



AUDITOR GENERAL

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STATE OF FLORIDA LOCAL GOVERNMENT FINANCIAL REPORTING SYSTEM Performance Audit

SUMMARY

Our performance audit of the State of Florida local government financial reporting system disclosed the following:

Finding No. 1: Auditor selection procedures were not used by all local governments and some local government officials and staff indicated they were unaware of the statutory requirements.

Finding No. 2: Local governments had not always established and used an audit committee to select an auditor, contrary to law, or used the audit committee to perform other audit oversight duties.

Finding No. 3: Factors to be used to evaluate audit services, or procedures to publicly announce and evaluate requests for proposals for audit services, were not established by all local governments.

Finding No. 4: Local government contracts for audit services did not always include the required elements, such as a finite contract term or conditions for renewal or termination. Additionally, in many instances, invoices for audit services were not in sufficient detail to determine compliance with the contracts.

Finding No. 5: Although greatly improved, some local governments continued to file paper-based annual financial reports with the Department of Financial Services (DFS) rather than file electronically.

Finding No. 6: DFS's required notification to the Legislative Auditing Committee of unaudited local governments that had not submitted an annual financial report for the 2005-06 fiscal year did not include 12 special districts.

Finding No. 7: Although greatly improved due to the implementation of the Local Government Electronic Reporting System, some unaudited local governments were still not reporting the required financial information on their annual financial reports to DFS.

Finding No. 8: Department of Management Services, Division of Retirement (DMS), did not always acknowledge the receipt of the local governments' actuarial reports or actuarial impact statements pertaining to public employee retirement systems and plans, contrary to Section 112.63(4), Florida Statutes. Furthermore, DMS did not prioritize its backlog of actuarial reports and impact statements pending review to ensure that the reviews were performed in a timely manner.

Finding No. 9: DMS did not include the required response time, or notification of the consequences for failure to provide requested information, in its correspondence with pension plan administrators. Also, DMS did not maintain a system for tracking and timely following up on requests for additional information relating to its review of public employee retirement systems and plans.

Finding No. 10: Executive Office of the Governor staff did not, in some instances, timely contact local governments that met a financial emergency condition specified in law.

FINDINGS AND RECOMMENDATIONS

Local Government Auditor Selection Process

Local government audits provide independent assessments as to the accuracy and completeness of the financial statements and are usually considered to

be vital to the development of local government bond ratings by the bond rating services, which can significantly impact the entity’s bond issuance costs. In addition, audits provide a means for evaluating the effectiveness of a local government’s internal controls and determining the extent to which the entity has complied with applicable laws, administrative rules, contractual requirements, and good business practices.

Recognizing the importance of audits, the Legislature has established general provisions for audits of local governments. Section 218.39(1), Florida Statutes, requires each county, and each municipality and special district with certain revenue or expenditure totals, that have not been notified as of July 1 in any fiscal year that a financial audit will be performed by us, to obtain an annual financial audit of its accounts and records. The audit is to be performed by an independent certified public accountant retained by the local government and paid from public funds.

Section 218.391, Florida Statutes, establishes required procedures for the selection of auditors to perform the annual financial audits required by Section 218.39, Florida Statutes. This section of law was amended by Chapter 2005-32, Laws of Florida, effective July 1, 2005, to specify a consistent auditor selection process for all counties, municipalities, special districts, and others. Many of the law changes contained in Chapter 2005-32, Laws of Florida, were based on recommendations of the Auditor Selection Task Force (Task Force), comprised of staff representatives of the Legislative Committee on Intergovernmental Relations, the Joint Legislative Auditing Committee, the Auditor General, and various audit and local government associations (e.g., Florida Government Finance Officers Association, and the Florida Institute of Certified Public Accountants). The purpose of the Task Force was to provide recommendations to the Legislature for improvements in the auditor selection requirements. The Task Force also developed non-mandatory guidelines to provide additional guidance to local governments in the implementation of the legal requirements regarding the selection of auditors. As used in this report, *Guidelines* means the *Auditor*

Selection Guidelines prepared by the Auditor Selection Task Force.

We reviewed the auditor selection process at 69 local governments to determine if local governments were complying with the requirements of Section 218.391, Florida Statutes, and the extent to which they followed the *Guidelines*. Our review disclosed that 8 local governments were not yet subject to the auditor selection procedures in effect as of July 1, 2005, because they were still under contract with audit firms (i.e., contracts that were entered into prior to July 1, 2005, and had not yet expired). Finding Nos. 1 through 4 below describe the results of our review for the remaining 61 local governments, including 5 counties, 18 municipalities, and 38 special districts.

Finding No. 1: Auditor Selection Procedures

Section 218.391, Florida Statutes, provides that each local government, prior to entering into a written contract for audit services, shall use auditor selection procedures when selecting an auditor to conduct the annual financial audit. The law requires local governments to select an audit committee, assigns certain responsibilities to the audit committee in evaluating and recommending an auditor for the annual financial audit, and specifies certain provisions that must be included in the written contract for audit services.

Of the 61 local governments reviewed, 28 entities (2 counties, 11 municipalities, and 15 special districts) did not use auditor selection procedures to select an auditor for the annual financial audit and many did not, as further discussed in finding Nos. 2 through 4, comply with the requirements of Section 218.391, Florida Statutes.

Properly performed audits play a vital role in the public sector by helping to preserve the integrity of the public finance functions and, thereby, maintaining citizens’ confidence in their elected leaders. The use of an objective auditor selection process helps ensure selection of a qualified auditor and satisfactory audit effort.

In discussing finding Nos. 1 through 4 with local government officials and staff, some indicated that they were unaware of the requirements of, or the 2005 changes to, Section 218.391, Florida Statutes. We received similar responses from local government officials and staff in discussing finding Nos. 1 through 8 in report No. 2006-186. Additionally, as further discussed in finding No. 7 and in various findings in our prior audits of the local government financial reporting system, we have recognized that technical assistance may be needed to aid smaller local governments in properly reporting information required by law.

Recommendation: Local governments should use auditor selection procedures to ensure compliance with Section 218.391, Florida Statutes. Additionally, to ensure that officials and finance officers are aware of statutorily required local government financial reporting responsibilities, we recommend that local government officials and staff attend periodic, relevant financial reporting training offered by various audit and local government associations.

Finding No. 2: Use of Audit Committees

Section 218.391(2), Florida Statutes, requires the local government’s governing body to establish an audit committee. The composition of the audit committee is not specified in law, except that the composition of a noncharter county, at a minimum, must include each of the county officers elected pursuant to Article VIII, Section 1(d) of the State Constitution, or a designee, and one member of the board of county commissioners or its designee. The primary purpose of the audit committee is to assist the governing body in selecting an auditor to conduct the annual financial audit; however, the audit committee may serve other audit oversight purposes, as determined by the entity’s governing body.

Legal Compliance. As discussed in finding No. 1 above, 28 local governments did not use auditor selection procedures. These entities, as well as one other municipality noted in our review, did not establish an audit committee, contrary to law.

Non-mandatory Guidance. According to the *Guidelines*, a properly constituted audit committee provides the governing body with the expertise needed to make informed decisions in selecting auditors; facilitates communication between management, the auditors, and the governing body; and helps to enhance the auditor’s real and perceived independence.

In addition to the statutorily prescribed audit committee responsibilities, our review included a determination as to whether the suggested practices included in the *Guidelines* were being followed by the local governments. Of the 32 local governments that did use audit committees, the audit committees of 24 entities (2 counties, 5 municipalities, and 17 special districts) were not assigned one or more additional (i.e., in addition to selection of the auditor) audit oversight responsibilities recommended by the *Guidelines*. The results of our review, as shown in Appendix A of this report, disclosed that over 70 percent of the entities that established an audit committee did not use the audit committee to perform the following:

- Monitor the audit.
- Review the financial statements prior to completion of the audit.
- Evaluate management’s proposed corrective action plan.
- Monitor corrective action taken.
- Evaluate auditor performance.

Although not required by law, use of the audit committee for responsibilities other than selecting the auditor would enhance the value of the audit committee to the local government and provide added assurance that the audit is meeting the needs of the local government and that corrective action is being taken, as anticipated.

Recommendation: Local governments should establish an audit committee as required by Section 218.391(2), Florida Statutes. Also, in addition to selecting an auditor, we recommend that local governments assign the audit committee other audit oversight responsibilities.

Finding No. 3: Requests for Proposals for Audit Services

Section 218.391(3), Florida Statutes, lists the duties of the audit committee as follows:

- Establishing factors to be used for the evaluation of audit services to be provided by the audit firm, including ability of personnel, experience, and ability to furnish the required services.
- Publicly announcing the Request for Proposal (RFP).
- Providing interested audit firms with the RFP, including information on how proposals are to be evaluated.
- Evaluating RFPs provided by qualified audit firms.
- Ranking and recommending, in order of preference, no fewer than three audit firms deemed to be the most highly qualified to perform the required services. If fewer than three audit firms respond to the RFP, the committee shall recommend such audit firms as it deems to be the most highly qualified.

Legal Compliance. Of the 32 local governments in our review that established audit committees, 2 special districts did not establish factors to be used for the evaluation of audit services and 5 entities (1 county and 4 special districts) did not publicly announce their RFP or provide information in the RFP on how proposals were to be evaluated.

Of the 29 local governments in our review that did not establish an audit committee, as discussed in finding No. 2 above, more than half of the entities did not issue an RFP; rather, they engaged the same audit firm used in the previous year. Explanations given for not issuing an RFP included:

- Town Charter specified that the auditor may be selected without the use of competitive bids.
- Upon verbally contacting three auditors, the auditor providing the lowest quote was used.
- A request for “Qualifications Statements from Qualified CPA Firms” was publicly noticed rather than an RFP. However, the request did not include information on how qualifications statements were to be evaluated.

Non-mandatory Guidance. In addition to the statutorily prescribed RFP-related responsibilities of the audit committee, our review included a determination as to whether the suggested practices in the *Guidelines* with regard to RFPs were being followed by the local governments. The *Guidelines* recommend that local governments consider using a variety of key elements in the RFP. Generally, the *Guidelines* indicate that a sound RFP should obtain from proposers the information needed to evaluate their technical qualifications to perform the audit, and provide proposers with a detailed description of the local government, its specific audit needs, and the local government’s auditor selection process. The results of our review, as shown in Appendix B of this report, disclosed numerous instances in which the RFPs did not include one or more of the key elements listed in the *Guidelines*. While not all of the elements discussed in the *Guidelines* would be applicable or necessary to all entities, certain information, such as a statement from the auditors that they meet the appropriate criteria for independence, should be included by all entities.

Recommendation: Local government audit committees should issue and evaluate RFPs for audit services as required by law. Additionally, local governments should consider inclusion of key elements appropriate to the local government in the RFP, as recommended by the *Guidelines*.

Finding No. 4: Audit Services Contracts

Section 218.391(7), Florida Statutes, provides that every procurement of audit services shall be evidenced by a written contract embodying all provisions and conditions of the procurement of such services. An

engagement letter signed and executed by both parties shall constitute a written contract. The written contract shall, at a minimum, include the following:

- A provision specifying the services to be provided and fees or other compensation to be paid for such services;
- A provision requiring that invoices for fees or other compensation be submitted in sufficient detail to demonstrate compliance with the terms of the contract; and
- A provision specifying the contract period, including renewals, and conditions under which the contract may be terminated or renewed.

Legal Compliance. Our review of 61 contracts for audit services disclosed that the contracts specified the services to be provided and the fees or other compensation for such services. However, we noted the following:

- Fifteen of the 61 contracts did not specify a finite contract period.
- Twenty of the 61 contracts did not specify the conditions under which the contract may be terminated or renewed.
- Thirty-six of the 61 contracts did not include a provision requiring that invoices for fees or other compensation (e.g., travel reimbursements, copy charges, telephone calls, etc.) be submitted in sufficient detail to demonstrate compliance with the terms of the contract.

Our review of the invoices submitted for the 61 contracts discussed above disclosed:

- Invoices submitted for 37 of the 61 contracts did not provide sufficient detail to determine whether the fees charged were consistent with the fees specified in the contract (e.g., invoice did not list staff that performed the service, hours worked, hourly rate, etc., for a contract on which staff time is specified as the basis for the fees charged).

- Invoices submitted for 30 of the 61 contracts did not include documentation supporting the actual cost incurred for reimbursable costs.

Non-mandatory Guidance. In addition to the statutorily prescribed elements of an audit services contract, our review included determining whether the suggested elements of the contract included in the *Guidelines* were being used by the local governments. The results of our review, as shown in Appendix C of this report, disclosed that a high percentage of the audit services contracts did not include the suggested elements. Some of the more common elements excluded from the contracts were:

- Language establishing the auditor’s sole liability for claims arising from the auditor’s performance of the engagement.
- Language clarifying the contract’s separate provisions should stand alone, so that a failure to meet one provision does not nullify the entire contract.
- A requirement for the auditor to obtain insurance coverage.

Although local governments must determine the most appropriate provisions for an audit services contract in a given set of circumstances, a sound contract helps to preclude any subsequent misunderstanding regarding the auditor’s responsibilities.

Recommendation: Local governments should ensure that contracts for audit services include the provisions required by law. Additionally, local governments should consider the additional contract elements recommended by the *Guidelines*.

Local Government Financial Reporting

Finding No. 5: Electronic Filing of Annual Financial Reports

Section 218.32(1), Florida Statutes, requires local governments to submit to the Department of

Financial Services (DFS) an annual financial report (AFR) covering their operations for the preceding fiscal year in a format prescribed by DFS. Additionally, Section 218.32(2), Florida Statutes, requires DFS to annually file, by December 1, a report with the Governor, the Legislature, the Auditor General, and the Special District Information Program of the Department of Community Affairs showing the revenues and expenditures of each entity required to submit an AFR.

Although DFS made available to local governments an electronic filing system that accumulated the financial information reported on the AFR in a database, we noted in our report No. 2006-186 that only 20 percent of local governments were utilizing the electronic filing system, and we recommended that DFS continue its efforts to enhance the local government database and electronic filing system. We also recommended that such efforts, at a minimum include a survey of all local governments that continue to file their AFRs manually to determine what changes, if any, would be necessary for them to use the electronic filing system.

Our current review disclosed that DFS surveyed local governments in September 2006 and obtained an understanding of the local governments' AFR filing procedures, their preferences for anticipated changes to the electronic filing system, and their availability of technology resources for electronically filing AFRs. DFS continued to enhance the electronic filing system and, in November 2007, implemented the new Local Government Electronic Reporting System (LOGER), a Web-based system for local governments to use for filing their AFRs, starting with the 2006-07 fiscal year. According to DFS's records, as of July 2008, electronic filing of AFRs, through LOGER, had increased by 59 percent as compared to the same time in the previous year, as detailed in Table 1:

Table 1 – AFR Filings

Method of Filing	As of July 1, 2007	%	As of July 1, 2008	%
Paper	932	79%	253	20%
Electronic	251	21%	995	80%
Total	1,183	100%	1,248	100%

Although the first reporting year using LOGER is still in progress (some entities have until September 30, 2008, to file the AFR for the 2006-07 fiscal year), based on these results, it appears that DFS has been successful in increasing the number of electronic filings of AFRs. The AFR information provided through LOGER systematically updates DFS's database, which is used to prepare DFS's annual report pursuant to Section 218.32(2), Florida Statutes. For those entities that do not file the AFR electronically with DFS, DFS staff must manually record the information into its database from the paper copies filed. This is both an inefficient use of DFS staff resources and increases the likelihood of error in recording the data. As further discussed in finding No. 7, as a result of its online edits, the use of LOGER also assists the local governments by notifying them of incomplete data.

Recommendation: To ensure continued success in the electronic filings of AFRs, and ultimately eliminate paper-based AFRs, we recommend that DFS formally require the electronic filing of AFRs through LOGER.

Finding No. 6: Reporting of Noncompliant Local Governments

Section 218.32(1)(d), Florida Statutes, requires local governments that are required to provide for an audit in accordance with Section 218.39, Florida Statutes, to submit an AFR to DFS no later than 12 months after the end of the fiscal year. Additionally, Section 218.32(1)(e), Florida Statutes, requires local governments that, in a given fiscal year, are not required to provide for an audit pursuant to Section 218.39, Florida Statutes, to submit the AFR to DFS no

later than April 30 of the following year. Pursuant to Section 218.32(1)(f), Florida Statutes, if DFS does not receive a completed AFR from the local government within the required period, DFS shall notify the Legislative Auditing Committee (LAC) of the local government’s failure to comply with the reporting requirements. LAC shall proceed in accordance with Section 11.40(5), Florida Statutes, which provides for the possibility of withholding of State funds payable to such local government until it complies with the law.

Our review disclosed that DFS timely notified LAC of those local governments that, although required, did not submit an AFR to DFS by April 30, 2007, or September 30, 2007, for the 2005-06 fiscal year, and by April 30, 2008, for the 2006-07 fiscal year. However, our review of DFS’s notifications to LAC for the 2005-06 fiscal year (dated May 1, 2007, and January 10, 2008) disclosed that the information was incomplete. Using the Official List of Special Districts on the Department of Community Affairs’ (DCA) Web site, we identified 11 special districts, with creation dates ranging from February 27, 2001, to September 25, 2006, which should have been, but were not, included in DFS’s notifications to LAC. In response to our inquiry as to the reason for not including these 11 special districts in the 2005-06 fiscal year notifications to LAC, DFS personnel stated that, since the special district information was not initially recorded on the DCA Web site until the 2006-07 fiscal year, they did not feel it would be appropriate to include the 11 special districts in the notifications to LAC for the 2005-06 fiscal year. Neither the date on which these special districts notified DCA of their existence, nor the date on which the DCA added them to its Web site, has any affect on the special districts’ responsibility to file an AFR with the DFS.

In addition to the special districts omitted from the DFS notifications discussed above, we identified an independent special district that did not file an AFR for the 2005-06 fiscal year and was not included on the DFS notification. However, DFS did not include this special district in its notification to the LAC because the district’s information was included as a component

unit in the AFR of the county in which it was located. Section 218.32(1)(a), Florida Statutes, requires all independent special districts to separately file an AFR with DFS.

Recommendation: DFS should ensure that all known entities that fail to provide the required AFR are included in its notifications to LAC, including independent special districts that were reported on the AFR of the governing authority wherein they are located.

Finding No. 7: Significant Financial Trends Reporting

Section 11.45(7)(f), Florida Statutes, requires us to annually compile and transmit to the President of the Senate, the Speaker of the House of Representatives, and the LAC a summary of significant findings and financial trends identified in local government audit reports. The summary must also include financial information (balance sheet information) included in AFRs for those local governments not required to provide for an audit.

In our report No. 2006-186, we noted that some local governments had either not submitted the required information or submitted inaccurate information and recommended that DFS consider providing technical assistance to smaller local governments to assist them on proper completion of the AFR; review AFRs received for reasonableness; and, if necessary, request additional information from the local governments.

In response to our request on the status of DFS’s actions regarding our recommendations, DFS personnel stated that their procedures for certifying all AFR submissions included reconciling the AFR to a checklist of materials required for a successful submission and communicating via telephone, electronic mail, or fax with the local government to assist in completing the AFR and requesting missing information. Additionally, DFS included system edits in its LOGER system (as discussed in finding No. 5), which was available for electronic AFR filing beginning with the 2006-07 fiscal year, that prevent unaudited local governments from electronically filing

AFRs without the inclusion of the necessary balance sheet information.

Our review of AFRs required to be submitted to DFS by April 30, 2007 (for the 2005-06 fiscal year), disclosed that 23 (46 percent) of the 50 AFRs reviewed did not contain the required balance sheet information. Our review of AFRs required to be submitted to DFS by April 30, 2008 (for the 2006-07 fiscal year), disclosed that while all of the electronically filed AFRs contained the required balance sheet information (as a result of LOGER’s online edits), there were 4 of 14 paper-based AFRs (28 percent) reviewed that did not contain the balance sheet information. AFR information is important for our reporting of complete and accurate information regarding financial trends to the President of the Senate, the Speaker of the House of Representatives, and the Legislative Auditing Committee, as required by law.

Recommendation: DFS should continue its technical assistance to smaller local governments to assist them with proper completion and filing of the AFR.

Finding No. 8: Review of Actuarial Reports and Impact Statements

Chapter 112, Part VII, Florida Statutes, provides for the operation and funding of public employee retirement systems and plans, and requires each system and plan to have regularly scheduled actuarial reports prepared and certified by an enrolled actuary. The frequency of the actuarial reports is to be at least every three years commencing from the last actuarial report of the plan or system, and the actuarial report is to be furnished to the Department of Management Services, Division of Retirement (DMS), within 60 days after receipt from the actuary. Additionally, actuarial impact statements of proposed changes to local retirement systems are to be furnished to DMS. Upon receipt of the actuarial report or actuarial impact statement, DMS is to acknowledge such receipt, but shall review and comment on each retirement system’s

or plan’s actuarial valuations at least on a triennial basis.

Our review of 15 actuarial reports and impact statements received during the 2007 calendar year disclosed that, although required by law and DMS procedures, DMS records did not evidence the required acknowledgement of receipt in 3 instances (20 percent). In response to our inquiry, DMS personnel stated the reasons were due, in part, to a delay in implementing an acknowledgment procedure and to employee turnover.

According to DMS records, as of December 31, 2007, there were a cumulative total of 2,150 actuarial reports and 1,252 impact statements that were received but not “State accepted.” DMS typically documented the completion of its review by providing a letter of “State acceptance” to the pension plan administrator and by recording “State acceptance” in its records. According to DMS records, of the 2,150 actuarial reports and 1,252 impact statements that had not been reviewed by DMS, 1,040 actuarial reports (48 percent) and 637 impact statements (51 percent) were reported as received at least three years ago, with three impact statements reported as received as far back as 1994. We noted in our review of the records that multiple, consecutive years and types of pension plans (e.g., reports for a particular government’s police pension plan for 2002, 2003, 2004, and 2005) had been submitted by many of the local governments, with no indication of review priority or the triennial review schedule provided for in law. Although requested, we were not provided with a cumulative listing of the actuarial reports and impact statements received, but not “State accepted,” in priority order for DMS review. Such a listing would benefit DMS in identifying its backlog of actuarial reports and impact statements pending review in order to request any needed resources to perform the statutorily required reviews in a timely manner.

Furthermore, our review of ten current “State acceptance” letters (issued between February and May 2008, and referencing actuarial reports and impact statements for the years from 1999 to 2007) disclosed

that multiple consecutive years continue to be included in DMS’s review of a local government’s actuarial report or impact statement, although the law provides for the review at least on a triennial basis. More frequent reviews of actuarial valuations than specified in law may have contributed to the backlog of reports to review.

A similar finding was noted in our report Nos. 2004-006 and 2006-186, issued in July 2003 and June 2006, respectively. Additionally, in our report No. 2006-186, we noted that DMS had not adopted written procedures for the review of actuarial plans and impact statements and recommended that such procedures be established. The Secretary of DMS at that time, in his written response to that report, stated that a written procedures manual was compiled to document the policies and procedures that are to be followed during the review process. Section 2.1 of the procedures manual, dated May 10, 2006, indicates that staff will consult the list of plans quarterly and prioritize the review schedule to ensure that each retirement system’s actuarial valuations are reviewed and commented on at least on a triennial basis and that staff will update the schedule as necessary to maintain the integrity of the three-year review cycle. Although the DMS has established written procedures for the review of actuarial reports and impact statements, our review disclosed that those procedures were not being effectively implemented.

Recommendation: DMS should ensure that all local governments are notified in a timely manner that DMS has received their actuarial reports and impact statements. Additionally, DMS should take appropriate action to ensure that reviews are performed in a timely manner, and that the written procedures established for the review of actuarial reports and impact statements are followed, including prioritizing its backlog based on the triennial review schedule provided for in law.

Finding No. 9: Actuarial Report Information Requests

Section 112.63(4), Florida Statutes, provides DMS with the authority to notify the pension plan

administrator and request the additional information needed in instances in which a local government does not submit complete and adequate data necessary for DMS to perform its statutorily required functions. Additionally, DMS Rule 60T-1.005(1), Florida Administrative Code, provides that the local government shall comply with the request within 60 days from the receipt of the request. Furthermore, to compel local governments to respond timely to DMS requests for additional information or concerns regarding the actuarial soundness of general pension plans, the law requires DMS to notify the affected governmental entity of the consequences for failure to comply with the requests, which includes requiring the Department of Revenue and the Department of Financial Services to withhold certain funds.

Our review disclosed that during the period October 1, 2006, through September 30, 2007, DMS sent 56 letters to local governments requesting additional information regarding the local governments’ retirement systems or plans. However, these letters did not inform the local governments of the requirement to respond within 60 days from the receipt of the request or the consequences for failure to comply with the requests, contrary to law. Of the 56 letters that were sent, 17 local governments (30 percent) had not responded as of February 2008, and 24 local governments (43 percent) responded from 3 to 255 days past the required 60-day period. We requested from DMS, but were not provided, a prioritized listing of outstanding correspondence related to unresolved local government retirement system issues. Such a listing would benefit DMS in tracking and timely following up on outstanding issues with the actuarial reports and impact statements. In response to our request for procedures regarding the receiving, tracking, responding, and monitoring of correspondence, DMS personnel stated that they are updating their procedures and will be improving the process to ensure timely review and follow-up to plan responses. DMS personnel also stated that the procedures will specifically outline how the status of correspondence will be tracked, including the generation of an aging report.

A similar finding was noted in our report No. 2006-186, issued in June 2006. In that report, we recommended that DMS establish written procedures for the follow-up of requests for information for which responses were not received. Section 3.5 of the written procedures established by the DMS (discussed in finding No. 8) require staff to notify the plan administrator and plan sponsor of the remedies available to the Department under the provisions of Section 112.63(4), Florida Statutes, for a failure to provide the requested information within a reasonable period of time. However, we were provided no evidence of follow-up on those instances in which additional information had been requested but not received within 60 days.

Recommendation: DMS should include the required response time and indicate the consequences for failure to provide the requested information, as provided for in law and rule, in requests to pension plan administrators for additional information. Additionally, DMS should establish a tracking system for its correspondence to ensure timely monitoring and follow-up, and, if necessary, enforce the consequences for failure to provide the required information in a timely manner.

Finding No. 10: Financial Emergencies

Section 11.45(7)(e), Florida Statutes, requires us to notify the Governor and LAC of any local government audit report we review that contains a statement that the entity has met one or more of the conditions specified in Section 218.503(1), Florida Statutes. Upon notification, Section 218.503(3), Florida Statutes, provides that the Governor, or his or her designee, shall contact the local governmental entity to determine what actions have been taken by the local government to resolve the condition. The Governor shall determine whether the local government needs State assistance to resolve the condition and, if State assistance is needed, the local government is considered to be in a state of financial emergency. The Governor has the authority to implement measures to assist the local government in resolving the financial emergency.

Our review of 20 local governments, for which we notified the Executive Office of the Governor (EOG) during the 2007 calendar year that the local government’s audit report contained a statement that the local government met one or more of the specified financial emergency conditions, disclosed that EOG took the following actions with regard to its oversight responsibilities:

- Eight entities were in the process of being analyzed, but no determination of financial emergency had been made. However, at the time of our review, EOG was in receipt of our information an average of 115 days (ranging from 54 days to 252 days).
- One entity had not responded to the EOG’s request for information, so no determination was made.
- Four entities were determined to not be in a state of financial emergency. The determination was made an average of 182 days (ranging from 33 to 273 days) following the receipt of our notification.
- One entity was not contacted due to the misfiling of our notification letter, which was sent 358 days previously.

While the law does not provide a time certain for EOG to contact local governments or to make a determination of a state of financial emergency, the more timely the contact and determination is made, as applicable, the sooner State assistance could be provided, if required.

Recommendation: EOG should timely contact local governments which have met a financial emergency condition and make the determination as to whether or not the local government is in a state of financial emergency.

SCOPE AND OBJECTIVES

Section 11.45(2)(h), Florida Statutes, requires the Auditor General to make a performance audit of the local government financial reporting system (System) at least every two years to determine the accuracy, efficiency, and effectiveness of the System in achieving its goals and to make recommendations to the local governments, the Governor, and the Legislature as to how the reporting system can be improved and program costs reduced. The “System” means any statutory provisions related to local government financial reporting and is intended to provide for timely, accurate, uniform, and cost-effective accumulation of financial and other information that can be used by members of the Legislature and other appropriate officials to accomplish the following goals:

- Enhance citizen participation in local government;
- Improve the financial condition of local governments;
- Provide essential government services in an efficient and effective manner; and
- Improve decision making on the part of the Legislature, state agencies and local government officials on matters relating to local government.

The scope and objectives of this audit included System components as defined in Section 11.45(2)(h), Florida Statutes, related to:

- The local government auditor selection procedures provided in Section 218.391, Florida Statutes, and
- Follow-up on finding Nos. 9 through 14 included in our report No. 2006-186.

METHODOLOGY

The methodology used to develop the findings in this report included the examination of pertinent State and local government records, inquiry of State and local government personnel, and observation of procedures in practice. This audit was conducted in accordance

with applicable Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the audit to obtain sufficient appropriate evidence to provide a reasonable basis for our findings and recommendations based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and recommendations based on our audit objectives.

AUTHORITY

Pursuant to the provisions of Section 11.45(2)(h), Florida Statutes, I have directed that this report be prepared to present the results of our performance audit of the local government financial reporting system.



David W. Martin, CPA
Auditor General

MANAGEMENT RESPONSES

Responses to our findings from the Department of Financial Services, the Department of Management Services, and the Executive Office of the Governor are included in this report as Appendix D.

This audit was coordinated by Anita Marlowe, CPA, and supervised by Michael J. Gomez, CPA. Please address inquiries regarding this report to Marilyn D. Rosetti, CPA, Audit Manager, via e-mail at marilynrosetti@aud.state.fl.us or by telephone at (850) 487-9031.

This report and other audit reports prepared by the Auditor General can be obtained on our Web site (<http://www.myflorida.com/audgen>); by telephone (850 487-9024); or by mail (G74 Claude Pepper Building, 111 West Madison Street, Tallahassee, Florida 32399-1450).

APPENDIX A
REVIEW OF AUDIT COMMITTEE RESPONSIBILITIES FOR SELECTED LOCAL GOVERNMENTS

Non-mandatory Guidance Auditor Selection Task Force Guidelines Recommended Audit Committee Responsibilities	Audit Committees That Did Not Include Responsibility	
	Number (Out of 32)	Percent
Audit committee should have access to the services of at least one financial expert	1	3.1
Members of the audit committee should be members of the governing body	3	9.4
Audit committee members should be persons other than those who exercise managerial responsibilities that fall within the scope of the audit	16	50.0
Audit committee members should be provided with training	9	28.1
Audit committee should be formally established by charter, resolution, or other appropriate means	0	0
Composition and size of audit committee should be established	5	15.6
Responsibilities of audit committee should be established	12	37.5
Audit committee should monitor the audit	23	71.9
Audit committee should review the financial statements prior to completion of the audit	24	75
Audit committee should review the results of the audit	22	68.8
Audit committee should evaluate management’s proposed corrective action plan	23	71.9
Audit committee should monitor corrective action taken	23	71.9
Audit committee should evaluate auditor performance	23	71.9

APPENDIX B
REVIEW OF REQUESTS FOR PROPOSALS FOR SELECTED GOVERNMENTS

Non-mandatory Guidance Auditor Selection Task Force Guidelines Key Elements to Consider	RFPs That Did Not Include Element	
	Number (Out of 32)	Percent
How proposals will be evaluated	4	12.5
Procedures to be followed in the proposal process	5	15.6
Brief description of the government and its accounting systems and financial reporting structures	16	50.0
Known weaknesses in the government’s internal control structure	31	96.9
Anticipated implementation problems arising from new authoritative pronouncements	31	96.9
Principal contacts inside and outside the government	13	40.6
Level of assurance to be required of the auditor for each type of information contained within the report	18	56.3
Auditing standards required for the engagement	11	34.4
The auditor’s specific reporting responsibilities	12	37.5
The type and amount of assistance available from the government	20	62.5
Required audit timetable and deliverables	18	56.3
Additional services to be required of the auditor	21	65.6
Information on auditor workspace and access to telephones, copiers, FAX machines, and computers	24	75.0
Procedures to be followed to determine if additional audit work is necessary and the fee basis applicable to such work	22	68.8
Information needed from proposers to evaluate their qualifications	4	12.5
Requirement for auditors to furnish a statement that they meet the appropriate criteria for independence	17	53.1
Request for references from other government clients	5	15.6
Request for information on the results of peer reviews	19	59.4
Request for information on the status of any disciplinary actions undertaken against the firm	19	59.4

APPENDIX B (CONTINUED)
REVIEW OF REQUESTS FOR PROPOSALS FOR SELECTED GOVERNMENTS

Non-mandatory Guidance Auditor Selection Task Force Guidelines Key Elements to Consider	RFPs That Did Not Include Element	
	Number (Out of 32)	Percent
Request for detailed information on the proposer’s anticipated audit approach	18	56.3
Requirements applicable to working papers and cooperation with other auditors	21	65.6
Policy toward joint proposals or the use of subcontracting	20	62.5
Right to reject proposals, demand additional information, and use unsuccessful proposals	10	31.3
Any additional language to meet the requirements of applicable laws and regulations	11	34.4

APPENDIX C
REVIEW OF AUDIT SERVICES CONTRACTS FOR SELECTED LOCAL GOVERNMENTS

Non-mandatory Guidance Auditor Selection Task Force Guidelines Recommended Key Elements	Contracts That Did Not Include Element	
	Number (Out of 61)	Percent
An independence assertion by the auditor	51	83.6
Language describing the actions to be taken in the event of a disagreement as to whether certain procedures are within the scope of the agreement	44	72.1
Legal provisions to assure the availability of the auditor’s services to aid the government in the defense of claims that may arise as the result of audit work	52	85.2
Clarification of the auditor’s duty to maintain the confidentiality of certain sensitive information	29	47.5
Provisions establishing the government’s right to terminate the contract and the procedures for doing so	44	72.1
Language establishing the auditor’s sole liability for claims arising from the auditor’s performance of the engagement	57	93.4
Language requiring both the government and the auditor to resolve disputes amicably	51	83.6
Requirement for formal notification to the other party to the agreement if a disagreement arises and language indicating what is to be considered notification in such instance	52	85.2
Language specifying how the terms of the contract can be waived or modified	52	85.2
Language to clarify that the contract’s separate provisions are to stand alone, so that a failure to meet one provision does not nullify the entire contract	56	91.8
A requirement for the auditor to obtain insurance coverage	55	90.2
A prohibition against the auditor’s delegating or subcontracting audit work without the government’s permission	53	86.9
Stipulation as to how the value of the auditor’s work is to be determined if the engagement is terminated prior to completion	40	65.6

APPENDIX D
MANAGEMENT RESPONSES – DEPARTMENT OF FINANCIAL SERVICES



CHIEF FINANCIAL OFFICER
STATE OF FLORIDA

ALEX SINK

September 22, 2008

Mr. David W. Martin
Auditor General
State of Florida
Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450

Dear Mr. Martin:

Pursuant to Section 11.45(4) (d), Florida Statutes, the enclosed response is provided for the preliminary and tentative audit findings included in the Auditor General's Performance Audit of the Local Government Financial Reporting System.

If you have any questions or would like to discuss the matter further, please contact Bob Clift, Inspector General, at (850) 413-4960.

Sincerely,

A handwritten signature in black ink that reads "Alex Sink".

Alex Sink

AS:Cc

Enclosures

APPENDIX D (CONTINUED)
MANAGEMENT RESPONSES – DEPARTMENT OF FINANCIAL SERVICES

Florida Department of Financial Services
Performance Audit
Local Government Financial Reporting System
Preliminary and Tentative Audit Findings

Finding No. 5: Although greatly improved, some local governments continued to file paper-based annual financial reports with the Department of Financial Services (DFS) rather than file electronically.

Recommendation: To ensure continued success in the electronic filings of AFRs, and ultimately eliminate paper-based AFRs, we recommend that DFS formally require the electronic filing of AFRs through LOGER.

Response: The Department concurs. The Bureau of Local Government has rule-making authority over the AFR submission process and is presently considering mandating electronic submission of the report. The Bureau will contact as many governments as possible that submitted the report manually (paper-based) to ascertain any valid reason(s) that make electronic submission impossible at the close of the 2007 fiscal year reporting cycle.

Finding No. 6: DFS's required notification to the Legislative Auditing Committee of unaudited local governments that had not submitted an annual financial report for the 2005-06 fiscal year did not include 12 special districts.

Recommendation: DFS should ensure that all known entities that fail to provide the required AFR are included in its notifications to LAC, including independent special districts that were reported on the AFR of the governing authority wherein they are located.

Response: The Department concurs. The reporting environment within the LOGER system has been programmed to create the Noncompliant Report directly from the database which houses all submitted data. All independent local governments, including special districts, that are not compliant with submitting an AFR by the deadline pursuant to Section 218.32, Florida Statutes, will be included on all subsequent reports to the JLAC. The Department of Community Affairs (DCA) Special District Information Program's maintains a database of all special districts. The Bureau has implemented a policy to analyze the DCA database on a monthly basis to ensure all special districts are tracked in LOGER.

Finding No. 7: Although greatly improved due to the implementation of the Local Government Electronic Reporting System, some unaudited local governments were still not reporting the required financial information on their annual financial reports to DFS.

Recommendation: DFS should continue its technical assistance to smaller local governments to assist them with proper completion and filing of the AFR.

APPENDIX D (CONTINUED)
MANAGEMENT RESPONSES – DEPARTMENT OF FINANCIAL SERVICES

Response: The Department concurs. The Bureau will continue to assist smaller local governments with the AFR reporting requirement through as many means as possible. The Bureau will provide direct assistance via e-mail, phone and fax, as well as using a ListServ mass e-mailing system that allows the Bureau to offer technical assistance to many local governments, large and small alike. The Bureau will continue to seek speaking engagements for local governments' conferences.

APPENDIX D (CONTINUED)
MANAGEMENT RESPONSES – DEPARTMENT OF MANAGEMENT SERVICES



Governor Charlie Crist

Office of the Secretary
4050 Esplanade Way
Tallahassee, Florida 32399-0950
Tel: 850.488.2786
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Secretary Linda H. South

September 18, 2008

Mr. David W. Martin, CPA
Auditor General
G74 Claude Pepper Building
111 West Madison Street
Tallahassee, Florida 32399-1450

Dear Mr. Martin:

Pursuant to Section 11.45(4)(d), Florida Statutes, I am responding to the preliminary and tentative audit findings and recommendations pertaining to the Department of Management Services in your performance audit of the *Local Government Financial Reporting System*. We concur with your findings and recommendations regarding Division of Retirement operations related to local government pension plans. As communicated to your staff, the Division has formulated an Action Plan to address similar issues and recommendations made by my Inspector General in his *Advisory Report on Oversight of Local Government Pension Plans* published May 16, 2008. A copy of this report was provided to your staff.

The attached response corresponds with the specific findings and recommendations contained in your preliminary and tentative report.

If you need further information concerning our response, please contact Steve Rumph, Inspector General, at 488-5285.

Sincerely,

A handwritten signature in blue ink, appearing to read 'L. South', is written over a light blue horizontal line.

Linda H. South
Secretary

Attachment

cc: David Faulkenberry, Deputy Secretary
Sarabeth Snuggs, Director, Division of Retirement

We serve those who serve Florida.

APPENDIX D (CONTINUED)
MANAGEMENT RESPONSES – DEPARTMENT OF MANAGEMENT SERVICES

Mr. David W. Martin
September 18, 2008
Attachment, Page 1

ATTACHMENT
Department of Management Services' Response
To the Auditor General's Audit of the
Local Government Financial Reporting System

Finding No. 8: Review of Actuarial Reports and Impact Statements

Department of Management Services, Division of Retirement (DMS), did not always acknowledge the receipt of the local governments' actuarial reports or actuarial impact statements pertaining to public employee retirement systems and plans, contrary to Section 112.63(4), Florida Statutes. Furthermore, DMS did not prioritize its backlog of actuarial reports and impact statements pending review to ensure that the reviews were performed in a timely manner.

Recommendation:

DMS should ensure that all local governments are notified in a timely manner that DMS has received their actuarial reports and impact statements. Additionally, DMS should take appropriate action to ensure that reviews are performed in a timely manner, and that the written procedures established for the review of actuarial reports and impact statements are followed, including prioritizing its backlog based on the triennial review schedule provided for in law.

Response:

Concur. Division procedures require the Division to acknowledge receipt of actuarial reports and impact statements. Staff enter into a logbook the date of receipt of each actuarial valuation and/or impact statement and the date the acknowledgement letter was issued. A copy of the acknowledgement letter is placed in the monthly correspondence file. To ensure staff are complying with these procedures, management has instituted the practice of verifying that the acknowledgement letter was issued. Each month, management will review the hard copy file of a sample of approximately 20% of the plans that submitted reports during the past month to verify that the acknowledgement letter was issued.

In response to recommendations by the Department's Office of Inspector General the Division has established a comprehensive action plan to address issues related to prioritizing the review of actuarial reports and adherence to a triennial review schedule. Accordingly, the Division has established a risk-based schedule for accomplishing the triennial review of all local government pension plans. The schedule specifies the order in which plans are to be reviewed with the most overdue plans given the highest priority for review. In addition, the Division has implemented a policy whereby it no longer reviews actuarial valuations older than three years. The Division expects to complete the revision of its written policies and procedures for conducting actuarial reviews by January 1, 2009.

APPENDIX D (CONTINUED)
MANAGEMENT RESPONSES – DEPARTMENT OF MANAGEMENT SERVICES

Mr. David W. Martin
September 18, 2008
Attachment, Page 2

The Division has also obtained additional resources to assist in its review efforts. A budget amendment approved on September 4, 2008 provides additional funding in the current fiscal year for external actuarial services to help reduce the work backlog. The 2008 Legislature authorized a second actuary position to help address the backlog and assist in maintaining a triennial review schedule.

Finding No. 9: Actuarial Report Information Requests

DMS did not include the required response time, or notification of the consequences for failure to provide requested information, in its correspondence with pension plan administrators. Also, DMS did not maintain a system for tracking and timely following up on requests for additional information relating to its review of public employee retirement systems and plans.

Recommendation:

DMS should include the required response time and indicate the consequences for failure to provide the requested information, as provided for in law and rule, in requests to pension plan administrators for additional information. Additionally, DMS should establish a tracking system for its correspondence to ensure timely monitoring and follow-up, and, if necessary, enforce the consequences for failure to provide the required information in a timely manner.

Response:

Concur. The Division is in the process of revising its notification letters. The revised letters will advise plan administrators of the 60-day response requirement and of the consequences for failure to provide requested information. The Division expects to begin issuing the revised letters by October 1, 2008. The Division is in the process of revising procedures for tracking responses from plan administrators. The revised procedures will permit management to readily identify and timely follow-up with plans that have not responded within the 60-day response period. The Division anticipates that the revised tracking procedures will be implemented by January 1, 2009.

APPENDIX D (CONTINUED)
MANAGEMENT RESPONSES – EXECUTIVE OFFICE OF THE GOVERNOR



CHARLIE CRIST
GOVERNOR

STATE OF FLORIDA
Office of the Governor

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September 26, 2008

Mr. David Martin, C.P.A.
Auditor General
111 West Madison Street
G-74 Pepper Building
Tallahassee, FL 32399-1450

RE: Local Government Financial Reporting System

Dear Mr. Martin:

In compliance with Section 11.45(4)(d), Florida Statutes, the Executive Office of the Governor is pleased to provide the following response to your preliminary audit finding and recommendation specific to this office contained in the above referenced report.

Finding on Financial Emergencies: Executive Office of the Governor staff did not, in some instances, timely contact governments that met a financial emergency condition specified in law.

Response: We concur there were some instances that were not timely. We also concur that the law does not provide a time certain for this contact and that the more timely the contact and determination is made, the sooner State assistance could be provided, if required. The delays are attributable to staff vacancies for the following periods: July 2005 to September 2005; January 2007 to March 2007; July 2007 to November 2007; and since July 2008. We successfully removed the backlog that existed and will continue to focus available resources on contacting entities in a timely manner.

This response is being electronically submitted to flaaudgen_audreport@aud.state.fl.us per your instructions. If you have any questions regarding this submission or need additional information, please contact Melinda Miguel, Chief Inspector General, at (850) 922-4637.

Sincerely,

A handwritten signature in black ink, appearing to read "Eric Eikenberg".

Eric Eikenberg
Chief of Staff