



## Local Governmental Auditing and Accounting

# Newsletter



Published by the Office of the Utah State Auditor

### LOCAL GOVERNMENT DIVISION

October 2006

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### ***Questions or Concerns?***

If you have any questions or concerns regarding budgeting, financial reporting, or compliance with state law or policy, please feel free to call any of the individuals listed above. If we don't have the answer, we can research the question or refer you to the office or individual that can help you! Outside the Salt Lake City area, feel free to use our toll-free telephone number: 1-800-622-1243. You can also e-mail us at the addresses shown above.

### ***Impact Fees — New Reporting Requirements***

During the 2006 General Session, the Utah Legislature modified *Utah Code Sections* 10-5-129, 10-6-150, 17-36-37, and 17A-1-4 to require governments to provide additional reporting in their financial statements when they collect impact fees

Within 180 days after the close of year-end, each county, municipality, and special district is required to prepare an annual financial report. "Each annual report shall identify impact fee funds by the year in which they were received, the project from which the funds were collected, the capital projects for which the funds are budgeted, and the projected schedule for expenditure."

The required information must be presented as a schedule in the "supplementary information" section of the government's financial statements. This schedule requires no auditing or "in-relation-to" opinion.

The State Auditor's Office had discussions with several officials from local governments regarding how they account for impact fees and what the schedule for this new requirement should look like. It soon became clear that there was not going to be one format that would work well for all local governments. Therefore, the State Auditor's Office has not prescribed a format for this report.

All local governments are required, however, to provide a report on their impact fee activities in accordance with the sections cited above beginning for the fiscal year ending June 30, 2006, and later periods. The State Auditor's Office will be watching for those schedules in the financial reports of those entities collecting impact fees and will be looking to see that they adequately disclose the information required by the new laws. Of course, we do not have detailed information about each government's impact fees and will be relying on the local governments to ensure that the information is properly disclosed.

Independent auditors do not have any responsibility for this schedule except to "determine that a schedule identifying impact fee funds by year in which they were received, the project from which the funds were collected, the capital projects for which the funds are budgeted, and the projected schedule for expenditure has been properly included in the 'supplementary information' section of the government's financial statements," as required by the State Legal Compliance Audit Guide.

# *New Financial Reporting Requirements for Transient Room Taxes and Tourism, Recreation, Cultural and Convention Taxes*

During the 2006 legislative session, HB 40, *Expenditures for Tourism, Recreation, Cultural, and Convention Facilities and Activities*, was passed by the Legislature. It includes new reporting requirements for counties that collect the transient room tax under Utah Code Section 59-12-301 and/or the tourism, recreation, cultural and convention facilities tax under Utah Code Section 59-12-603.

*Utah Code* 17-31-5.5 provides that the legislative body of each county imposing the transient room tax and/or tourism, recreation, cultural, and convention facilities tax shall annually engage an independent auditor to perform an audit to verify that transient room tax funds and tourism, recreation, culture, and convention facilities tax are used only as authorized by State law and to report the findings of the audit to the county legislative body. This should be done as part of the regular annual audit.

This is accomplished by reporting the breakdown of expenditures as required by *UC* 17-31-5.5(3). This breakdown of expenditures should be included as an attached schedule to the Independent Auditor's Report on Legal Compliance With Applicable Utah State Laws and Regulations. **The auditor should issue an "in-relation-to opinion" on this schedule.**

*Utah Code* Section 17-31-5.5(3) requires a breakdown of expenditures into the following categories:

## **Transient Room Tax**

Establishing and promoting:

- Recreation
- Tourism
- Film production
- Conventions

Acquiring, leasing, constructing, furnishing, or operating:

- Convention meeting rooms
- Exhibit halls
- Visitor information centers
- Museums
- Related facilities

Acquiring or leasing land required for or related to:

- Convention meeting rooms
- Exhibit halls
- Visitor information centers
- Museums
- Related facilities

Mitigation costs

Payment of principal, interest, and premiums on bonds

## **Tourism, Recreation, Culture, and Convention Facilities Taxes**

Financing tourism promotion

Development, operation, and maintenance of:

- Tourist facilities
- Recreation facilities
- Cultural facilities

## **Reserves and Pledges**

Reserves on bonds related to TRT funds

Pledges as security for evidences of indebtedness related to TRCC

## **Suggested Audit Procedures**

The following are suggested audit procedures that independent auditors should consider performing to determine if the county has complied with state law. (The compliance requirements and suggested audit procedures may be found in section GC-14 of the *State of Utah Legal Compliance Audit Guide*.)

1. Determine the amount of transient room tax and tourism, recreation, culture, and convention facilities tax collected by the county during the fiscal year.
2. Determine expenditures made from amounts collected.
3. Test a representative sample of those expenditures to determine that they were made only for purposes and in the proportions authorized in *Utah Code* 17-31-2(1), (2), and (3).
4. If the collections exceeded the expenditures during the fiscal year, determine that the remainder was reserved and retained in a special fund and did not revert to the general fund.
5. Determine that the breakdown of expenditures into categories on the schedule attached to the Independent Auditor's Report On Legal Compliance With Applicable Utah State Laws is proper and accurate.
6. Report any findings in the State Legal Compliance report and to the county legislative body.

## 2006-2007 State Legal Compliance Audit Guide Update

The Utah State Legal Compliance Audit Guide has been updated as of July 1<sup>st</sup>, 2006. The audit guide is posted on our website at [www.sao.gov./sulcag/index2006.htm](http://www.sao.gov./sulcag/index2006.htm) in a pdf format. Some CPA firms like the audit guide in word format as well. For those firms who would like the audit guide in word format, please contact Kent Godfrey at (801) 538-1384 or e-mail him at [kgodfrey@utah.gov](mailto:kgodfrey@utah.gov). The word files will be burned to a CD and mailed to your firm.

Changes to the audit guide for 2006 have been minimal; however there have been a couple of changes that you should be aware of. First, we have eliminated some of the unused compliance requirement numbers. Therefore, many of the compliance requirements have been renumbered.

Second, the 2006 legislature passed a couple of bills that have added additional compliance requirements relating to transient room tax (TRT), tourism, recreation, culture and convention facilities tax (TRCC) and impact fees. (Significant compliance requirement changes have therefore been made to GC14 and GC15.) The changes basically require additional schedules to be added to the financial statements for governments that collect impact fees and for governments who receive TRT and TRCC funds (counties only). The impact fee schedule will be included as supplementary information (SI) in the financial statements. No auditor's opinion will be required. Because local governments do not account for impact fees the same way, local governments should develop a schedule that incorporates all the requirements of the law. (See separate article on impact fees.)

The TRT and TRCC schedule will be included as an attachment to the State Legal Compliance Report. (A template of what the schedule should look like is included the audit guide.) This schedule will require an in-relation-to opinion by your auditor. The two new schedules will be required for governments with a fiscal year-end for the June 30, 2006 financial statements. For those governments with a calendar year-end, the schedules will be required for the December 31, 2006 financial statements.

Finally, for school districts, the due date of the agreed-upon procedures engagement relating to adult education has been moved up from November 1<sup>st</sup> to September 15<sup>th</sup>. Other minor changes have also been made to this attestation engagement. Please review APP C-6 to en-

sure that the attestation engagement is performed correctly. Any questions or concerns with these changes should be communicated directly to the Utah State Office of Education.

**A special note to CPAs.** SAS 103 has been issued and specifically relates to audit documentation. This new SAS will also apply to Utah State Legal Compliance audit test work. CPAs need to become familiar with SAS 103 and adjust their audit documentation accordingly. When performing audit test work in regards to State Legal Compliance, simply writing "done" next to the audit step will probably not be appropriate under SAS 103. Documentation regarding what test work was actually done or who you talked with about compliance will need to be documented so that an experienced auditor could reperform your test work and come to a similar conclusion.

If you have any questions or concerns regarding State Legal Compliance, please feel free to contact our office. Good luck!



## *Risk Assessment Standards for Audits*

The AICPA's Auditing Standards board has recently issued a number of new Statements on Auditing Standards (SAS). In our May training we addressed new SASs through 103; however, SASs 104 through 112 have recently been issued and will be effective for audits of financial statements for periods beginning on or after December 15, 2006. SASs 104 through 111 are referred to as Audit Risk Assessment Standards because of the statements' common objective to assist auditors in more effectively assessing risk and focusing audit procedures in those areas of identified risk.

These new standards contain a significant amount of information which will require substantial effort and planning to ensure that they are put into operation by the implementation date. It would be impossible to address all significant aspects of these new standards in this article. However, we would like to address a few points specifically related to the Risk Assessment Standards to provide a sample of the information contained in these standards.

The Risk Assessment Standards expand, clarify and change terms frequently used by auditors. For example, SAS 104 expands the definition of the term *reasonable assurance* to now require the auditor to obtain a "... high, but not absolute level of assurance..."

SAS 106 defines audit evidence as all the information used by the auditor in arriving at the conclusions on which the audit opinion is based and includes:

- The entity's accounting records,
- Confirmations,
- Minutes,
- Industry reports,
- Audit procedures such as inquires, observations, inspections, etc.

This Statement also addresses the sufficiency (quantity) and appropriateness (quality) of audit evidence including the relationship of sufficiency and appropriateness. For example, if audit evidence gathered is of higher quality then the quantity of audit evidence may be reduced. However, the statement points out that obtaining more audit evidence may not compensate for lower quality evidence.

SAS 107 defines the financial statement user and the auditor's consideration of the financial statement user. The statement states that the auditor should, "consider the needs of users as a group" and not "the possible ef-

fect of misstatements on specific individual users, whose needs may vary widely."

The statement further defines the financial statement user as an individual having "...appropriate knowledge of business and economic activities and have a willingness to study the information in the financial statements with an appropriate diligence". The financial statement user should also understand materiality and that estimates and judgment are used in the preparation of financial statements.

The definitions noted above represent a small sample of the topics addressed in the Risk Assessment Standards. However, these topics illustrate that effectively assessing risk is not limited to a small number of considerations, but will require a broad assessment considering many aspects of an audit.



## *Management's Discussion and Analysis*

In our March 2006 newsletter there was an article titled "Management's Discussion & Analysis (MD&A) and Comparative Information". The article outlined a problem our office had noticed during reviews of financial reports. Most financial reports contained "Condensed financial information... comparing the current year to the prior year". However, when a financial report presented two complete years, the MD&A occasionally did not contain a three year comparison as required by GASB 34 (see previous article for details).

The March 2006 newsletter article proposed an alternative based upon guidance found in the AICPA's Audit and Accounting Guide for State and Local Governments (see paragraphs 2.50 – 2.51). The alternative is to present prior year partial or summarized financial information in the financial statements. When financial statements do not provide all of the information needed for a full GAAP presentation for the prior year, this information is considered partial or summarized information.

The guidance allows a financial report to present comparative prior year data on the face of the financial statements, but not repeat the footnotes or provide a third year of comparative data in the MD&A. Because the footnotes do not include two complete years and the MD&A does not present condensed financial information for three years the financial statements would not contain all of the information needed for full GAAP presentation for the prior year. When presenting partial

or summarized information, the auditor should remember that their opinion should only extend to the current period.

The audit guide further states in paragraph 2.51 that, "If prior-period financial information is presented in a partial or summarized manner and does not include the minimum information required by GAAP, the nature of the prior-period information should be described by the use of appropriate titles on the face of the financial statements and in a note to the financial statements."

Paragraph 2.51 further states that, "The use of appropriate titles includes a phrase such as 'with [*partial / summarized*] financial information for the year ended June 30, 20PY,' as part of the title of the statement or, instead, column headings that indicate the partial or summarized nature of the information."

The audit guide also provides the following sample footnote disclosing the prior-period information:

*The basic financial statements include certain prior-year summarized comparative information in total but not at the level of detail required for a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the government's financial statements for the year ended June 30, 20PY, from which the summarized information was derived.*



## *The Ins and Outs of Reporting for Redevelopment Funds*

The procedures for submitting budgets and financial reports for Redevelopment Funds (RDAs) are just a little confusing because they vary slightly from other local government entities. For this reason, we thought it would be good to review the procedures that have been established for RDAs.

There are separate and unique budget forms and certifications of budget for Redevelopment Funds. These should be completed and submitted to the State Auditor's Office and are due 30 days after the budget is adopted. Some municipalities may want to include the

RDA budget as a special revenue fund and as part of the municipality's budget. This is fine. However, the separate certification and budget form should also be submitted.

For financial reporting, the RDA should be included within the financial report of municipality that created the RDA as a Special Revenue Fund. The auditor's report or auditor's opinion will include the RDA and is due, of course, at the same time the municipality's report is due . . . 180 days after the close of the fiscal year.

## *Proper Fund Accounting*

Our reviews of this year's municipal budgets has turned up a rather unusual practice that has not been not been much of a problem in the past. However, more and more municipal budgets are showing this problem.

Our concern centers around municipalities creating governmental funds to service the needs of proprietary enterprise funds just as they would the general fund. When determining what funds should be budgeted for, each entity should remember that the budget and financial report should reconcile. That is, for every fund in the budget there should be a corresponding fund in the annual financial report and visa versa; for every fund in the financial report, there should be a corresponding budget. The only exception to this might be that no budget is required to be submitted for a trust fund. Local governments should not create a fund "for your own purposes" or budget for that fund when you know that it is not a generally accepted fund type and would not appear in your annual audited financial statements.

Enterprise funds are proprietary fund types and as such should be 'all inclusive.' That is, all aspects of

their operations should be budgeted and accounted for within the enterprise fund itself. Enterprise funds are not like the general fund which utilizes a debt service fund to service its debt, a capital projects fund to build its construction projects, etc. All of this activity should be budgeted and reported within the enterprise fund itself. Impact fees relating to the water, sewer or electric funds should be budgeted and reported in their respective enterprise or proprietary fund, not a capital projects or special revenue fund, which are governmental fund types.

We often hear the comment, "But we thought impact fees required their own fund," because of the legal restrictions on their use. It is true that impact fees do require extra care to verify that they are spent in accordance with legal requirements, but this can be accomplished by segregating them in a specific account . . . not their own fund.

We hope that this clarifies the proper budgeting procedures with regard to budgeting for enterprise funds. If you have concerns or questions, please do not hesitate to contact the State Auditor's Office.