

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 349

Auditor Selection Procedures

**SPONSOR(S):** Brummer

**TIED BILLS:**

**IDEN./SIM. BILLS:** SB 1072

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| REFERENCE                                   | ACTION          | ANALYST         | STAFF DIRECTOR  |
|---------------------------------------------|-----------------|-----------------|-----------------|
| 1) <u>Governmental Operations Committee</u> | <u>4 Y, 0 N</u> | <u>Brazzell</u> | <u>Everhart</u> |
| 2) <u>Local Government Council</u>          | <u>6 Y, 0 N</u> | <u>Camechis</u> | <u>Hamby</u>    |
| 3) <u>State Administration Council</u>      | <u></u>         | <u>Brazzell</u> | <u>Bussey</u>   |
| 4) <u></u>                                  | <u></u>         | <u></u>         | <u></u>         |
| 5) <u></u>                                  | <u></u>         | <u></u>         | <u></u>         |

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### SUMMARY ANALYSIS

HB 349 revises the requirements governing the selection by counties, municipalities, special districts, district school boards, charter schools, and charter technical centers of auditors to perform the fiscal audit required by s. 218.39(1), F.S. The bill requires the use of audit committees, allows only licensed and qualified firms to provide audits, and amends the processes for selecting and contracting with audit firms.

The bill addresses certain problems with local government auditor selection identified in Auditor General Report No. 2004-006, *State of Florida Local Government Financial Reporting System*.

The fiscal impact on local governments is indeterminate but expected to be minimal.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. HOUSE PRINCIPLES ANALYSIS:

*Provide limited government*—The bill increases the responsibilities of other governmental organizations by providing additional requirements with which certain local governments must comply when selecting auditors, as further described below.

#### B. EFFECT OF PROPOSED CHANGES:

##### Present situation

A local government financial audit provides an independent assessment about the accuracy and completeness of the entity's financial statements. Bond rating services use such audits to rate local governments' bonds, affecting their bond issuance costs. These audits also allow for evaluation of local governments' internal controls and compliance with applicable laws, rules, contractual requirements, and good business practices.<sup>1</sup>

Pursuant to s. 218.391(1), F.S., certain local governments must have an annual financial audit performed by an independent certified public accountant retained by the local government and paid from public funds. The requirements that the local governments follow in selecting their auditors vary by entity type:

- Noncharter counties and school districts must comply with specific requirements as set forth in s. 218.391(3), F.S.
- Charter counties, municipalities, special districts, charter schools, and charter technical centers may choose to follow the requirements in s. 218.391(3), F.S., or may establish auditor selection committees and procedures of their choosing.

Section 218.391(3), F.S., provides for the use of an auditor selection committee (committee), public announcement of the need for auditing services, qualification of certified public accountants and adoption of evaluation procedures by the committee, the process for selection of firms with which to negotiate, and negotiation procedures.

Pursuant to s. 11.45(2)(h), F.S., which requires the Auditor General to conduct a performance audit of the local government financial reporting system at least every two years to determine the accuracy, efficiency, and effectiveness of that system in achieving its goals, the Auditor General issued report no. 2004-006, *State of Florida Local Government Financial Reporting System*. In that report, the Auditor General found that those local government entities they reviewed which did not follow the provisions of s. 218.391(3), F.S.,<sup>2</sup> were often not carrying out best practices.<sup>3</sup> For example, the Auditor General found:

- Over half of the 81 entities reviewed that needed to procure an audit firm did not use a competitive selection process to select their auditor for the 1999-2000 fiscal year audit;
- High percentages of those entities that did not use competitive selection processes did not document consideration of key evaluation criteria in selecting their audit firm such as past performance of the firm, workload, and availability of professional personnel;

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<sup>1</sup> Auditor General Report No. 2004-006, *State of Florida Local Government Financial Reporting System*, July 2003, pg. 4.

<sup>2</sup> Entities that did not follow the provisions of s. 218.391(3) comprised 90% of the entities reviewed.

<sup>3</sup> According to Auditor General Report No. 2004-006 (pp.4-5), sources of best practices include the National Intergovernmental Audit Forum's *How to Avoid a Substandard Audit: Suggestions for Procuring an Audit* and the Government Finance Officers Association's *Audit Management Handbook*.

- 24% of the entities that used a competitive selection process and from which evaluation criteria were available used fees as the sole or most heavily weighted factor in selection; and
- 61% of entities reviewed did not include payment terms in their written agreements with auditors.

The report listed several recommendations for legislative action to address these areas of concern, including:

- Requiring local governments to establish written auditor selection procedures and establish limits on how long an auditor could be retained without re-procuring that service using a competitive selection process;
- Requiring local governments to establish and use audit committees and to specify their membership;
- Requiring the use of requests for proposals containing certain provisions;
- Clarifying the extent to which local governments should consider audit fees during the auditor selection process; and
- Requiring written agreements containing certain provisions between local governments and auditors.

The Auditor General convened the Auditor Selection Task Force to assist in evaluating the various methods used by entities subject to s. 218.39, F.S., and make recommendations to the Legislature as appropriate. This task force included representatives from the Florida Association of Counties, Florida Association of Court Clerks and Controller, Florida Association of Special Districts, Florida Association of Public Purchasing Officers, Florida Government Finance Officers Association, Florida League of Cities, Florida School Finance Officers Association, Florida Institute of Certified Public Accountants, charter schools, and the Joint Legislative Auditing Committee. This task force met in Fall 2003 and Summer 2004 and drafted consensus language to implement some of these recommendations.

#### Proposed changes

HB 349 contains revisions proposed by the Auditor Selection Task Force. Accordingly, the bill:

- Creates a uniform set of auditor selection requirements which must be used by charter counties, noncharter counties, municipalities, special districts, district school boards, charter schools, and charter technical career centers, except that noncharter counties have additional audit committee membership requirements;
- Requires that firms be licensed under chapter 473, F.S., and qualified to conduct audits in accordance with government auditing standards as adopted by the Florida Board of Accountancy;
- Requires the use of audit committees and provides that audit committees can serve other audit oversight purposes;
- Requires the use of a request for proposal solicitation which must, at a minimum, contain certain information;
- Provides that compensation may not be the sole or predominant factor in evaluating proposals;
- Provides a new process for ranking of respondents and conducting negotiations;
- Requires a written contract including specific provisions;
- Removes the requirement for the completion of truth-in-negotiations certificates for contracts over \$50,000; and
- Allows a governing body to allow a designee to conduct negotiations on the body's behalf.

#### C. SECTION DIRECTORY:

Section 1 amends s. 218.391, F.S., to revise the auditor selection procedures used by counties, municipalities, district school boards, charter schools, and charter technical career centers.

Section 2 provides an effective date of July 1, 2005.

## **II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT**

### **A. FISCAL IMPACT ON STATE GOVERNMENT:**

1. Revenues: None.
2. Expenditures: None.

### **B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

1. Revenues: None.
2. Expenditures: Indeterminate but expected to be minimal. Local governments may continue to consider price in selecting auditors, which may mitigate against sharp price increases. Also, local governments which have not been using competitive selection procedures may experience lower audit costs due to greater competition among potential audit providers. Local governments which have used very simple auditor selection processes may experience higher administrative costs from using the new procedures; however, the impact is still expected to be minimal.

### **C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR: Indeterminate but expected to be minimal.** Some local government entities' processes may become more detailed and competitive. Thus, some certified public accountant firms which compete to be awarded local government financial auditing work may have increased expenditures in complying with the selection process. However, local governments are able to retain the same auditor for extended periods, and thus the selection process may not occur annually. Thus marginal changes are expected to be minimal.

### **D. FISCAL COMMENTS: None.**

## **III. COMMENTS**

### **A. CONSTITUTIONAL ISSUES:**

1. Applicability of Municipality/County Mandates Provision: None.
2. Other: None.

### **B. RULE-MAKING AUTHORITY: None.**

### **C. DRAFTING ISSUES OR OTHER COMMENTS: None.**

## **IV. AMENDMENTS/COMMITTEE SUBSTITUTE & COMBINED BILL CHANGES**

None.