



TOWN OF LOS GATOS
FINANCE COMMISSION REPORT

MEETING DATE: 4/29/2024

ITEM NO: 1

DATE: April 24, 2024
TO: Finance Commission
FROM: Laurel Prevetti, Town Manager
SUBJECT: Review the Staff Report to Town Council on April 16, 2024 (Item #19) and Discuss Options and Scope of Services Potentially Required Arising from the Finance Commission's Recommendation to Retain a Separate Firm to Provide the Non-Attest Services as Outlined in the Chavan and Associates Engagement Letter.

RECOMMENDATION:

Discuss the Town Council's action to move forward with the Finance Commission's recommendation to hire a separate firm to compile the Annual Comprehensive Financial Report (ACFR), including the financial statements, as distinguished from the work of the Town's independent auditor.

BACKGROUND:

The Finance Commission Chair requested this agenda item (see Attachment 4). At the December 11, 2023 Finance Commission meeting, Commissioners passed a motion to "make a recommendation to the Town Council to adopt a practice to hire a separate accounting firm who will perform the work and someone else who will do the final preparation of the financial statements."

At the January 8, 2024 Finance Commission meeting, the intent of the motion was clarified verbally to be "make a recommendation to the Town Council to adopt a practice to hire separate entity from our independent audit firm to perform work necessary for the preparation of the Town's financial statements."

At the April 16, 2024 Council meeting, the Council approved the Finance Commission's recommendation and directed that staff engage in a process of selection a separate entity for

PREPARED BY: Eric Lemon, CPA
Finance & Accounting Manager

Reviewed by: Town Manager, Town Attorney, and Finance Director

BACKGROUND (continued):

assisting with the preparation of the Annual Comprehensive Financial Report (ACFR) (Attachment 1 contains the report to Town Council).

DISCUSSION:

At the December 11, 2023 meeting, the Finance Commission indicated that the reason for the motion was to avoid a misconception by having the Town's independent auditor complete the preparation of the financial statements. During the discussion portion of the meeting, the Town's independent auditor agreed with the recommendation and clarified that the firm is currently following all audit standards and do not audit their own work. The process is first to complete the audit, and then prepare the financial statements.

At the April 16, 2024 Town Council meeting, staff presented the Commission's recommendation accurately and provided additional information regarding other municipalities in Santa Clara County that have their independent auditors complete the same work to allow efficiency (Attachment 1). During discussion, a question was asked by a Council member regarding the reason for the recommendation and staff answered that it was due to a potential threat to independence. The potential threat to independence is mitigated by safeguards as described in the following paragraphs.

Financial Statement preparation is a common non-attest service completed by the external auditor of municipalities. Non-attest services are permitted under the American Institute of Certified Public Accountants (AICPA) Code of Conduct section 1.295.040-.01. The details of the AICPA Code of Conduct are contained in Attachment 2. Based on review of the Engagement Letter, the Town's independent auditor has met all the requirements to perform the non-attest service (see Attachment 3).

To issue an opinion on the financial statements and the related opinion units, the independent auditor tests the underlying accounts and supporting records. All of this starts with the Town's Trial Balance (TB) which is the hub of the audit in terms of substantiating the numbers via the audit procedures. The financial statements and notes in the ACFR are prepared from this audited Trial Balance. The audited trial balance allows the independent auditor to issue opinions on each opinion unit contained within the ACFR.

The Town's most recent Request for Proposal for Auditing Services was reviewed by the Finance Commission at its August 9, 2021 meeting (see Item 11 at the following link):

<https://mccmeetings.blob.core.usgovcloudapi.net/losgatos-pubu/MEET-Packet-a5e23a0ea71d484fb5efa614cd507771.pdf> .

DISCUSSION (continued):

The Finance Commission participated in the selection of the current independent auditor (see Item 4 from the 12-6-2021 Special Finance Commission meeting at the following link):

<https://mccmeetings.blob.core.usgovcloudapi.net/losgatos-pubu/MEET-Packet-3e79e964cfd94a859b41582bfc08c498.pdf> .

The Town's independent auditor will be available via Zoom to address the Commissioner's questions at the meeting.

CONCLUSION:

As staff mentioned at the Council meeting, staff is open to hiring a separate consultant. Staff is in the process of developing the Request for Qualifications. As this is not a common practice in local government, staff will make all efforts to promote this opportunity to find qualified consultants to assist with the completion of the ACFR. Once responses are received, the Town will select the most qualified firm. The cost of the service will not be known until responses are received.

Staff anticipates that the independent auditor will closely work with the selected consultant, providing the audited trial balance for the compilation of the data. Setting up the mapping of the accounts and providing the audited data require additional preparation time for the ACFR. It is likely that the first year of this agreement will cause delays in the preparation of the ACFR. This also means that the timeline of a special meeting to discuss the ACFR will likely change, and the Finance Commission will receive the ACFR less than seven days prior to the special Finance Commission meeting at which the Commission begins its discussion of the document.

FISCAL IMPACT:

There is no fiscal impact associated with the Commission's discussion of this item.

ENVIRONMENTAL ASSESSMENT:

This is not a project defined under CEQA, and no further action is required.

Attachments:

1. Council Staff Report 4/6/2-24 – Item 19
2. American Institute of Certified Public Accountants (AICPA) Professional Conduct – Section 1.295 – Non-Attest Services
3. Chavan and Associates Engagement Letter
4. Auditor Communication
5. Commissioner's Communications