



Item No. 5 Town of Atherton

FINANCE COMMITTEE STAFF REPORT

TO: FINANCE COMMITTEE

FROM: ROBERT BARRON III, FINANCE DIRECTOR

DATE: SEPTEMBER 15, 2016

SUBJECT: DISCUSSION OF THE FISCAL YEAR 2015-16 PRELIMINARY AUDIT & SCOPE

RECOMMENDATION

Discuss the Fiscal Year 2015/16 Year Audit with independent auditor regarding the preliminary audit work and scope.

BACKGROUND

Maze and Associates is the Town's independent auditor and is tasked with the audit of the basic financial statements. The Town began its interim audit phase of fiscal year 2015-16 as the Town independent auditor was on site during the week of April 25 – 29. Audit engagement partners Katherine Yuen and Grace Zhang are here to communicate the auditor's responsibilities under generally accepted auditing standards, the planned scope, timing, independence, and process of the audit. The auditor will discuss the preliminary audit and any new governmental accounting standards statements that need to be implemented.

FINDINGS | ANALYSIS

This is a communication of the FY 2015/16 interim audit phase. The final audit field work is scheduled for the week of November 7, 2016. The Auditor will give an update on the required audit planning communications (SAS 114) for the independent audit of the Town.

FISCAL IMPACT

None

ATTACHMENT

Audit Planning Communication-Year End June 30, 2016

TOWN OF ATHERTON
AUDIT PLANNING COMMUNICATIONS AND FRAUD CONSIDERATIONS
For The Year Ended June 30, 2016

Audit standards require us to communicate with our clients the audit process including:

- Auditor's responsibilities under U.S. Generally Accepted Auditing Standards
- Concept of materiality in planning and executing the audit
- Audit scope
- Audit timing
- Management representations
- Fraud considerations

Our Responsibility under U.S. Generally Accepted Auditing Standards

Our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of the audit we will consider the Town of Atherton's internal control. Such considerations are solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

Materiality

Financial Accounting Standards Board Statement of Financial Accounting Concepts No. 2 (CON-2), *Qualitative Characteristics of Accounting Information*, defines materiality as the "magnitude of an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement." In planning and performing the audit, we use professional judgment to determine a level of materiality. Factors considered in this evaluation include the components of the financial statements believed to be the most critical to users and the extent of adjustments detected in prior audits.

Audit Scope

The Town Council approved our contract which incorporates our proposal detailing our audit approach and timing. Audit scope generally includes the following items which are subjected to adaptation as a result of our risk assessment process:

- Perform risk assessment brainstorming and planning
- Create audit plan tailored to the Town and sector.
- Transactions cycles subject to control testing and sampling:
 - Revenue/receivable
 - Disbursements/accounts payable
 - Payroll/accrued liabilities
 - New debt issuance and recorded transactions (if applicable)
 - Federal award transactions (if applicable)
 - Transportation Development Act program transactions (if applicable)
 - Measure A
- Transactions cycles testing:
 - Controls over cash transactions and accruals
 - Test of transactions
 - Tests of information system application controls
 - Confirmations generally not used as they are ineffective.
 - Accrual tests at year end.
- Transactions and balances tested in total:
 - Cash: and investments: tested via bank reconciliation tests and confirmation of bank balances.
 - Capital assets: tested through corroboration with capital outlay and council authorizations on a test basis and estimate of depreciation
 - Compensated balances: tested through estimation
 - Claim payable: tested through claims loss run and actuarial studies if any
- Evaluate overall staff duties/functions assignment including:
 - Focused attention to conflict of duties – employees with access to assets and related recorded used to control and account for those assets
 - Tests of mitigating controls
- Information system controls tests:
 - An information system review is performed by our IT specialist
 - Application controls tested via transaction cycle tests
- Perform compliance tests
 - Single Audit Act (if applicable): Federal regulations applicable to federal awards (Uniform Guidance applicable starting 12/26/14)
 - Measure A
 - Certain Government Code provisions applicable to cash and investments
 - Local policy compliance, typically:
 - Investment
 - Purchasing

- Financial Statement preparation assistance
 - Staff has requested that we provide assistance with the preparation of financial statements and disclosures
 - We are satisfied staff have the capability to perform this task themselves
 - Financial statement presentation and disclosures are evaluated; and amendments are proposed as needed

Audit Timing

We have met with staff and agreed the following schedule:

- Interim audit fieldwork: 1 week in April 2016.
- Final audit fieldwork: 1 week in November 2016.

Management Representations

At the end of the audit, we will request representations from management that data and assertions provided are complete and accurate. We rely primarily on our audit verification tests and procedures. However, management assertions and judgments, without doubt, affect financial data.

Fraud Considerations: Statements on Auditing Standard (SAS) No. 99, *Consideration of Fraud in a Financial Statement Audit*. This Standard was issued due to the collapse of Enron, WorldCom and other private sector frauds.

1. “Fraud” is defined as an intentional act that results in a *material misstatement in financial statements* that are subject to audit. In this case, fraud includes two concepts:
 - a. Fraudulent financial reporting:
 - i. Misstatement including misapplication of accounting principals, omission of data or disclosures, fictitious transactions or sham transactions
 - ii. Concealment
 - b. Misappropriations of assets:
 - i. Theft
 - ii. Concealment
 - iii. Conversion

As part of the audit, we make certain inquiries regarding the risk or knowledge of fraud.

1. Do you have any knowledge of any fraud or suspected fraud? If so, what steps were taken to investigate the incident and what was done to resolve the situation?
2. Are there areas that you believe are “Susceptible to Fraud”? If so, what steps were taken to deter and detect fraud?
3. Are you aware of any allegations of fraud or suspected fraud?
4. Are you aware of any related party transactions?