office.

OMB Circular A-133 and *Government Auditing Standards* require the auditor to report all *significant deficiencies*. Any *significant deficiencies* cited in the management letter also must be included in the Yellow Book report and/or identified as a finding in the single audit report.

4. **Additional investigative audit work required** - Item #12 to the contract requires the auditor to inform the governing board in writing of the need for any additional investigations as a result of the audit and any additional fees required. This includes additional work required as a result of deficiencies in accounting records, compliance violations, or potential criminal activities. **The audit contract should be amended to reflect the additional work and additional fees. Any amendment to the contract must be approved by our office.**
5. **Due date for audit reports and audited financial statements** - Local governmental units and independent auditors are encouraged to contract for audit engagements as early as possible so that the auditor may promptly begin performance of the audit engagement. Item #18 of the contract states that the contract should be approved before the audit begins. Interim audit work is encouraged and in fact may be essential as part of the evaluation of the internal control structure required in a compliance audit.

It is our policy to require financial statements be submitted no later than four months after the end of the fiscal year. **Therefore, Item #6 of the contract must require audited financial statements for fiscal years ending June 30th to be submitted by October 31st. Contracts (other than amended contracts) submitted with a due date (in Item # 6) later than 4 months after the fiscal year-end will not be approved by this office.**

Auditors submitting final audited financial statements after **December 1st** (for June 30th year-end audits) **will be required to submit an amended contract** before final invoice approval can be given. After December 1st, **final** and **interim** invoice approval will require **three** copies of an amended contract, **a written explanation of the delay in submitting the audited financial statements, and a description of corrective actions to be taken to ensure the timely completion of future audit engagements.** The amended contract should include a modified due date and be signed by the original parties to the contract, unless the duties of the original parties have been assumed by other persons. **All amendments to the audit contract must be approved by a vote of the governing board in a public meeting.**

6. **Issuance of a qualified opinion** - The contract is prepared contemplating that an unqualified opinion will be issued. If the auditor becomes aware of circumstances that will prevent the issuance of an unqualified opinion, the auditor should immediately contact the staff of the LGC. G.S. 159-34(a) requires units of local government to have annual financial statements prepared in accordance with generally accepted accounting principles and that those statements be audited in accordance with generally accepted auditing standards. When the unit can prevent a qualification by performing additional work or contracting with a third party to perform additional work, we require that work to be performed. An audit report with a qualified opinion is acceptable only in circumstances where it is not possible or practical to prevent the qualification through additional work. In this case, the amended contract must state in Item #3 or #4 the reasons for the qualification. **A final invoice for the audit of financial statements upon which a qualified opinion is issued will not be approved without a contract amended in this manner.**
7. **Submission of audited financial statements to the LGC - The responsibility for filing the reports with the LGC is assigned to the auditor in Item #11 of the contract.** The failure to submit these copies by **December 1st**, regardless of when copies are presented to the unit, will result in an amended contract being required for invoice approval. In most cases, the unit still has an obligation to supply other organizations with copies of its audited financial statements. The auditor is responsible for submitting **two bound copies (three for councils of governments and units with participating PSAPS that must report to the State 911 Board)** of the audited financial statements and the management letter to the LGC when a single audit has been performed under the requirements of the federal Single Audit Amendments of 1996 and OMB Circular No. A-133, when a single audit is required to be performed under the requirements of the State Single Audit Implementation Act only, or a financial audit is required to be performed in accordance with Government Auditing Standards. The auditor also is required to submit one copy of the federal Data Collection Form to the LGC to fulfill the terms of the contract.

The LGC provides the additional required copy of the reporting package to the State agency that most commonly distributes funds to that type of government to allow the agency to follow up on identified compliance and internal control problems. We will distribute this copy of the audit report for the following types of entities to the agencies indicated below. The Agencies listed below utilize only copies of the reporting package that have first been reviewed by the staff of the LGC, so copies sent directly to these agencies by the unit or auditor will be discarded.

Unit of Government

Boards of Education and Charter Schools
Counties
Regional Mental Health Centers
Councils of Governments

District Health Departments
Hospitals
Municipalities
Regional Libraries
Regional Airports

State Agency Receiving Copy of Report from LGC

Department of Public Instruction
Department of Health and Human Services
Department of Health and Human Services
Department of Health and Human Services and
Department of Commerce
Department of Health and Human Services
Department of Health and Human Services
Department of Transportation
Department of Cultural Resources
Department of Transportation

The audit report we send to the Department of Health and Human Services (DHHS) will be utilized by all of the divisions within that agency. Each local government will be responsible for providing copies to other State agencies that provided assistance in programs that had findings. In addition to the copies required to be submitted to the LGC and the federal clearinghouse, one copy of the reporting package must be submitted to each State grantor that provided State financial assistance, except for the State agencies that receive copies of the reports from the LGC as noted above.

Submission of audit reports by Municipalities to the N.C. Department of Transportation - The Local Government Commission is requiring that **two** copies (**three if the unit has a participating PSAP**) of **tax levying municipal** audit reports be submitted, regardless of the level of audit performed. The LGC will forward the second copy to the NC Department of Transportation (DOT) upon review and approval of the audit. In previous years, the LGC would submit only audits that were performed under Governmental Auditing Standards (Yellow Book), which includes Single Audits.

All others units whose audits are not performed under Single Audit or Government Auditing Standards or do not have a participating PSAP should submit only a **single bound** copy of the audited financial statements to the LGC. All audited financial statements should include a management letter or a letter stating no management letter was issued.

8. **Secondary market disclosure requirements** - Item #11 of the contract acknowledges the use of the audited financial statements by units with outstanding debt to fulfill secondary market disclosure requirements imposed by the U.S. Securities and Exchange Commission. Units will have to submit copies of their annual financial statements to all nationally recognized municipal securities information repositories (NRMSIRs).
9. **Use of engagement letters** –SAS No. 108 (AU 311) states that engagement letters should be used. **A copy of the letter should be included with the contracts when submitted to our office. Also, the engagement letter should be referenced in Item #14 of the audit contract.** The engagement letter will be void as to any terms that conflict with the audit contract (See Item #16 of the Contract to Audit Accounts). Contracts with engagement letters that contain indemnification clauses will **not** be approved by our office. The auditor and unit may not by mutual agreement exclude audit-related services from the scope of the contract and from approval of the Secretary of the LGC. Any agreement relating to the audit engagement (i.e. engagement letter) that is not attached to and referenced in the Contract to Audit Accounts will not be enforceable. Audit fees should be specified in the contract as Item # 9 or a reference given to the engagement letter if the fee structure is included there.
10. **Additional State Requirements to Audit Certain Federal Programs as Major** – The Office of State Auditor (OSA) performs the Single Audit for the State of North Carolina. For several major programs of the State, a local government will make eligibility determinations. Under the 2003 federal Compliance Supplements, OSA would have to either test the eligibility determinations made by local governments or rely upon the testing of eligibility by local government auditors. The OSA, North Carolina Association of County Commissioners (NCACC), North Carolina Association of Certified Public Accountants (NCACPA), and several county finance officers agreed that the local government auditors would test this new eligibility requirement. In order to meet the objectives of this compliance requirement, the OSA will identify major programs of the State that have eligibility determinations made by the local government. OSA will determine which local governments need to have the program included as a major program in their audits. OSA has committed to make this notification as early in April as possible each year. A complete discussion of this requirement can be found in LGC Memorandum No. 993.

For those units that have eligibility determinations for the Single Audit for the State of North Carolina, the auditor will have to complete and submit additional documentation with the contract and audit report. Additional documentation that is required by the local government auditor is a one page “Turnaround Document” and a CPA Representation letter addressed to the State Auditor, The Honorable Leslie W. Merritt, Jr., CPA. These are submitted to our office along with the audit report. The OSA, as part of their audit documentation to satisfy the federal eligibility compliance requirement, will use the turnaround document. Copies of both the turnaround document and representation letter may be obtained at our

Single Audit Resources website. The LGC will not approve invoices for audit reports that do not have the required turnaround document and CPA representation letter enclosed with the audit-reporting package.

11. **Peer reviews to be provided to governmental units and LGC** - By accepting an audit engagement that is subject to the standards for audit as set forth in Government Auditing Standards issued by the Comptroller General of the United States, the auditor warrants that he/she will meet all of these standards, as well as the standards for a peer review and continuing professional education. Item #5 of the contract requires the independent auditor to provide a copy of their most recent peer review report to the governmental unit and the Secretary of the LGC.
12. **Fee Structure-** The fees structure under Item #9 is divided into 3 elements: year-end bookkeeping assistance, audit, and preparation of financial statements.

The fee for the each element may be a fixed amount, a variable amount, or a combination of both. The fixed fee must be stated as a fixed dollar amount. The variable fee must be stated as a rate per hour or rate per some other unit of work. For instance, some contracts specify a certain rate per major program for the compliance portion of the audit. Variable rates for the contract must be shown on the face of the contract or in the engagement letter or addendum attached to the contract. A maximum limit may or may not be stated.

If both a fixed and a variable fee are shown, the contract must clearly indicate how those fees are to be determined. The contract should specify what services the fixed portion covers. The contract may show a minimum or maximum fee. The variable fee must be stated as a rate per hour or rate per some other unit of work. If standard hourly rates are submitted on a separate sheet, all parties should confirm the rates before LGC approval of contract.

The invoice should show all calculations necessary to compute the fee from the rates shown in the contract.

Auditors performing Yellow Book and Single Audits may perform very limited bookkeeping services for their client. Therefore, we anticipate that the line for year-end bookkeeping assistance under item # 9 will be blank or contain limited fees. Please refer to Memo #994 for further discussion of this issue. Fees for proposing adjusting entries should be included with fees for audit services.

13. **Signatures that must appear on the contract** - The mayor or chairman of the governing board must sign the contract and type or print his/her name and title in the space provided. The manager or executive director cannot sign in place of the mayor or chairman. The representative of the audit firm should print or type his/her name above his/her signature. The audit firm representative must be a partner or someone with the authority to legally contract for the firm. The Finance Officer of the governmental unit must sign and date the preaudit certificate on the bottom of page two of the contract. (The pre-audit certificate is not required for public hospitals or charter schools.)

The contract form includes a signature line for the Chairman of the Audit Committee. We feel that for those of you that have established an audit committee, the committee should be a part of the contracting process. For units that have not established an audit committee, this line should be marked "N/A".

14. **Audit Committees-** Units with audit committees should fully utilize them. In order for the unit and the auditor to understand what is occurring at each stage of the audit, communication between the two parties is essential. Regular meetings between the auditor and audit committee are strongly encouraged in order

to discuss and resolve issues that arise during the course of the audit. Units without audit committees are encouraged to establish such a committee.

15. **Local governmental units preparing a CAFR** - Local governmental units that are preparing and printing a CAFR will routinely need additional preparation time and three to four weeks printing time, which may prevent the auditor from submitting final bound and printed copies of the CAFR to this office by October 31st. We allow two options to overcome this problem. First, we will accept reports that meet the terms of the audit contract for the purpose of invoice approval. These reports should be complete, accurate and contain any required compliance reports. The appropriate number of copies should be forwarded to our office. Two copies of the final bound CAFR should be forwarded to our office when completed.

Second, a unit or auditor may prefer to submit a single camera-ready copy of a CAFR to be reviewed for invoice approval. This copy must include all signed opinions and reports as well as all necessary statements and schedules. We will still need to receive the appropriate number of final bound copies as soon as they become available.

Approval of Interim and Final Invoices

As addressed earlier in this memo, auditors performing a Yellow Book or Single Audit may not perform bookkeeping services or make management decisions for the client. Consequently, if year-end bookkeeping is needed to prepare the records for audit, the auditor cannot do it. A determination should be made as early as possible if bookkeeping services are needed so that the unit may secure the needed assistance of a third party (unless the audit is a GAAS audit) and that the audit may proceed in a timely matter.

A significant portion of the auditor's total charges could be determined by the condition of the local government's accounting records. Communications between the local governmental unit and its independent auditor about the condition of the accounting records should be established prior to setting a fee for the audit engagement. This is particularly important when the auditor is performing its initial review of the client. The local governmental unit should discuss with the auditor the preparations and assistance that can be provided by its personnel before the auditor begins the audit. The work to be performed by each party should be clearly defined before the contract is signed.

1. **Setting the fee for the audit engagement** - The fee for the audit engagement may be stated as a fixed dollar amount or as a rate per hour or day, with or without a maximum limit being stated. If a fixed fee for the audit is not stated, the invoice should show all calculations necessary to compute the fee from the rates shown in the contract. Fees for non-auditing services, such as systems design, management consulting, and accounting services performed on a regular basis (i.e., monthly or quarterly), should not be included in the fee for the audit and bills for these services should not be submitted to the LGC for approval. **However, once a contract is signed, all accounting, bookkeeping, and financial reporting services necessary to prepare for the audit, as permitted by the auditing standards applicable to the audit, are covered by the audit contract, and invoices for these services must be approved by this office as required by G.S. 159-34.** Contracts will not be approved if these fees have not been detailed. Also, if fees are discussed in the engagement letter, they also must be disclosed in Item #9 of the contract. **If the original contract contemplates that only an audit will be performed, the auditor should indicate "N/A" on the fee lines for year-end bookkeeping assistance and preparation of the financial statements.**

2. **Unforeseen circumstances requiring additional work** - Circumstances requiring additional work and compensation are sometimes inevitable. The contract can and should be revised as soon as these conditions become known (Item #12 - Contract to Audit Accounts). Invoices in excess of a fixed fee contract cannot be approved without a properly executed contract amendment with the appropriate signatures of all involved parties. Payments for any procedures related to possible criminal activity must be covered by the audit contract, and this office must approve invoices for those services.
3. **Progress billings** - Progress billings may be made if the local governmental unit and the auditor both concur. The staff of the LGC may only approve up to 75% of a fixed fee contract. On variable fee contracts, approval of interim billings is based on 75% of the fixed portion of the fee (if there is a fixed portion) or 75% of the prior year's total fee, whichever is greater. If a portion of the fee is variable, the entire fee is considered variable. **No progress billings for June 30th year-end audits will be approved after December 1st without receipt of the audited financial statements or a properly amended contract with a due date extending beyond December 1st and a written letter of explanation.**
4. **Approval of invoices by the LGC** - No interim or final bills for audit services may be paid by the local governmental unit prior to approval by the Secretary of the LGC. Before any invoices can be approved, there must be an approved contract on file with the LGC. Invoices should be submitted in triplicate. Upon approval by the Secretary, the original and one copy will be returned to the auditor.
5. **Submission/approval of final invoices** - Final invoices for audit services are normally submitted to our office with the unit's audited financial statements. We will contact auditors by fax if revisions to reports are required; otherwise, sending approved invoices by mail is our means of communicating that the audit reports and audited financial statements have been accepted. Final invoices may be submitted separately from the audited financial statements; however, they cannot be approved until we receive all required copies of the report and management letter or a letter stating that no management letter will be issued and LGC approved copy/changes are reaccepted. [Note: An exception involves the situation in which a local governmental unit is printing its CAFR. In this case, final invoices can be approved when the final camera-ready form of the CAFR (including the required signed opinions, reports, and schedules related to a single audit) is approved by our office. A cover letter should accompany the copy of the CAFR clarifying this situation. Two copies of the printed CAFR should be submitted as soon as they are available. As an alternative, we will approve invoices on the basis of financial statements that satisfy the requirements of the audit contract if a unit is preparing a CAFR.
6. **Requests for revisions/corrections to audit reports or audited financial statements** - Corrections and/or revisions requested by the staff of the LGC must be reviewed and accepted by the staff of the LGC before final invoice approval is made. Auditors may submit copies of corrected pages, which will be inserted into the original report or audited financial statements by our staff. If the number of corrections is extensive, new bound copies of the report may be requested. If changes are made to the report, the unit and the auditor must change all copies of the report that have been distributed. If additional copies have been sent to other federal or State agencies, those copies should reflect any corrections made. Anytime an audit report or audited financial statements are revised after being submitted to the LGC, revised copies must be sent to the LGC, regardless of whether the revisions were requested by the LGC.

Review of Drafts of Audited Financial Statements

Our office will review camera ready final copies only for those units that are issuing a comprehensive annual financial report or have a scheduled bond sale. In those cases we must receive a camera ready final copy of the entire report and the management letter. However, there is no deadline for submitting these drafts for review.

Requests for Audit Fee Information

Audit contract fees and terms for North Carolina local governmental units are public information. We frequently receive requests for this information from local governmental units and independent auditors. It is our responsibility to maintain adequate documentation and to provide accurate information to benefit both the local governmental unit and the independent auditor. We appreciate your cooperation and assistance in accomplishing this goal. A listing of audit fees is available on our website at www.nctreasurer.com, under "State and Local Government Finance," then "Auditing and Reporting Resources". Questions concerning invoices should be directed to Lisa Olson at (919) 807-2382 or lisa.olson@nctreasurer.com

If you have questions or comments related to this memo, please contact Alexia Forte for contract issues at (919) 807-2393 or alexia.forte@nctreasurer.com. Please contact Jim Burke for compliance audit issues (919) 807- 2389 or james.burke@nctreasurer.com. A fill-in copy (in pdf format) of the 2007 contract is available on our website at www.nctreasurer.com. Select "State and Local Government Finance", then "Auditing and Reporting Resources", then "Memos". The contract form will be at the beginning of the list of documents.

IMPORTANT

In an effort to streamline our communications efforts and increase our efficiency in publishing new documents, we are increasing the use of email as a means of notifying units of government and their auditors of newly available resources. We feel that transmitting data electronically is more efficient and more easily shared with other staff, in addition to eliminating postage and printing costs. In that regard, please provide us with an active email address to which we should send notification of new publications. **If your contact information has changed, please complete and fax this from to our office. If there is no change in your contact information it is not necessary to complete this form.**

Name of Unit: _____

Contact: _____

Active email address
(primary means of communication): _____

Rewrite email address to confirm: _____

Fax number (secondary means of communication): _____

**IF YOUR CONTACT INFORMATION HAS CHANGED
PLEASE FAX THIS COMPLETED PAGE TO OUR OFFICE
AT (919) 807-2398, CALL LISA OLSON AT (919) 807-2382 OR
EMAIL LISA.OLSON@NCTREASURER.COM.**

CONTRACT TO AUDIT ACCOUNTS

File in Triplicate.

of _____
Governmental Unit

On this _____ day of _____, _____, _____
Auditor

Mailing Address
_____, hereinafter referred to as

the Auditor, and _____ of _____, hereinafter referred
Governing Board Governmental Unit
to as the Governmental Unit, agree as follows:

1. The Auditor shall audit all statements and disclosures required by generally accepted accounting principles and additional required legal statements and disclosures of all funds and/or divisions of the Governmental Unit for the period beginning _____, _____, and ending _____. The non-major combining, and individual fund statements and schedules shall be subjected to the auditing procedures applied in the audit of the basic financial statements and an opinion will be rendered in relation to (as applicable) the governmental activities, the business-type activities, the aggregate discretely presented component units, each major governmental and enterprise fund, and the aggregate remaining fund information (nonmajor government and enterprise funds, the internal service fund type, and the fiduciary fund types).
2. At a minimum, the Auditor shall conduct his/her audit and render his/her report in accordance with generally accepted auditing standards. The Auditor shall perform the audit in accordance with Government Auditing Standards if required by the State Single Audit Implementation Act, as codified in G.S. 159-34. If required by OMB Circular A-133 and the State Single Audit Implementation Act, the auditor shall perform a Single Audit. This audit and all associated workpapers may be subject to review by Federal and State agencies in accordance with Federal and State laws, including the staffs of the Office of State Auditor (OSA) and the LGC. If the audit and/or workpapers are found in this review to be substandard, the results of the review may be forwarded to the North Carolina State Board of CPA Examiners.
3. *This contract contemplates an unqualified opinion being rendered.* If financial statements are not prepared in accordance with generally accepted accounting principles (GAAP), or the statements fail to include all disclosures required by GAAP, explain that departure from GAAP in the space below:
4. *This contract contemplates an unqualified opinion being rendered.* The audit shall include such tests of the accounting records and such other auditing procedures as are considered by the Auditor to be necessary in the circumstances. *Any limitations or restrictions in scope which would lead to a qualification should be fully explained in an attachment to this contract.* The audit will have no scope limitations except:
5. If this audit engagement is subject to the standards for audit as defined in Government Auditing Standards, July 2007 revisions, issued by the Comptroller General of the United States, then the Auditor warrants by accepting this engagement that he has met the requirements for a peer review and continuing education as specified in Government Auditing Standards. The Auditor agrees to provide a copy of their most recent peer review report to the Governmental Unit and the Secretary of the Local Government Commission prior to the execution of the audit contract. (See Item 21.)
6. It is agreed that time is of the essence in this contract. All audits are to be performed and the report of audit submitted by _____, _____.
7. It is agreed that generally accepted auditing standards include a review of the Governmental Unit's system of internal control and accounting as same relates to accountability of funds and adherence to budget and law requirements applicable thereto; that the Auditor will make a written report, which may or may not be a part of the written report of audit, to the Governing Board setting forth his findings, together with his recommendations for improvement. That written report must include all matters defined as "significant deficiencies and material weaknesses" in AU 325 of the AICPA Professional Standards. The Auditor shall file a copy of that report with the Secretary of the Local Government Commission.
8. All local government and public authority contracts for annual or special audits, bookkeeping or other assistance necessary to prepare the Unit's records for audit, financial statement preparation, any finance-related investigations, or any other audit-related work in the State of North Carolina require the approval of the Secretary of the Local Government Commission. Invoices for services rendered under these contracts shall not be paid by the Governmental Unit until the invoice has been approved by the Secretary of the Local Government Commission. (This also includes any progress billings.) [G.S. 159-34 and 115C-447] All invoices should be submitted in triplicate to the Secretary of the Local Government Commission. The original and one copy will be returned to the Auditor. Approval is not required on contracts and invoices for system improvements and similar services of a non-auditing nature.
9. In consideration of the satisfactory performance of the provisions of this agreement, the Governmental Unit shall pay to the Auditor, upon approval by the Secretary of the Local Government Commission, the following fee which includes any cost the Auditor may incur from work paper or peer reviews or any other quality assurance program required by third parties (Federal and State grantor and oversight agencies or other organizations) as required under the Federal and State Single Audit Acts:

Year-end bookkeeping assistance – [For audits subject to Government Auditing Standards, this is limited to bookkeeping services permitted by revised Independence Standards] _____

Audit - _____

Preparation of the financial statements - _____

10. After completing his audit, the Auditor shall submit to the Governing Board a written report of audit. This report shall include, at least, Management's Discussion and Analysis, the financial statements of the governmental unit and all of its component units and notes thereto prepared in accordance with generally accepted accounting principles, combining and supplementary information requested by the client or required for full disclosure under the law, and the Auditor's opinion on the material presented. The Auditor shall furnish the required number of copies of the report of audit to the Governing Board as soon as practical after the close of the accounting period.

11. **The Auditor shall file** with the Local Government Commission two copies of the report of audit, including one copy of the federal Data Collection Form, if a federal single audit is conducted. In addition, if the North Carolina Office of the State Auditor designates certain programs to be audited as major programs, a turnaround document and a representation letter addressed to the State Auditor shall be submitted to the Local Government Commission. Two copies of the report of audit should be submitted if the audit is performed only under the provisions of the State Single Audit Implementation Act or a financial audit is required to be performed in accordance with Government Auditing Standards. Three copies of the audit should be submitted for Councils of Governments. Two copies of the audit should be submitted for tax levying Municipalities. Otherwise, one copy shall be submitted. Copies of the report shall be filed with the Local Government Commission when (or prior to) submitting the invoice for the services rendered. All copies of the report submitted **must be bound**. The report of audit, as filed with the Secretary of the Local Government Commission, becomes a matter of public record for inspection and review in the offices of the Secretary by any interested parties. Any subsequent revisions to these reports must be sent to the Secretary of the Local Government Commission. These audited financial statements are used in the preparation of Official Statements for debt offerings (the auditors' opinion is not included), by municipal bond rating services, to fulfill secondary market disclosure requirements of the Securities and Exchange Commission, and other lawful purposes of the government, without subsequent consent of the auditor.
14. Should circumstances disclosed by the audit call for a more detailed investigation by the Auditor than necessary under ordinary circumstances, the Auditor shall inform the Governing Board in writing of the need for such additional investigation and the additional compensation required therefore. Upon approval by the Secretary of the Local Government Commission, this agreement may be varied or changed to include the increased time and/or compensation as may be agreed upon by the Governing Board and the Auditor.
15. If an approved contract needs to be varied or changed for any reason, the change must be reduced to writing, signed by both parties, preaudited if necessary, and submitted to the Secretary of the Local Government Commission for approval. **No change shall be effective unless approved by the Secretary of the Local Government Commission, the Governing Board, and the Auditor.**
16. Item 17 may be completed by referencing the engagement letter and attaching a copy of the engagement letter to the contract to incorporate the engagement letter into the contract. In case of conflict between the terms of the engagement letter and the terms of this contract, the terms of this contract will control. Engagement letter terms are deemed to be void unless the conflicting terms of this contract are specifically deleted in Item 22 of this contract. Engagement letters containing indemnification clauses will not be approved by the Local Government Commission.
17. There are no special provisions except:
18. A separate contract **should not** be made for each division to be audited or report to be submitted. A separate contract must be executed for each component unit which is a local government and for which a separate audit report is issued.
19. The contract should be executed and submitted **in triplicate** to the Secretary of the Local Government Commission. The mailing address is 325 North Salisbury Street, Raleigh, North Carolina 27603-1385. The physical address is 4505 Fair Meadow Lane, Suite 102, Raleigh, North Carolina 27607-6449.
20. Upon approval, the original contract will be returned to the Governmental Unit, a copy will be forwarded to the Auditor, and a copy retained by the Secretary of the Local Government Commission. **The audit should not be started before the contract is approved.**
21. There are no other agreements between the parties hereto and no other agreements relative hereto that shall be enforceable unless entered into in accordance with the procedure set out herein and approved by the Secretary of the Local Government Commission.
22. If this audit engagement is not subject to Government Auditing Standards, then Item 5 shall be listed as a deleted provision in Item 22. An explanation must be given for deleting this provision.
23. All of the above paragraphs are understood and shall apply to this agreement, except the following numbered paragraphs shall be deleted: (See Item 16.)

Firm _____
 By _____
 (Please type or print name)

 (Signature of authorized audit firm representative)
 Date _____

Approved by the Secretary of the Local Government Commission as provided in Article 3, Chapter 159 of the General Statutes or Article 31, Part 3, Chapter 115C of the General Statutes.

 For the Secretary, Local Government Commission

 (Signature)
 Date _____

By _____
 (Please type or print name and title)

 (Signature of Mayor/Chairperson of governing board)

Date _____

By _____
 (Chair of Audit Committee- please type or print name)

 (Signature of Audit Committee Chairperson)

Date _____
 (If unit has no audit committee, this section should be marked "N/A.")

This instrument has been preaudited in the manner required by The Local Government Budget and Fiscal Control Act or by the School Budget and Fiscal Control Act.

 Governmental Unit Finance Officer (Please type or print name)

 (Signature)

Date _____

(Preaudit Certificate must be dated.)

Checklist for Contracts To Audit Accounts (Form LGC-205)

(Most Common Errors Resulting in Contract Being Returned)

- Item No. 1 - Is the fiscal year-end date correct?
- Item No. 6 - Is the due date correct? For all units, the contract due date can be no later than 4 months after the end of the fiscal year, even though amended contracts may not be required until a later date.
- For variable fees for services, are the hourly rates or other rates clearly stated? If issued separately (detailed by position's hourly rates) has it been acknowledged by the government?
- For fees for services that are a combination of fixed and variable fees, are the services to be provided for the fixed portion of the fee clearly stated? Are the hourly rates or other rates clearly stated for the variable portion of the fee?
- If the auditor is performing an audit under the yellow book or single audit rules, has year-end bookkeeping assistance been limited to those areas permitted under the revised GAO Independence Standards? Although not required, we encourage units and auditors to disclose the nature of these services in the contract or an engagement letter.
- Item No. 15- If there is a reference to an engagement letter or other document, has it been acknowledged by the government and attached to the contract?
- Does the engagement letter contain an indemnification clause?
If so, the clause must comply with Memo # 986.
- Has the preaudit certificate been SIGNED and DATED?
- Has the name and title of the Mayor or Chairperson of the governing board been typed or printed on the contract?
- Have all parties SIGNED and DATED the contract?
- Has the latest peer review report been included with the contract?