AMENDED IN ASSEMBLY APRIL 14, 2011

AMENDED IN ASSEMBLY APRIL 13, 2011

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california legislature—2011–12 regular session

ASSEMBLY BILL No. 229

Introduced by Assembly Member Lara

February 2, 2011

An act to amend Section 12410.5 of, to add Sections 12410.6, 12410.7, and 12410.9 to, and to add and repeal Section 12410.8 of, the Government Code, relating to audits.

legislative counsel's digest

AB 229, as amended, Lara. Controller: audits.

Existing law requires the Controller to superintend the fiscal concerns of the state. Existing law requires the Controller to receive every audit report prepared by any local agency to comply with the federal Single Audit Act of 1984.

This bill would require the audit reports prepared in this regard to be submitted to the Controller within 9 months of the end of the period audited or in accordance with applicable federal law. This bill would authorize the Controller to appoint a qualified certified public accountant to complete an audit report if it is not submitted by the local agency within the required timeframe, with associated costs to be borne by the local agency, as specified. This bill would require the audit to comply with the Government Auditing Standards issued by the Comptroller General of the United States. This bill would require the audits to be made by a certified public accountant that is licensed by the California Board of Accountancy and selected by a local agency from a directory of accountants to be published by the Controller by December 31 of each year. The Controller would be required to use specified criteria to determine those certified public accountants that are to be included in the directory.

This bill would require the Controller to develop a plan to review and report the financial and compliance audits of local agencies, and to review and monitor the audit reports performed by independent auditors, according to specified criteria. This bill would require the Controller, in consultation with specified entities, to propose and adopt the content of an audit guide. This bill would also require the Controller to report to the Legislature by January 31 of each year the results of the Controller's oversight activity. The requirement that the Controller report to the Legislature would be repealed on December 31, 2015.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. The Legislature finds that financial audits provide an independent assessment of, and reasonable assurance about, whether local agencies' reported financial condition, results, and use of resources are presented fairly in accordance with recognized standards. Accordingly, it is the intent of the Legislature to promote accountability over local government funding by establishing a process for reviewing and reporting on financial and compliance audits conducted of local agencies. It is further the intent of the Legislature that the Controller shall have oversight responsibilities for implementing and ensuring compliance with this act.

SEC. 2. Section 12410.5 of the Government Code is amended to read:

12410.5. (a) The Controller shall receive every annual financial audit report prepared for any local agency, as defined in Section 53890, including those reports prepared in compliance with the federal Single Audit Act of 1984 (P.L. 98-502; 31 U.S.C. Sec. 7501 et seq.) and required under any law to be submitted to any state agency, and shall, after ascertaining its compliance with that federal act, transmit the report to the designated state agency.

(b) An audit for any local agency submitted to the Controller pursuant to this section shall comply with the Government Auditing Standards issued by the Comptroller General of the United States.

(c) An audit for any local agency submitted to the Controller pursuant to this section shall be made by a certified public accountant, licensed by the California Board of Accountancy, and selected by the local agency, as applicable, from a directory of certified public accountants maintained by the Controller which shall be published by the Controller not later than December 31 of each year.

(1) In determining which certified public accountants shall be included in the directory, the Controller shall use the following criteria:

(A) The certified public accountants or public accountants shall be in good standing as certified by the California Board of Accountancy.

(B) The certified public accountants or public accountants, as a result of a quality control review conducted by the Controller pursuant to Section 12410.9, shall not have been found to have conducted an audit in a manner constituting noncompliance with subdivision (b) of this section and subdivision (a) of Section 12410.7, and the Controller referred the matter to the California Board of Accountancy for consideration of disciplinary action pursuant to subdivision (d) of Section 12410.9. In that instance, if the certified public accountant or public accountant had been included in the directory, the certified public ~~accountant's~~ *accountant* or public accountant shall be removed from the directory until such time as the board makes a determination on the matter. If the board suspends, or revokes, the certified public accountant or public accountant's license, or prohibits the licensee from performing audits of local agencies, the certified public accountant or public accountant shall be excluded from the directory until such time as he or she is in good standing with the board.

(2) Commencing with the 2011–12 fiscal year, it shall be unlawful for a public accounting firm to provide audit services to a local agency if the lead audit partner, or coordinating audit partner, having primary responsibility for the audit, or the audit partner responsible for reviewing the audit, has performed audit services for that local agency in each of the six previous fiscal

years. The Controller may waive this requirement if he or she finds that no otherwise eligible auditor is available to perform the audit.

(d) The governing board of each local agency shall include all of the following in its contracts for audits:

(1) A provision to withhold 10 percent of the audit fee until the Controller certifies that the audit report conforms to the reporting provisions of subdivision (a) of Section 12410.7.

(2) A provision to withhold 50 percent of the audit fee for any subsequent year of a multiyear contract if the prior year's audit report was not certified as conforming to the reporting provisions of subdivision (a) of Section 12410.7. This provision shall include a statement that a multiyear contract shall be null and void if a public accounting firm or independent auditor is declared ineligible pursuant to subdivision (d) of Section 12410.9. The amount withheld shall not be payable unless payment is ordered by the board or the audit report for that subsequent year is certified by the Controller as conforming to the reporting provisions of subdivision (a) of Section 12410.7.

(3) A provision that will provide the Controller access to audit working papers.

SEC. 3. Section 12410.6 is added to the Government Code, to read:

12410.6. (a) The Controller shall develop a plan to review and report on financial and compliance audits of local agencies. The Controller, in consultation with the Department of Finance, and representatives of the League of California Cities, the California State Association of County Auditors, and the California Society of Certified Public Accountants, shall propose the content of, and adopt, an audit guide.

(b) The audit reports shall be submitted to the Controller within nine months after the end of the period audited, or in accordance with applicable federal law.

(c) If the audit reports required by Section 12410.5 have not been submitted by a local agency to the Controller on or before the due date established by this section, the Controller may appoint a qualified certified public accountant to complete the report and to obtain the information required. Any cost incurred by the Controller pursuant to this subdivision, including contracts with, or the employment of, the certified public accountants in completing the audit shall be borne by the local agency and shall be a charge against any unencumbered funds of the local agency.

SEC. 4. Section 12410.7 is added to the Government Code, to read:

12410.7. (a) The Controller on an annual basis shall review and monitor the audit reports performed by independent auditors. The Controller shall determine whether the audit reports conform with the reporting provisions of government auditing standards and the audit guide and shall notify each local agency, and the auditor of each local agency regarding each determination.

(b) The independent auditor shall correct his or her audit report within 30 days of notification of any deficiency. The Controller may suspend the independent auditor from performing any local agency audits if the auditor does not correct his or her audit report within 30 days of the Controller's notification.

(c) (1) Within 30 days from the date of receipt of written notification that the Controller refuses to certify an audit report as conforming to the reporting provisions described in subdivision (a), an independent auditor or audit firm having a portion of an audit fee withheld pursuant to paragraph (1) or (2) of subdivision (d) of Section 12410.5 may file an appeal in writing with the California Board of Accountancy.

(2) The board shall complete an investigation of the appeal within 90 days of the filing of the appeal and, on the basis of the investigation, do one of the following:

(A) (i) Order the Controller to provide notification that the audit report conforms to the reporting provisions described in subdivision (a).

(ii) If the board orders the Controller to provide notification that the audit report conforms to the reporting provisions described in subdivision (a), the Controller shall notify the contracting local agency, which shall then release the portion of the audit fee being withheld in accordance with paragraph (1) or (2) of subdivision (d) of Section 12410.5.

(B) Schedule the appeal for a hearing, in which case the final action on the appeal shall be completed by the board within one year from the date of the filing of the appeal.

SEC. 5. Section 12410.8 is added to the Government Code, to read:

12410.8. (a) The Controller shall report to the Legislature by January 31 of each year the results of the Controller's oversight activity, including the results of the Controller's quality control reviews.

(b) A report submitted pursuant to subdivision (a) shall be submitted in compliance with Section 9795.

(c) Pursuant to Section 10231.5, this section is repealed on December 31, 2015.

SEC. 6. Section 12410.9 is added to the Government Code, to read:

12410.9. (a) The Controller may perform quality control reviews of audit working papers to determine whether audits are performed in conformity with government audit standards and the local agency audit guide. The Controller shall communicate the results of his or her reviews to the Department of Finance, the independent auditor, and the local agency for which the audit was performed, and shall review his or her findings with the independent auditor.

(b) Prior to the performance of any quality control reviews, the Controller shall develop and publish guidelines and standards for those reviews. Pursuant to the development of those guidelines and standards for those reviews, the Controller shall provide an opportunity for public comment. The Controller shall update the guidelines and standards for any changes in audit standards.

(c) The Controller is responsible for selecting audits for review based on criteria, including, but not limited to, disciplinary actions by the California Board of Accountancy, results of the Controller's review and monitoring of the audit reports, the extent of findings in the audit reports issued by the independent auditor, the number of audits of local agencies performed annually by the independent auditor, the independent auditor's experience in performing audits of local agencies, the complexity of state and federal programs administered by the local agencies, and requests or leads from other sources.

(d) If the Controller finds that the audit was conducted in a manner that constitutes unprofessional conduct as defined pursuant to Section 5100 of the Business and Professions Code, or that there were multiple and repeated failures to disclose noncompliant acts, the Controller shall refer the case to the California Board of Accountancy. In that instance, the independent auditor shall be prohibited from performing an audit *of a local agency* until such time as the board resolves the matter. If the California Board of Accountancy finds that the independent auditor conducted an audit in an unprofessional manner, the Controller may prohibit the independent auditor from performing any audit of a local agency for the period during which the independent auditor is not in good standing with the board, in addition to any other penalties that the California Board of Accountancy may impose.

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