Fiscal Impact Analysis: Proposed revisions by the Local Government Commission to Audit Contract and Audit Billings Rules and Proposed New Rule for Submission of Responses by Local Units

Agency:	Local Government Commission
Rule Citation(s):	20 NCAC 03 .0502 Audit Contract 20 NCAC 03 .0505 Audit Billings 20 NCAC 03 .0508 Response to the Independent Auditor's Findings, Recommendations, and Fiscal Matters (See **Appendix A** for proposed rule text)
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Rulemaking Authority:	N.C.G.S. §§ 159-3(f), 159-34
Impact Summary:	State Government: Yes Local Government: Yes Private Entities: Yes Substantial Impact: No

Introduction and Purpose

As part of its statutory responsibilities under N.C.G.S. Chapter 159, the Local Government Commission (the "Commission" or the "LGC"), operating as a division of the Department of State Treasurer through the State and Local Government Finance Division, engages in centralized financial oversight of approximately 1,300 North Carolina local governments and public authorities ("Units"). The LGC's duties include promulgating best financial management practices, reviewing Units' annual audit reports, monitoring Units' fiscal health, and counseling Units on sound fiscal management and internal controls. Units are required under N.C.G.S. § 159-34(a) to annually submit one or more of the following to the Secretary of the LGC (the "Secretary"):

- the contract to audit the accounts of the Unit, for the Secretary's approval,
- the audit report, and
- the bills and claims for audit fees, for the Secretary's approval prior to payment.

The LGC is proposing to revise and adopt rules updating:

- the requirements related to the submission and presentation of audit reports to local governments and public authorities,
- the submission and approval of audit invoices, and
- the process for Units that are required to provide responses and corrective action plans to the Commission as a result of audit findings and financial indicators of concern,

with the goal of conforming to industry best practices and/or current business processes and improving financial transparency.

Implementation of the proposed rule changes will promote conformity to best practices and improve financial transparency by ensuring that auditors will present findings and fiscal issues identified in an annual audit report to Units and the public and by ensuring that all Units receive relevant information in a consistent manner through the auditor's presentation, regardless of the auditor employed. Additionally, the proposed rule changes streamline and simplify both the audit contract and audit fee business processes and the responsibilities of the LGC.

Description of Proposed Rules and Impact Analysis

Each proposed rule change and new rule is listed on the following pages, along with background and benefits to each proposed change.

<u>Rule: 20 NCAC 03 .0502 Audit Contracts</u>

Intent: Ensure that Units and the public will be presented with findings and financial issues identified in an annual audit report.

Rule Section: New subsection (c)(6)

Addition/Modification: Addition to existing rule

Background: Current subsection (c)(4) of this rule requires the auditor to "submit" a report of the audit to the Unit's governing body, however, there is currently no statute or rule that requires the report be "presented" to the governing body. Presentation of an audit report to a Unit's governing body in an official meeting in open session ensures that all members of the governing body are aware of the results of the audit and have the opportunity to ask questions of the auditor as needed. It also gives the public the opportunity to hear that same presentation, any questions asked, and the answers provided, improving the transparency of the process. Presentation of a completed audit to the governing body is an industry best practice.

Proposed Change: The new subsection section (c)(6) would require auditors to present audit findings, including "Financial Performance Indicators of Concern," to a Unit's governing body or audit committee in an official meeting in open session and to notify the Unit of the requirement to provide a response to the Secretary of the findings and Indicators of concern if required under proposed new rule 20 NCAC 03 .0508.

Benefit: This rule would enforce an industry best practice, ensure the presentation of relevant information in a consistent manner regardless of the auditor employed, and provide Units and the general public with more transparency concerning the audit results, as well as the meaning of those results. The Rule would ensure that the governing board members are made aware of any fiscal matters needing corrective action.

Impact: Auditors that do not currently present their findings to Units' governing bodies would be required to do so. As a result of this new requirement, potential financial impacts to the Units may include additional charges for an auditor's time and travel in attending the meeting and making the presentation. However, because this requirement is an industry best practice and is already being followed by most auditors, the number of auditors impacted by this change is believed to be minimal. Additionally, impacted Units could arrange for auditors to conduct virtual presentations, reducing the cost of time and travel.

Rule: 20 NCAC 03 .0502 Audit Contract

Intent: Require that certain data included in the audit is submitted to the Secretary.

Rule Section: New subsections (c)(3) and (e)

Addition/Modification: Addition to existing rule

Background: The data presented in audit reports provide valuable information in supporting the LGC's responsibility to monitor the fiscal health of units and also provide the basis for reports and analysis used by Units, the general public, policy makers, and others. However, because audit reports are presented in a format not conducive to extracting data, the staff of the LGC currently asks that all audit reports submitted to the Secretary be accompanied by a worksheet with data from the report. LGC staff provides a template worksheet for this purpose into which the requested data from the audit can be reported. The completion and submission of this worksheet is a current business practice that has been complied with for the last nine years.

Proposed Change: The addition of new subsections (c)(3) would formally require that data from the audit reports be submitted to the Secretary and authorizes the Secretary to identify Financial Performance Indictors ("Indicators") derived from the data submitted and to set benchmarks for those Indicators. Failure to meet a given benchmark is then noted as an item of concern (Financial Performance Indicators of Concern) respecting a Unit's financial health. New subsection (e) explains and defines the factors considered in establishing the Indicators and how assessing and monitoring the Indicators ties back to the duty of the LGC to advise and assist Units with sound fiscal management and address areas of concern.

Benefit: This rule would ensure that valuable data from audit reports are made available as part of the presentation of the audit to the governing body. It also ensures the data are available in a format that can be extracted and utilized by the LGC to identify financial concerns in Units, and to provide valuable data via reports and analysis used by the LGC, Units, the general public, policy makers, and others.

Impact: These changes would create an enforceable rule for a current business practice that is complied with by all impacted parties. Therefore, no additional financial impact is expected.

Rule: 20 NCAC 03 .0508 Response to the Independent Auditor's Findings, Recommendations, and Fiscal Matters

Intent: Require that Units whose annual audit reports include certain findings or Indicators of concern develop and adopt a response and submit the response to the Secretary.

Section: New Rule

Addition/Modification: New rule

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Background: LGC staff reviews nearly 1,300 annual reports and identifies those Units whose audits contain internal control findings or financial issues of concern. LGC staff issue letters to those Units ("Unit Letters") requesting a response to the findings identified in the audit and requests the Unit to present a corrective action plan addressing the findings and issues identified. The identification of finding(s) and issue(s), and the Units' responses, are an integral component of the LGC's efforts:

- to monitor the fiscal health of Units (N.C.G.S. § 159-181(c),
- to provide guidance and support as needed to ensure Units' continued fiscal health (N.C.G.S. § 159-181(c)), and
- to further the General Assembly's intent to "prescribe for local governments a uniform system of…fiscal control" (N.C.G.S. § 159-7(c)).

Proposed Change: This new rule would require that the Unit initiate a response to the findings and provide a detailed corrective action plan based on the findings and Indicators of concern presented by the auditor in a public meeting in open session. This requirement would replace the current process in which LGC staff must identify findings and financial issues, issue Unit Letters, and request a response from the Unit.

Benefit: In the current process, LGC staff must review each audit report to determine if findings or financial issues were identified, then generate and mail a Unit Letter to the unit and the auditor identifying the issue(s) and requesting a response from the Unit with detailed corrective action. Due to the high volume of audit reports received, it may take the LGC staff 30 to 90 days from receipt of an audit report to review the audit report, provide a second review for accuracy, and send a Unit Letter requesting corrective action. The Unit must then respond to the Unit Letter within 45 days of its receipt. This current process leads to significant delays in LGC staff being notified of corrective actions planned or taken by Units to address findings and financial issues. The new process will eliminate the delay in identifying and notifying Units with internal control findings and financial issues of concern and will eliminate the time and expense of LGC staff to generate and mail Unit Letters, with no additional burden being placed on most Units. The elimination of this delay provides significant benefit to the Units and the public because Units' plans to correct any internal control and financial issues will be known to the LGC more quickly and appropriate action can be taken to support and monitor Units' fiscal health and monitor the corrective actions required to address the identified findings and issues. Although a slight decline in the submission of responses may be anticipated as the transition is made from the current business process to a Unit-initiated response, no long-term impact on the rate of response by impacted Units is expected.

Impact: The business process of generating and mailing Unit Letters to Units and requiring a response has been in place for over 30 years. This new rule would permit a more streamlined process by requiring that a Unit's response to findings or financial issues in an audit be initiated by the Unit (upon notification by the auditor in the auditor's presentation) instead of by request of the LGC.

The rule would primarily impact the same types of Units currently impacted by the current business practice – those Units whose audits identified specific findings or financial issues (and therefore received a Unit Letter). Current auditing standards already require Units that have audits conducted in accordance with Government Auditing Standards (commonly known as Yellow Book standards) to submit a response and corrective action plan to the auditor that addresses any findings noted in the audit by the auditor. In Fiscal Year 2018, 921 of 1303 units (71%) were subject to either a Single Audit or Yellow Book standards audit, which would require Units to respond to the auditor regarding any findings. An additional 97 units (7%) were not subject to either of these audits but received a Unit Letter based on the required financial audit, which would require Units to respond to the LGC regarding the findings or financial issues. These Units would see minimal impact on the time required to submit a response to the LGC, since they are already required to develop a response to the findings or financial issues for submission to either their auditor or the LGC.

Under the proposed rule, some Units may be required to submit a response to the LGC when the current business process wouldn't have required them to do so. This situation would occur when a Unit has a finding, but the Unit is not subject to Yellow Book or single audit requirements (and therefore not required to provide a response to the auditor regarding the findings) <u>and</u> the issue in the finding is known to LGC staff who has determined that a special circumstance exists for not requesting a response for that finding. For example, if a Unit does not have the financial resources to resolve an issue identified in the finding but actively takes steps to mitigate the risk or address the issue and the LGC is aware of the situation, a Unit Letter may not be requested. In Fiscal Year 2018, 285 Units were not subject to Yellow Book or single audit requirements and did not receive a Unit Letter. This number is the absolute maximum impact this rule could have and also includes Units that did not receive a letter simply because they did not have findings or financial issues identified. The actual estimated impact of this rule, based on extensive staff experience, is estimated to be approximately 150 Units (in 2018, that would equate to 12% of audits) and approximately 300 hours of Units' staff time. It is important to note that in these cases, the acknowledgement of the finding and a response including the process(es) implemented to mitigate the risk or address the issue would provide an added measure of accountability and transparency for the Unit and would allow LGC staff to ensure that Units are actively addressing areas of risk and/or concern.

This new rule would reduce state employees' staff time (LGC staff) in drafting the Unit Letters and mailing them to the Units, allowing staff to focus on other important work. In Fiscal Year 2018, LGC staff prepared and mailed 325 Unit Letters. Based on the estimated professional staff time required to develop and review each letter, plus the administrative time required to prepare and mail each letter, it is estimated that eliminating the issuance of these letters would result in annual savings of 730 staff hours ($28,062). In addition, in most instances it would not significantly impact Units' staff time in preparing responses to the audit findings for the LGC because the unit can utilize the response or corrective action plan provided to the auditor when preparing the response for the LGC. Further, the requirements of N.C.G.S. § 159-25(a)(1) to "keep the accounts of the local government or public authority in accordance with generally accepted principles of governmental accounting and the rules and regulations of the Commission" aligns with the requirement for a Unit response.

Rule: 20 NCAC 03 .0502 Audit Contract

Intent: Update the requirements for the audit engagement fee format to better correspond to auditors' current billing practices.

Rule Section: (c)(5)

Addition/Modification: Modification

Background: N.C.G.S. § 159-34(a) requires that all bills or claims for audit fees be submitted to the Secretary for approval. As auditing requirements have grown increasingly complex, auditors' fees and billing structures for annual audits have evolved to better represent the services provided. The current rule allows only that the "fee may be stated as a fixed dollar amount or as a rate per hour or day, either with or without a maximum." This structure does not allow for more complex fee structures as would be required in certain audit engagements. Auditors currently submit audit fees for approval by the Secretary that do not fall into the parameters provided for in this rule because of the limitations of the rule.

Proposed Change: Modifying the current rule from "fee may be stated as a fixed dollar amount or as a rate per hour or day, either with our without a maximum" to "all audit engagement fees and terms shall be clearly stated and shall allow for the computation of a final fee" allows for more complex fee structures, if necessary, while having no impact on other fees, and aligns the requirement of this rule with the obligations of the Secretary for approval of fees under N.C.G.S. § 159-34 and 20 NCAC 03 .0505 Audit Billings.

Benefit: This rule change would provide auditors with flexibility in presenting their fees for audit engagements to better reflect current billing practices and would reduce or eliminate LGC staff time in determining whether submitted fee invoices comply with the current rule. Any fiscal impact is measured in the time saved by state employee staff of the LGC in reviewing and approving audit billings.

Impact: This change would simply create an enforceable rule for a current business practice. Auditors who currently submit fees that comply with the current rule would still fall under the requirements of the new rule; auditors who currently submit fees that accurately represent services provided but do not comply with the limitations of the current rule will benefit from the new rule's flexibility.

Rule: 20 NCAC 03 .0505 Audit Billings

Intent: Simplify the approval of interim billings.

Sections: (b), (c)

Addition/Modification: Modification

Background: As auditing requirements have grown increasingly complex, auditors' fees and billing structures for annual audits have evolved to better represent the services provided. The current rule allows interim billings (those submitted prior to the completion of the audit) to be approved "up to a maximum of 75 percent of a fixed or maximum fee, or in the case where there is no fixed or maximum fee, up to a maximum of 75 percent of last year's billings". This fee structure is outdated and is addressed in a proposed change to 20 NCAC 03 .0502 (c)(5) Audit Contracts. Additionally, the growing complexity of audit fees makes it increasingly difficult for LGC staff to determine if an engagement fee is fixed or variable – e.g. there are often variable components to an otherwise fixed-fee contract. The determination of fixed vs variable may require analysis and in-depth knowledge of auditing services and fees beyond the scope of LGC staff and may result in auditors disagreeing with LGC staff determinations.

Proposed Change: Remove the distinction between fixed and variable fee contracts for the purposes of approving interim billings. All interim audit billings would be approved to a maximum of 75 percent of the billings for the last annual audit submitted, provided the billings meet the other requirements of the rule.

Benefit: LGC staff would save significant time in making determinations of fixed vs variable fee contracts, and disagreements and the resultant communications between LGC staff and auditors regarding the type of contract would be eliminated. It is estimated that staff could reduce by half the amount of time required to review each contract and make a determination of the fee structure, resulting in estimated annual savings of 302 staff hours ($6,980). Additionally, this rule change would likely increase compliance with the requirement for auditors to submit all audit billings to the Secretary for approval. Under N.C.G.S. § 159-34(a), all billings must be submitted to the Secretary for approval prior to payment by the Unit. Experience shows that although most auditors comply with this requirement, there will be a compliance benefit with regards to those auditors who submit invoices to the Units without first obtaining LGC approval. For example, an audit contract may have a stated fixed fee of $10,000 but LGC staff receives invoices totaling only $6,000 in audit fees to approve, meaning that $4,000 in invoices were likely not submitted for approval. If the approval of interim invoices for the current audit is based on 75% of audit fees received for the previous audit submitted, an auditor who does not submit invoices for approval in one year will be allowed a smaller interim approval cap the following year. In this example, the auditor would be approved for interim invoices of 75% of $6,000 vs 75% of $10,000. Note that all of these limitations apply to interim invoices only; this process benefits auditors by allowing them to receive payment for their services performed to date (up to 75%) prior to submission of the audit report.

Impact: This change could impact auditors who submit fixed-fee contracts. Under the current rule, they would be approved for interim invoices up to 75% of the current year's audit fee vs the proposed 75% of prior year's audit fees. If the fixed fee increases significantly from one year to the next, the 75% would be based on the prior year's fee vs the current year's fee, resulting in a slight reduction in the maximum of interim invoices that may be approved (impact would be 75% of the difference between the current year fee and the prior year fee). In most cases, this amount would be minimal and if it not, existing text of this rule gives the Secretary the authority to approve a higher amount if it would be more equitable.

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Summary

The North Carolina Local Government Commission was created in 1931, by North Carolina General Statutes Chapter 159, to address issues in local government finance that arose during the Great Depression. In the 80+ years since, the LGC has provided consistent financial oversight for over 1,300 units of local government, resulting in significant benefits to taxpayers, policymakers, and our communities.

If situations arise of extreme financial mismanagement, the LGC has enforcement authority, under the conditions set forth in N.C.G.S. § 159-181, to impound the books and records of any Unit and to assume full control of all its financial affairs. This enforcement authority is a costly and time-consuming drastic step that has rarely been taken in the past eight decades.

The resources of the LGC and the Units it oversees are more efficiently and effectively used when Units follow sound fiscal management practices and correct problems before they become severe enough to warrant the LGC assuming control of a Unit's financial affairs. The proposed new rule and rule changes would assist in that oversight, ensure that Units follow sound financial management practices, and streamline current business processes saving LGC staff time by:

- requiring auditors to present audit findings and financial issues to Units' governing bodies, which ensures Units' fiscal health problems are brought to the attention of the Units and the public and provides greater transparency and accountability of Units' finances.
- requiring Units' governing bodies to acknowledge fiscal and internal control issues and initiate a response to the LGC, which better ensures that issues are acknowledged and addressed months earlier than under the current process, and allows the LGC greater opportunity to provide guidance for struggling units,
- requiring submission of data from the audit report, which provides valuable, relevant fiscal health data in a consistent and usable form to both the Units' governing bodies and the LGC to assist Units in their sound financial management practices and assist the LGC's fiscal health monitoring, and
- modifying the invoicing and invoice approval process, which would better reflect auditors' current billing practices and save over 300 hours of LGC staff time.

APPENDIX A

20 NCAC 03 .0502 is proposed for amendment as follows:

20 NCAC 03 .0502 AUDIT CONTRACT

(a) The Secretary may promulgate a standard audit contract designed to include the specific requirements in Subdivision (c) of this Rule. The Secretary may revise the standard audit contract from time to time as circumstances require provided that the contract continues to include the requirements of this Section. The requirements may be included in the contract either specifically or by reference to this Section.

(b) Governmental units and their independent auditors may submit contracts on their own forms provided that the form includes all requirements, either specifically or by reference, in Subdivision (c) of this Rule.

(c) The following requirements and conditions shall be included in all contracts for governmental units:

(1) The scope of the audit shall include all funds and ledgers of the governmental unit, and the requirement that the audit shall be conducted in accordance with generally accepted auditing standards and shall include such tests of the accounting records and such other procedures (including direct confirmation of tax, utility and other receivables) as are considered by the auditor to be necessary in the circumstances. Exceptions to the scope of the audit may be made only by specific approval of the Secretary or a deputy secretary and only for reasons that are fully explained as to the circumstances of the particular situation.

(2) The audit shall include a review of the internal control system of the governmental unit as provided by generally accepted auditing standards. The auditor shall forward a management letter to the unit, detailing ~~his~~the auditor's findings and ~~his~~ recommendations for improvement. The auditor shall forward a copy of the management letter to the Secretary.~~Commission.~~

(3) Information based on the audited financial statements shall be submitted to the Secretary for the purpose of identifying Financial Performance Indicators and Financial Performance Indicators of Concern.

(4) The auditor shall, after ~~the~~ completion of his or her examination, submit to the governing body a report of the audit with as many copies as requested in the contract. The report shall include all funds and ledgers included in the scope of the audit, and an expression of opinion on the financial statements included therein. If the expression of opinion is in any way modified~~qualified~~ or if an opinion is disclaimed or not included for any reason, sufficient reasons therefor shall be included in the report of audit. Copies of the audit report and any special reports issued as a result of the audit engagement shall be transmitted forthwith to the Secretary~~Commission~~.

(5) The fee for the audit engagement shall be stated. All audit engagement fees and terms shall be clearly stated and shall allow for the computation of a final fee. ~~The fee may be stated as a fixed dollar amount or as a rate per hour or day, either with or without a maximum.~~

(6) The auditor shall present the audited financial statements including any compliance reports to the unit's governing body or audit committee in an official meeting in open session as soon as the audited financial statements are available but not later than 45 days after the submission of the audit

report to the Secretary. The auditor's presentation to the unit's governing body or audit committee must include:

(A) the description of each finding, including all material weaknesses and significant deficiencies, and any other issues related to the internal controls or fiscal health of the unit as disclosed in the management letter, the Single Audit or Yellow Book reports, or any other communications regarding internal controls as required by current auditing standards set by the Accounting Standards Board or its successor;

(B) the status of the prior year audit findings;

(C) the values of Financial Performance Indicators based on information presented in the audited financial statements; and

(D) notification to the governing body that the governing body must develop a "Response to the Auditor's Findings, Recommendations, and Fiscal Matters," if required under Rule 20 NCAC 03 .0508.

The Secretary shall verify auditors' compliance with the presentation requirement of Paragraph (c)(6) of this Rule.

(7) The auditor shall promptly notify the governing body and the Secretary ~~commission,~~ if circumstances disclosed ~~by~~ during the audit call for an expanded scope of work ~~more detailed investigation~~ by the auditor beyond that ~~than necessary under ordinary conditions~~ indicated by the auditor's audit planning and risk assessment.

(8) No agreement(s) relating to the audit engagement but not attached to and referenced in the audit contract shall be enforceable by any party to said agreement(s).

(d) Form LGC-205 shall be provided for the convenience of those auditors and units who wish to use the form.

(e) The Commission is the state's agency charged with the duty of advising and assisting unit officials in all phases of fiscal management, and with promoting sound fiscal management, careful borrowing, and sound debt management practices as described in Rule 20 NCAC 03 .0101. To fulfill these duties, and pursuant to its authority under G.S. 159-34(b), the Commission may establish relevant criteria for gathering financial data to timely assist and identify units that are facing or may face fiscal management challenges or distress. For purposes of this Section, the following definitions apply:

(1) Financial Performance Indicators are values derived from information included in the audited financial statements that assist the Secretary in improving the comparability of reporting a given unit's financial condition and financial performance. These criteria include, but are not limited to, adequacy of a unit's fund balance; liquidity or the ability to meet short-term obligations; solvency or the ability to meet long-term obligations; debt service coverage; leverage; and such other indicators of financial condition and financial performance as the Secretary may from time to time establish.

(2) Financial Performance Indicators of Concern are Financial Performance Indicators with values which may indicate inadequate financial conditions or fiscal management concerns within the unit.

History Note: *Authority G.S. 159-3(f); 159-34;*
Eff. February 1, 1976;
Readopted Eff. September 23, 1977;
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. January 9, ~~*2018.*~~*2018;*
Amended Eff. November 1, 2020.

20 NCAC 03 .0505 is proposed for amendment as follows:

20 NCAC 03 .0505 AUDIT BILLINGS

(a) All invoices for services rendered in an audit engagement as defined in Rule 20 NCAC 3 .0503 shall be submitted to the Commission for approval before any payment is made. Payment before approval is a violation of law.

(b) Invoices to be approved shall be submitted ~~in duplicate~~ to the Secretary.~~Secretary at the mailing address of the Commission.~~

(c) Invoices shall be approved only under the following circumstances:

(1) There is a valid contract;

(2) The report of audit has been received;

(3) The audit billing ~~and the report of audit conform~~conforms to the requirements of the contract and of this Section;

(4) ~~Except in the case of a fixed fee, the~~The audit billing shows all calculations necessary to compute the fee from the rates and terms shown in the contract; and

(5) There are no circumstances known to the ~~secretary~~Secretary indicating that the audit report may fail to conform to the requirements of the contract and of this Section. ~~a failure on the part of the auditor to perform the audit as provided in this Section.~~

Notwithstanding the above, the Commission may approve interim billings up to a maximum of ~~75 percent of a fixed or maximum fee, or, in the case where there is no fixed or maximum fee, up to a maximum of~~ 75 percent of the last ~~year's~~ billings for the last annual audit of the subject ~~unit.~~unit submitted to the Secretary. Provided however, that the Secretary or a deputy secretary may approve a higher or lower ~~amount, on an interim billing~~amount if he or she finds that such would be more equitable under a particular set of circumstances.

History Note: *Authority G.S. 159-3(f); 159-34;*
Eff. February 1, 1976;
Readopted Eff. September 23, 1977;
Pursuant to G.S. 150B-21.3A, rule is necessary without substantive public interest Eff. January 9, ~~2018.~~2018;
Amended Eff. November 1, 2020.

20 NCAC 03 .0508 is proposed for adoption as follows:

20 NCAC 03 .0508 RESPONSE TO THE INDEPENDENT AUDITOR'S FINDINGS, RECOMMENDATIONS, AND FISCAL MATTERS

(a) If the governing body of a unit of local government or public authority is notified by its independent auditor that the audited financial statements presented to the governing body included one or more significant deficiencies, material weaknesses, other findings or if the auditor determined that Financial Performance Indicators of Concern were identified based on information presented in the audited financial statements, then the governing body shall develop a "Response to the Auditor's Findings, Recommendations and Fiscal Matters" ("Response") signed by a majority of the members of the governing body and forward a copy of this response to the Secretary within 60 days of the auditor's presentation.

(b) The Response shall address each significant deficiency, material weaknesses and other finding(s) presented to the governing body and shall provide a financial plan to address each Financial Performance Indicator of Concern reported to the governing body and shall include the following:

(1) Audit Findings

(A) A written description of the procedure or process developed by the local government to address each finding, including all material weaknesses and significant deficiencies, and any other issues related to the internal controls or fiscal health of the unit as disclosed in the management letter, the Single Audit or Yellow Book reports, or any other communications regarding internal controls as required by current auditing standards set by the Accounting Standards Board or its successors.

(B) The description must provide sufficient detail that the governing body and the auditor can determine that the procedure or process will reasonably address the specific audit finding and is being properly implemented. The description may include such information as the date for implementation, the position titles responsible for implementation, the positions performing the procedures or processes, the frequency of performance, and other matters necessary to evaluate the success of the procedure or process.

(C) If the governing body disagrees with an audit finding, it shall fully describe its disagreement and explain the factors that support this determination.

(2) Financial Performance Indicators of Concern

(A) A written description of the plan developed by the governing body to address each Financial Performance Indicator of Concern.

(B) The plan must provide sufficient detail that the governing body and the auditor can determine that it will reasonably address the specific Financial Performance Indicator(s) of Concern. The description may include such information as the time period required for improvement, any governing body action required for implementation, the steps to increase revenue or reduce expenses, the frequency of performance evaluation, and other matters necessary to evaluate the success of the plan.

History Note: Authority G.S. 159-3(f); 159-34;
Eff. November 1, 2020.