

# Annual Audits, Special Audits, Audit Committees, Oh My!

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# Introduction

- ❑ School boards must ensure district funds are appropriately managed and disbursed in accordance with laws, regulations, terms of grants. School attorney, Elena M. Gallegos, and certified public accountant, Audrey J. Jaramillo, will provide guidance for before, during, after an audit, and in circumstances of suspected waste, fraud, abuse. Audit Act, Open Meetings Act, Procurement Code, Governmental Conduct Act will be discussed.

# Board Powers and Duties Related to Finance

- ❑ Review and approve the annual school district budget.
- ❑ Be responsible for oversight of revenue and expenditures within the district budget.
- ❑ Acquire, lease and dispose of property.
- ❑ Issue general obligation bonds of the school district.
- ❑ Except for expenditures for salaries, contract for the expenditure of money according to the provisions of the Procurement Code.
- ❑ The Board is the Board of Finance for public school funds under its jurisdiction.

See NMSA 1978, § 22-5-4, § 22-8-38, and 6.29.1.9(A) NMAC.

# Requirement of an Audit Committee

- ❑ The Board must appoint to the Audit Committee:
  - ❑ two board members,
  - ❑ one volunteer member who is a parent of a student attending that school district, and
  - ❑ one volunteer member who has experience in accounting or financial matters.
- ❑ The superintendent and the school district business manager must serve as ex-officio members of the committee.
- ❑ No term limits unless established in Board Policy.
- ❑ Address Audit Committee in Board Policy including process for appointing members. See NMSBA Policy B-1100 © BDE (Board Committees) and compare to NMSBA Policy B-1200 © BDF (Advisory Committees).

See NMSA 1978, § 22-8-12.3(D).

# Role of Audit Committee

- (1) Evaluate the request for proposal for annual financial audit services.
- (2) Recommend the selection of the financial auditor.
- (3) Attend the entrance and exit conferences for annual and special audits.
- (4) Meet with external financial auditors **at least monthly** after audit field work begins until the conclusion of the audit.
- (5) Be accessible to the external financial auditors as requested to facilitate communication with the board and the superintendent.
- (6) Track and report progress on the status of the most recent audit findings and advise the board on policy changes needed to address audit findings.
- (7) Provide other advice and assistance as requested by the board.
- (8) Be subject to the same requirements regarding the confidentiality of audit information as those imposed upon the board by the Audit Act and rules of the state auditor.

See NMSA 1978, § 22-8-12.3(D).

# Audit Committee and the Open Meetings Act

- ❑ According to the NM Attorney General: "A committee created by statute is a public body subject to the Open Meetings Act because the legislature considered the committee's functions important enough to provide it with a separate existence as a public body, and because the committee is not simply created by a public body as a means to carry out that body's business." (OMA Guide, pages 8-9.)
- ❑ In AG Opinion No. 87-82 (12/30/1987), the Attorney General addressed a statute requiring the Board of Dentistry to establish a Dental Hygiene Committee. The Attorney General acknowledged that the committee was strictly an advisory committee with no final decisive power including policymaking power. Instead, its only role was to make nonbinding recommendations to the Board. Nevertheless, the Attorney General concluded that because it is a statutory committee, it is subject to the OMA.

# Audit Committee Open or Closed?

- ❑ Section 12-6-5 of the Audit Act provides that an audit report does not become a public record, i.e., subject to public inspection, until five days after the auditor releases it to the audited agency.
- ❑ Section 22-8-12.3 of the Public School Code expressly states that the Audit Committee is subject to the same requirements regarding the confidentiality of audit information as those imposed upon the board by the Audit Act and rules of the state auditor.
- ❑ Therefore, the Audit Committee may meet in closed executive session when necessary to comply with the Audit Act's confidentiality requirements. When meeting in executive session, the Audit Committee should comply with the notice, agenda and other requirements of the Open Meetings Act.

# Annual Audit under the Public School Code

- ❑ Must be conducted as required by the Audit Act and rules of the state auditor.
- ❑ Must be completed and submitted to the state auditor by the date specified in rules of the state auditor (*November 15<sup>th</sup>*).
- ❑ A copy of the audit report must be submitted to the NMPED at the completion of the annual audit.
- ❑ Failure to submit a timely report may result in progressive sanctions (reporting, withholding of funds, CAP, suspension of Board as board of finance).

See NMSA 1978, § 22-8-13.1.



# Special Audit under the Public School Code

- ❑ Districts may self-designate for special audit.
- ❑ NM State Auditor's Office (OSA) may designate any NM government.
- ❑ Either way, the district most likely completes procurement and chooses the auditor.
- ❑ It is not truly an "audit" but rather: an examination, forensic, or consulting engagement.
- ❑ Special audits, like annual audits, are overseen by OSA and your Audit Committee.
- ❑ At the completion of any special audit, the district must submit a copy of the audit report to PED.

See NMSA 1978, § 22-8-13.1.

# Audit Act (NMSA 1978, §§ 12-6-1 through 12-6-14)

- ❑ Annual or Special Audits must be conducted by the state auditor or independent auditors approved by the state auditor. See NMSA 1978, § 12-6-3(A).
- ❑ Audits must be conducted in accordance with generally accepted auditing standards and rules issued by the state auditor. See NMSA 1978, § 12-6-3(A).
- ❑ Reasonable costs of all audits must be borne by the school district. See NMSA 1978, § 12-6-4.
- ❑ The state auditor may administer oaths, and cause subpoenas to be issued. See NMSA 1978, § 12-6-11.

# Audit Act (NMSA 1978, §§ 12-6-1 through 12-6-14)

- ❑ “The state auditor shall cause a complete written report to be made of each annual or special audit and examination made. Each report shall set out in detail, in a separate section, any violation of law or good accounting practices found by the audit or examination.” See NMSA 1978, § 12-6-5(A).
- ❑ “**Immediately** upon discovery of any violation of a criminal statute in connection with financial affairs, the state auditor shall report the violation to the proper prosecuting officer and furnish the officer with all data and information in his possession relative to the violation. An agency or independent auditor shall report a violation immediately to the state auditor.” See NMSA 1978, § 12-6-6.
- ❑ Audit Rule 2.2.2 10(N) also requires reporting any “**possible**” or “**alleged**” violations.
- ❑ “Any person subpoenaed under this section who fails to appear, refuses to testify or fails to produce the required books or records is guilty of a misdemeanor and shall be punished by a fine of not less than five hundred dollars (\$500) nor more than one thousand dollars (\$1,000).” See NMSA 1978, § 12-6-11(C).

# More on Special Audits

- ❑ **“Special audit”** means “a limited-scope examination of financial records and other information designed to investigate allegations of waste, fraud, abuse, theft, non-compliance, or misappropriation of funds, or to quantify the extent of such losses, including both attest engagements and non-attest engagements, performance audits, forensic accounting engagements, and any other engagement that is not part of the annual financial statement and compliance audit, depending on designation or scope.” 2.2.2.7 (S)(5) NMAC.
- ❑ School district initiated:
  - ❑ Requires prior written approval of the state auditor.
  - ❑ Must be by an IPA or other professional that has been approved by the state auditor to conduct such work.
  - ❑ Contract must include the fee, start and completion date, and the specific scope of services to be performed, and must follow any template that the state auditor may provide.

# More on Special Audit (Key Definitions)

- “‘Waste’ includes, but is not limited to, the act of using or expending resources carelessly, extravagantly, or to no purpose. Importantly, waste can include activities that do not include abuse. Rather waste relates primarily to mismanagement, inappropriate actions, and inadequate oversight. Waste does not necessarily involve fraud or illegal acts. However, waste may be an indication of potential fraud or illegal acts and may still impact the achievement of defined objectives. (GAO-14-704G federal internal control standards paragraph 8.03.)” 2.2.2.7 (W) NMAC.

# More on Special Audit (Key Definitions)

- “‘Fraud’ includes, but is not limited to, fraudulent financial reporting, misappropriation of assets, corruption, and use of public funds for activities prohibited by the constitution or laws of the state of New Mexico. Fraudulent financial reporting means intentional misstatements or omissions of amounts or disclosures in the financial statements to deceive financial statement users, which may include intentional alteration of accounting records, misrepresentation of transactions, or intentional misapplication of accounting principles. Misappropriation of assets means theft of an agency's assets, including theft of property, embezzlement of receipts, or fraudulent payments. Corruption means bribery and other illegal acts. (GAO-14-704G federal internal control standards paragraph 8.02).” 2.2.2.7 (F)(4) NMAC.

# More on Special Audit (Key Definitions)

- **“Abuse’** includes, but is not limited to, behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances but excludes fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. Abuse also includes misuse of authority or position for personal interests or for the benefit of another or those of an immediate or close family member or business associate. (GAGAS latest revision.) Abuse does not necessarily involve fraud or illegal acts. However, abuse may be an indication of potential fraud or illegal acts and may still impact the achievement of defined objectives. (GAO-14-704G federal internal control standards paragraph 8.03.)” 2.2.2.7 (A)(3) NMAC.

# Special Audits: Confidentiality of Files

- ❑ "A report alleging financial fraud, waste, or abuse in government that is made directly to the state auditor orally or in writing, or telephonically or in writing through the state auditor's fraud hotline or website, any resulting special audit, performance audit, attestation engagement or forensic accounting or other non-attest engagement, and all records and files related thereto are **confidential** audit documentation and may not be disclosed by the OSA or the agency, except to an independent auditor, performance audit team or forensic accounting team in connection with a special audit, performance audit, attestation engagement, forensic accounting engagement, non-attest engagement, or other existing or potential engagement regarding the financial affairs or transactions of an agency. Any information related to a report alleging financial fraud, waste, or abuse in government provided to an independent auditor, performance audit team or forensic accounting team, is considered to be **confidential** audit or engagement documentation and is subject to confidentiality requirements, including but not limited to requirements under Subsections E and M of 2.2.2.10 NMAC, the Public Accountancy Act, and the AICPA Code of Professional Conduct." 2.2.2.15(A)(3) NMAC.



# How Else Does the Board Exercise Its Financial Oversight Responsibilities?

- ❑ Each local school board must appoint at least two members of the board as a Finance Subcommittee to assist the board in carrying out its budget and finance duties.
- ❑ The finance subcommittee **must**:
  - (1) make recommendations to the local school board in the following areas:
    - (a) financial planning, including reviews of the school district's revenue and expenditure **projections**;
    - (b) review of financial statements and periodic monitoring of revenues and expenses;
    - (c) annual budget preparation and oversight; and
    - (d) procurement; and
  - (2) serve as an external **monitoring** committee on budget and *other financial matters*.

See NMSA 1978, § 22-8-12.3.

# Governmental Conduct Act (GCA) Principles

- ❑ Treat positions as a public trust.
- ❑ Advance only the public interest, not personal benefits.
- ❑ Earn the confidence of the public.
- ❑ Maintain integrity and act ethically.
- ❑ Fully **disclose** real and potential conflicts of interest.
- ❑ Do not receive money, anything of value, or a promise in exchange for promised performance of a public act.
- ❑ Memorize and use the rules for recusal. Note that the Board can vote to have a Board member recuse but they may still decline.

NMSA 1978, § 10-16-3.

# Key Provisions of the Procurement Code

- ❑ “A central purchasing office shall procure services, construction or items of tangible personal property having a value not exceeding sixty thousand dollars (\$60,000), excluding applicable state and local gross receipts taxes, in accordance with the applicable small purchase rules adopted by the secretary, a local public body or a central purchasing office that has the authority to issue rules.” NMSA 1978, § 13-1-125(A).
- ❑ “Notwithstanding the requirements of Subsection A of this section, a state agency or a local public body may procure services, construction or items of tangible personal property having a value not exceeding twenty thousand dollars (\$20,000), excluding applicable state and local gross receipts taxes, by issuing a direct purchase order to a contractor based upon the best obtainable price.” NMSA 1978, § 13-1-125(C).

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