



Unit Assistance List: Audit

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AGENDA

Budgeting

Cash
Management
&
Investments

Obligating &
Disbursing
Public Funds

Accounting &
Financial
Reporting

Auditing

Financial Reporting

- G.S. 159-34 requires that each local unit produce an annual financial report, which must include its financial statements prepared in accordance with generally accepted accounting principles.
- Preparation of the report's financial statements and their accompanying notes is the responsibility of management.

9) Financial Reporting

- Local units are required to prepare basic financial statements, which include:
 - Management's discussion & analysis
 - Government-wide financial statements
 - **Fund financial statements**
 - Note disclosures

Financial Reporting

- Three broad categories of funds:
 - Governmental (**general fund**, special revenue fund, debt service fund, capital projects fund, and permanent fund).
 - Proprietary (**enterprise fund** and internal service fund).
 - Fiduciary (pension trust fund, investment trust fund, private-purpose trust fund, and agency fund).

Annual Audit

- G.S. 159-34 requires that local units have their accounts audited by an independent auditor after the close of each fiscal year.

Annual Audit

- Audits must be conducted by an independent certified public accountant, chosen by the entity's governing board.
- Best practice states that local units should issue a request for proposal for a new auditor every five years.
- Best practice also suggests that if the same auditing firm is selected, then a new auditor should conduct the local unit's audit.



Annual Audit

- Reports are due to the Local Government Commission no later than October 31st.
- The Local Government Commission does give local units a 30-day grace period beyond this submission deadline.
- Local units that do not submit audited financial statements to the Local Government Commission are placed on the UAL.



Annual Audit

- Purpose of an audit is to ensure that financial statements report the financial position of a local government in accordance with generally accepted accounted principles (GAAP).



Annual Audit

- A local unit receives an unmodified audit opinion when its financial statements follow the purpose of the audit.
- The significance of this opinion does not represent fiscal strength or stress, requiring another step to determine financial condition.



Annual Audit

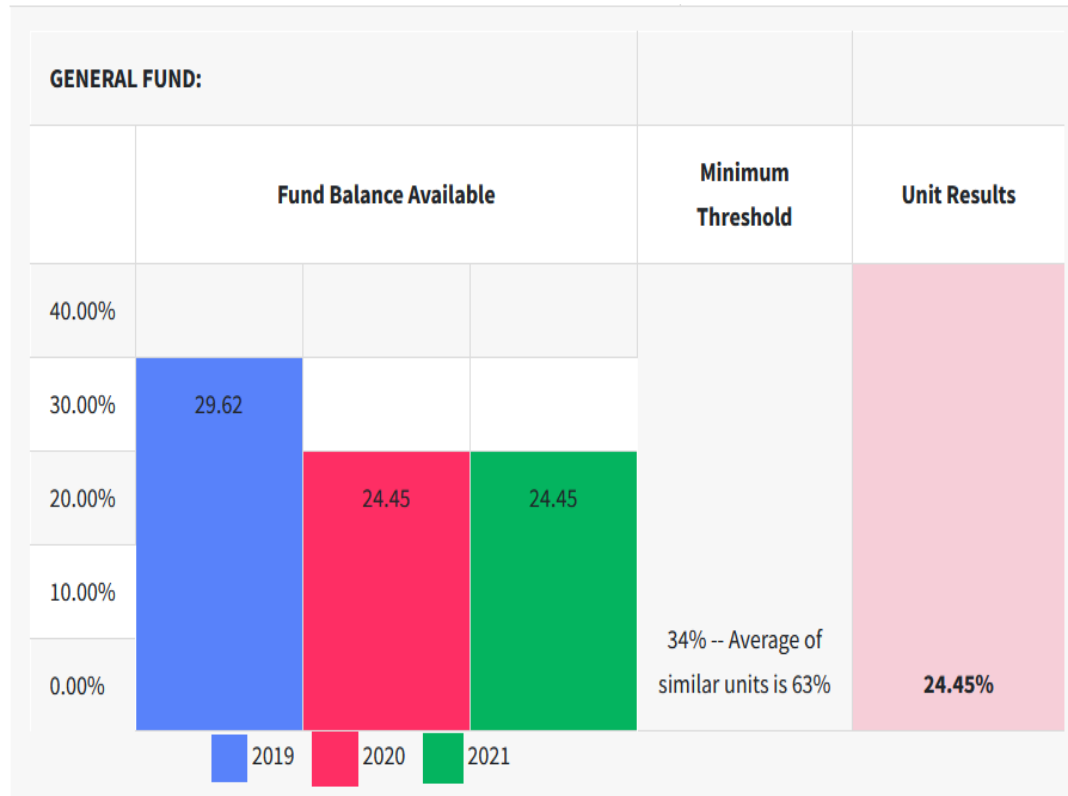
- Auditor is required to make a presentation to the board at a public meeting within 45 days after the audit is completed.
- Auditor's presentation should include:
 - Review of the management letter, including identifying areas of material weaknesses, significant deficiencies, other findings of note, and if applicable, financial performance “indicators of concern.”
 - The unit of government is then expected to develop a response to what the auditor presented, signed by majority of board members, which is submitted to the LGC staff within 60 days of presentation.

Financial Condition

- Financial metrics are used for moving from financial position to financial condition in local government given that an unmodified audit opinion does not represent fiscal strength or stress.
- The Local Government Commission uses selected financial metrics to gauge the financial condition of local units, using the results as the basis for placing local units on the UAL.

Financial Condition

- Fund Balance as Percentage of Expenditures for general fund is calculated by dividing available fund balance by total expenditures plus transfers out.
- The LGC's benchmarking is 50 percent or higher of group average.



Financial Condition

Strategies for Improvement

- Adopt a **fund balance policy** by resolution, which includes the fund balance threshold for annual review.
- Forecast and adopt realistic revenue estimates, maintaining high collection rates.
- Exercise control over expenditures, including the use of the preaudit requirement.
- Use a contingency appropriation, which cannot exceed five percent of the total of all other appropriations in the same fund [G.S. 159-13(b)(3)].

Financial Condition

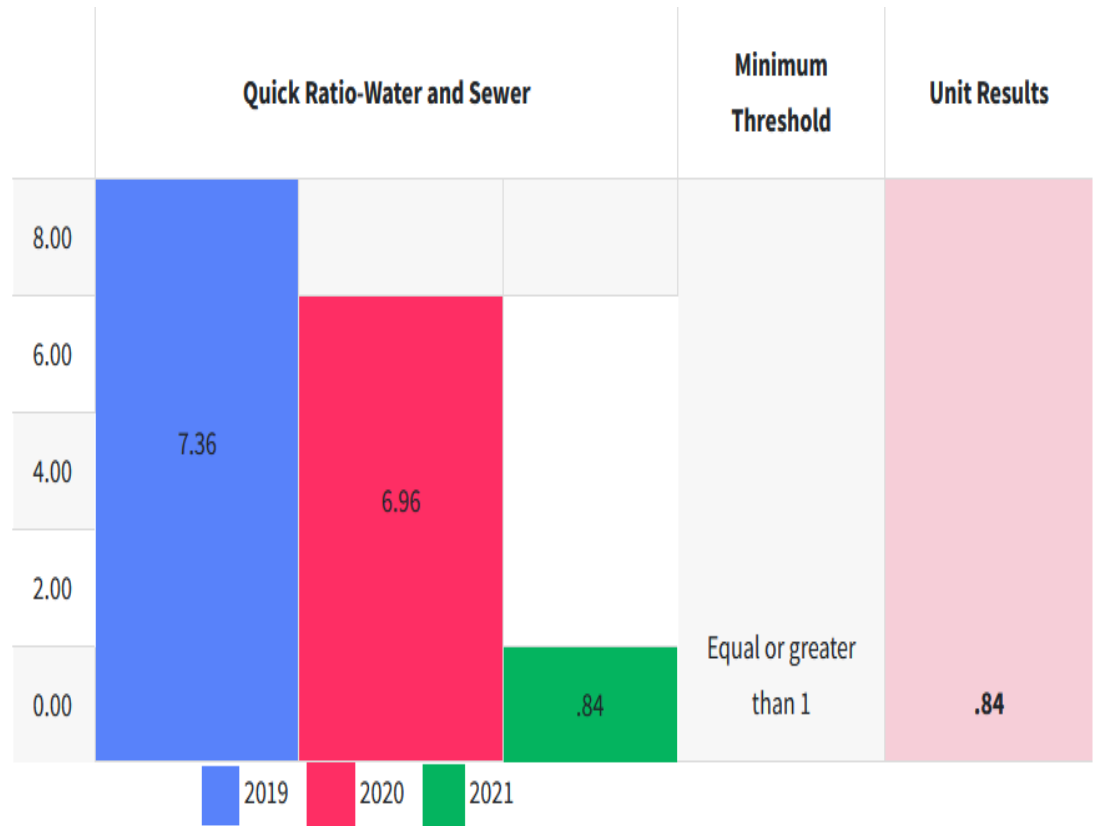
- Total Margin Ratio of the general fund is calculated by dividing total revenue by total expenditures plus transfers to debt service fund.
- The LGC's benchmark is 1.0 or greater.

Financial Condition

- Debt Service Ratio of the general fund is calculated by dividing debt service (principal and interest payments on long-term debt plus transfers to debt service fund) by total expenditures.
- The LGC's benchmark is 12 percent or below.

Financial Condition

- Quick ratio for an enterprise fund is calculated by dividing unrestricted cash plus accounts receivables by the sum of accounts payable, accrued liabilities, and current portion of long-term debt.
- The LGC's benchmark is 1.0 or higher.



Financial Condition

Strategies for Improvement

- Review **rate structure** on an annual basis, adjusting rates when necessary to avoid operating losses.
- Improve cash collections from customers of system.
- Review process for writing off uncollectable accounts.
- Exercise control over operating expenses, including the use of the preaudit requirement.
- Eliminate transfers out in support of other funds.
- Monitor the change in current liabilities over time, including accounts payable.

Financial Condition

- Operating Net Income of an enterprise fund is calculated by subtracting operating expenses (excluding depreciation plus debt service of principal and interest payments) from operating revenues.
- The LGC's benchmark is greater than zero.

Financial Condition

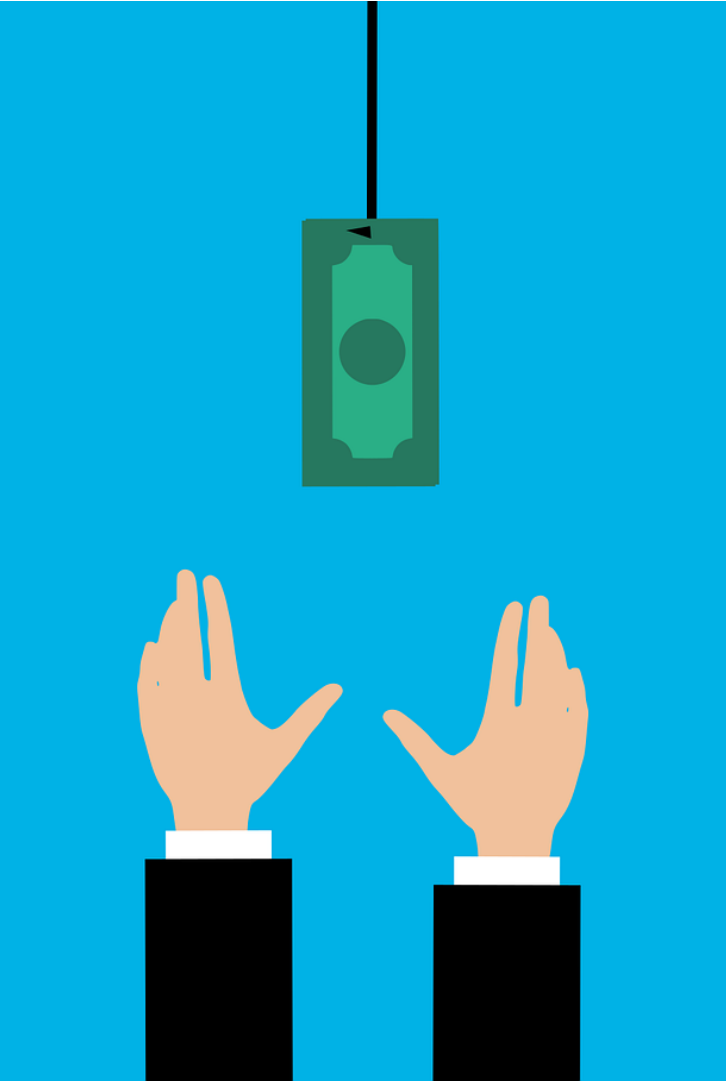
- Unrestricted Cash Ratio of an enterprise fund is calculated by dividing unrestricted cash by total expenses excluding depreciation plus debt service of principal and interest payments.
- The LGC's benchmark is 16 percent or greater (2 months).

Financial Condition

- Benchmarking Tool for North Carolina Counties and Municipalities on the LGC's website.
- <https://logos.nctreasurer.com/Reporting/Report/External?applicationCode=BMT>.

Exercise

- Discuss in groups your process to monitor the financial condition of your respective local unit.



KEY TAKEAWAYS

- Importance of timely audit
- Clean audit does not mean fiscal strength
- Use metrics to explore, understand, and improve financial condition