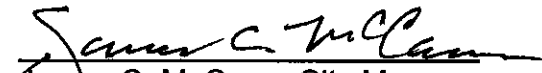


City of Calistoga

Staff Report

TO: Honorable Mayor and City Council
FROM: David W. Spilman, Administrative Services Director
DATE: May 20, 2008
SUBJECT: Audit Services for June 30, 2008 Comprehensive Annual Financial Report

APPROVAL FOR FORWARDING:


 James C. McCann, City Manager

1 **ISSUE:** To consider a Resolution to appoint Terry Krieg, CPA, to audit the
 2 City financial statements for the June 30, 2008.
 3

4 **RECOMMENDATION:** To adopt the Resolution authorizing the City Manager
 5 to accept the auditing and reporting services from Terry Krieg, CPA for the June
 6 30, 2008 financial statements for an amount not to exceed \$20,000.
 7

8 **BACKGROUND/DISCUSSION:** The City operates the budget and accounting
 9 system on a fiscal year from July 1st to June 30th. The twelve months of financial
 10 transactions are then reported, in summary form, in a Comprehensive Annual
 11 Financial Report (CAFR). The report is required to comply with the generally
 12 accepted accounting principles (GAAP) and the reporting requirements of the
 13 Governmental Accounting Standards Board (GASB). In addition, if the City has
 14 received certain Federal funds greater than \$500,000, then additional auditing
 15 procedures are required under the Federal Single Audit rules.
 16

17 Terry Krieg, CPA has provided accounting services and audited the financial
 18 statements since 1990. He is well experienced with the City's accounting
 19 system and has been asked to continue to provide these services to the City.
 20 Attached is an engagement letter from Mr. Krieg for accounting, reporting and
 21 auditing services relating to the June 30, 2008 CAFR. Included in these services
 22 is assistance in the preparation of the CAFR to continue to comply with GASB
 23 accounting and reporting standards. In addition, the City will be subject to the
 24 Federal Single Audit rules and require additional auditing and reporting.
 25

26 There have been additional GASB requirements in reporting formats (Statement
 27 #44), Post Employment Benefits Other Than Pensions (OPEB, Statement #45)

1 and Employee Termination Benefits (Statement #47). These issues will also
2 need to be addressed, as needed, in the June 30, 2008 CAFR.

3
4 The June 30, 2008 CAFR is planned to be completed and presented to the City
5 Council by no later than December 2008.

6
7 **The Audit of the Financial Statements**

8
9 The CAFR and all of the backup detail are then required to be audited by a
10 qualified independent auditor according to generally accepted auditing standards
11 issued by GASB. The auditor's report also includes comments on compliance
12 with internal accounting controls, separate reports for transit funding and grants
13 and reviews of other special financial reports. The City is also required under
14 several State laws, many Federal and State grant programs, various bond
15 requirements and best financial management practices to have an independent
16 auditor review the financial transactions of the City.

17
18 The fee for the June 30, 2008 CAFR is \$14,000 for the audit services, which is
19 the same amount as the previous year, in spite of the additional requirements for
20 audit reviews and increased complexity of financial activity of the City. In
21 addition, there is a \$3,000 fee for the preparation of the additional reporting
22 format requirements. The total of \$17,000 is the same as last year's fee. In
23 addition, the City will be subject to the Federal Single Audit requirements, there
24 will be an additional fee of \$3,000 for the separate report.

25
26 It is recommended to appoint Mr. Krieg for the June 30, 2008 accounting,
27 reporting and audit services for an amount not to exceed \$ 20,000. Attached is
28 Mr. Krieg's proposal letter, which outlines the services and fees. In addition,
29 there is a schedule to produce the June 30, 2008 audited Comprehensive Annual
30 Financial Report by no later than December 31, 2008.

31
32 **FISCAL IMPACT:** Funds for the audit services are included in the adopted
33 budget for FY 08-09.

34
35 **ATTACHMENTS:**

- 36
37 1. Resolution appointing Terry Krieg, CPA for auditing services in
38 connection with the June 30, 2008 Comprehensive Annual Financial
39 Report (CAFR)
40 2. Engagement Letter from Mr. Krieg

1
2 **RESOLUTION NO. 2008- _____**
3
4

5 **RESOLUTION OF THE CITY COUNCIL OF THE CITY OF CALISTOGA,**
6 **COUNTY OF NAPA, STATE OF CALIFORNIA, AUTHORIZING THE CITY**
7 **MANAGER TO EXECUTE THE LETTER OF ENGAGEMENT WITH TERRY E.**
8 **KRIEG, CPA FOR AUDIT SERVICES IN CONNECTION WITH THE JUNE 30,**
9 **2008 COMPREHENSIVE ANNUAL FINANCIAL REPORT**

10
11 **WHEREAS**, the City operates a finance system according to generally accepted
12 accounting principals that are codified by the National Governmental Accounting
13 Standards Board (GASB); and
14

15 **WHEREAS**, the City reconciles and closes the financial transactions as of June
16 30th of each year for the preceding twelve months; and
17

18 **WHEREAS**, the City has the year end Comprehensive Annual Financial Report
19 audited by a qualified independent audit firm; and
20

21 **WHEREAS**, GASB has implemented new accounting and reporting standards
22 which require significant changes to the accounting and reporting structures; and
23

24 **WHEREAS**, Terry E. Krieg, CPA, has been performing the audit services for a
25 number of years and is qualified to perform the audit, reporting and accounting services
26 needed to conform to various GASB statements.
27

28 **NOW, THEREFORE BE IT RESOLVED** that the City Council of the City of
29 Calistoga authorizes the City Manager to execute the letter of engagement for reporting
30 and accounting services and audit of June 30, 2008 Comprehensive Annual Financial
31 Report with Terry E. Krieg, CPA, for an amount not to exceed \$20,000.
32

33 **PASSED, APPROVED, AND ADOPTED** by the City Council of the City of
34 Calistoga at a regular meeting held this 20th of May 2008 following vote:
35
36

37 **AYES:**

38 **NOES:**

39 **ABSTAIN/ABSENT:**
40
41
42

43 _____
44 **Jack Gingles, Mayor**

45 **ATTEST:**
46
47

SUSAN SNEDDON, City Clerk



Terry E. Krieg, CPA

Certified Public Accountant

May 1, 2008

Mr. David Spilman
Administrative Services Director
City of Calistoga
1232 Washington Street
Calistoga, California 94515

Dear Mr. Spilman:

I am pleased to confirm my understanding of the services we are to provide to the City of Calistoga for the fiscal year ending June 30, 2008. We will audit the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information, which collectively comprise the basic financial statements of the City of Calistoga as of and for the fiscal year ending June 30, 2008. Accounting standards generally accepted in the United States of America provide for certain required supplementary information (RSI), such as management's discussion and analysis (MD&A) to accompany the City of Calistoga's basic financial statements. As part of our engagement, I will apply certain limited procedures to the City of Calistoga's RSI. These limited procedures will consist principally of inquiries of management regarding the methods of measurement and presentation, which management is responsible for affirming to us in its representation letter. Unless we encounter problems with the presentation of the RSI or with procedures relating to it, we will disclaim an opinion on it. The following RSI is required by generally accepted accounting principles and will be subjected to certain limited procedures, but will not be audited:

1. Management's Discussion and Analysis
2. General Fund Budgetary Comparison Schedule
3. General Fund Budgetary Comparison Schedule Reconciliation to GAAP Basis Financial Statement Revenues and Expenditures

Supplementary information other than RSI, such as combining and individual fund financial statements, also accompanies the City of Calistoga's basic financial statements. We will subject the following supplementary information to the auditing procedures applied to our audit of the basic financial statements and will provide an opinion on it in relation to the basic financial statements:

1. Combining Balance sheet for non-major governmental funds
2. Combining statement of revenues, expenditures, and changes in net assets for non-major governmental funds.
3. Schedule of expenditures of federal awards (only in those years in which it is required)

The following additional information accompanying the basic financial statements will not be subjected to the auditing procedures applied in my audit of the financial statements, and for which my auditors report will disclaim an opinion:

1. Information included in the Introductory section of the Comprehensive Annual Financial Report (CAFR) such as the letter of transmittal
2. Individual schedules of budget to actual comparisons for non-major governmental funds
3. Schedules of changes in general capital assets used in governmental activities
4. Statistical schedules included in the statistical section of the Comprehensive Annual Financial Report (CAFR)

Mr. David Spilman
May 1, 2008
Page 2

AUDIT OBJECTIVES

The objective of our audit is the expression of opinions as to whether your basic financial statements are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles and to report on the fairness of the additional information referred to in the first paragraph when considered in relation to the basic financial statements taken as a whole. The objective also includes reporting on:

- o Internal control related to the financial statements and compliance with the provisions of applicable laws, regulations, agreements, and grants, noncompliance with which could have a material effect on the financial statements in accordance with Government Auditing Standards.
- o Internal control related to major programs and an opinion (or disclaimer of opinion) on compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a direct and material effect on each major program in accordance with the Single Audit Act Amendments of 1996 and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations.

The reports on internal control and compliance will each include a statement that the report is intended for the information and use of management, specific legislative or regulatory bodies, federal awarding agencies, and if applicable, pass-through entities and is not intended to be and should not be used by anyone than these specified parties.

Our audit will be conducted in accordance with U.S. generally accepted auditing standards (in years in which a Federal Single audit is not required) and in years in which a Single Audit is required, the standards for financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; the Single Audit Act Amendments of 1996, and the provisions of OMB Circular A-133 and will include tests of the accounting, a determination of major programs in accordance with Circular A-133, and other procedures I consider necessary to enable me to express such opinions and to render required reports. If our opinions on the financial statements or the Single Audit compliance opinions are other than unqualified, I will fully discuss the reasons with you in advance. If, for any reason, I am unable to complete the audit or are unable to form or have not formed opinions, I may decline to express opinions or to issue a report as part of this engagement.

Our audit will be conducted in accordance with auditing standards generally accepted in the United States of America. A Federal Single Audit shall be performed in accordance with the standards for financial audits contained in Government Auditing Standards (because the City anticipates expending more than \$500,000 in federal grant funds in any one fiscal year).

MANAGEMENT RESPONSIBILITIES

Management is responsible for establishing and maintaining internal controls, including monitoring ongoing activities; for the selection and application of accounting principles; and for the fair presentation in the financial statements of the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Calistoga, and the respective changes in financial position and, where applicable, cash flows in conformity with U.S. generally accepted accounting principles; and for federal award program compliance with applicable laws and regulations and the provisions of contracts and grant agreements. Management is responsible for the basic financial statements and the accompanying information as well as the representations included therein.

You are also responsible for management decisions and functions. As part of the audit, I will prepare a draft of your financial statements, schedule of expenditures of federal awards, and related notes. In accordance with U.S. generally accepted auditing standards (or Government Auditing Standards), you will be required to review and approve those financial statements prior to their issuance and have a responsibility to be in a position in fact and appearance to make an informed judgment on those financial statements. Further, you are required to designate a qualified management-level individual with suitable skill, knowledge, or experience to oversee our services and any non-attest services we provide; and for evaluating the adequacy and the results of those services and accepting responsibility for them. We understand that the City has designated you, as the City's Administrative Services Director, to be the person responsible for such oversight of our services.

Management is responsible for making all financial records and related information available to us, including identifying significant vendor relationships in which the vendor has the responsibility for program compliance and for the accuracy and completeness of that information. Management's responsibilities include adjusting the financial statements to correct material misstatements and for confirming to us in the representation letter that the effects of any uncorrected misstatements aggregated by us during the current engagement and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

With regard to the electronic dissemination of audited financial statements, including financial statements published electronically on your website, you understand that electronic sites are a means to distribute information and, therefore, we are not required to read the information in these sites or to consider the consistency of other information in the electronic site with the original document.

With regard to using the auditor's report, you understand that you must obtain our prior written consent to reproduce or use our report in bond offering official statements or other documents.

You are responsible for the design and implementation of programs and controls to prevent and detect fraud, and for informing us about all known or suspected fraud or illegal acts affecting the government involving (1) management, (2) employees who have significant roles in internal control, and (3) others where the fraud or illegal acts could have a material effect on the financial statements. Your responsibilities include informing us of your knowledge of any allegations of fraud or suspected fraud affecting the City received in communications from employees, former employees, regulators, or others. In addition, you are responsible for identifying and ensuring that the City complies with applicable laws, regulations, contracts, agreements, and grants.

Mr. David Spilman
May 1, 2008
Page 4

Additionally, as required by OMB Circular A-133, it is management's responsibility to follow-up and take corrective action on reported audit findings and to prepare a summary schedule of prior audit findings and a corrective action plan. The summary schedule of prior audit findings should be made available for our review no later than the week of our on-site visit for final fieldwork.

Management is responsible for establishment and maintenance of a process for tracking the status of audit findings and recommendations. Management is also responsible for identifying for us previous audits or other engagements or studies related to the objectives discussed in the Audit Objectives section of this letter. This responsibility includes relaying to us corrective actions taken to address significant findings and recommendations resulting from those audits or engagements or studies. You are also responsible for providing management's views on our current findings, conclusions, and recommendations, as well as your planned corrective actions, and the timing and format related thereto.

AUDIT PROCEDURES GENERAL

An audit includes examining, on a test basis, evidence supporting amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested. We will plan and perform the audit to obtain reasonable assurance rather than absolute assurance about whether the financial statements are free of material misstatement, whether from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the City or to acts by management or employees acting on behalf of the City. Because the determination of abuse is subjective, Government Auditing Standards do not expect auditors to provide reasonable assurance of detecting abuse.

Because an audit is designed to provide reasonable, but not absolute, assurance and because I will not perform a detailed examination of all transactions, there is a risk that material misstatements or noncompliance may exist and not be detected by me. In addition, an audit is not designed to detect immaterial misstatements or violations of laws or government regulations that do not have a direct and material effect on financial statements or major programs. However, I will inform you of any material errors, material fraudulent financial reporting, or material misappropriation of assets that come to my attention. I will also inform you of material violations of laws or governmental regulations that come to our attention. I will include such matters in reports required for a Single Audit. My responsibility as an auditor is limited to the period covered by our audit and does not extend to any later periods for which we are not engaged as auditors.

Our procedures will include tests of documentary evidence supporting the transactions recorded in the accounts, and may include tests of the physical existence of inventories, and the direct confirmation of receivables, cash, investments and other assets and liabilities by correspondence with selected individuals, creditors, and financial institutions. We will request written representations from your attorneys as part of the engagement, and they may bill you for responding to this inquiry. At the conclusion of our audit, we will also require certain written representations from you about the financial statements and related matters.

Mr. David Spilman
May 1, 2008
Page 5

AUDIT PROCEDURES-INTERNAL CONTROLS

My audit will include obtaining an understanding of the city and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures.

Tests of controls may be performed to test the effectiveness of certain controls that I consider relevant to preventing and detecting errors and fraud that are material to the financial statements and to preventing and detecting misstatements resulting from illegal acts and other noncompliance matters that have a direct and material effect on the financial statements. My tests, if performed, will be less in scope than would be necessary to render an opinion on internal control and accordingly, no opinion will be expressed in our report on internal control issued pursuant to Government Auditing Standards when such a report is required.

When a Single Audit is performed, as required by OMB Circular A-133, we will perform tests of controls over compliance to evaluate the effectiveness of the design and operation of controls that we consider relevant to preventing or detecting material noncompliance with compliance requirements applicable to each major federal award program. However, our tests will be less in scope than would be necessary to render an opinion on those controls and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to OMB Circular A-133.

An audit is not designed to provide assurance on internal control or to identify significant deficiencies in internal control. However, during the audit, we will communicate to management and those charged with governance internal control related matters that are required to be communicated under professional standards (and Government Auditing Standards or OMB Circular A-133 when so required)

Under new reporting standards, audit firms are now required to communicate with those charged with governance audit matters related to the financial reporting process. Those matters may include among other matters:

- o Auditor's responsibilities
- o Planned scope and timing of the audit
- o Significant audit findings (such as new accounting policies, significant estimates, sensitive disclosures in the financial statements)
- o Difficulties encountered in performing the audit (such as reasons for delays in completion)
- o Corrected and uncorrected misstatements (Disclosure nature of significant correcting entries)
- o Disagreements with management
- o Management representations
- o Management's consultations with other independent accountants (if pertaining to application of accounting principles in use)
- o Other audit findings and issues

Mr. David Spilman
May 1, 2008
Page 6

AUDIT PROCEDURES-COMPLIANCE

As part of obtaining reasonable assurance about whether the basic financial statements are free of material misstatement, we will perform tests of the City's compliance with applicable laws and regulations and the provisions of contracts and agreements, including grant agreements. However, the objective of those procedures will not be to provide an opinion on overall compliance and I will not express such an opinion in my report on compliance issued pursuant to Government Auditing Standards (when so required).

In years in which a Single Audit is required, OMB Circular A-133 requires that I also plan and perform the audit to obtain reasonable assurance about whether the City has complied with applicable laws and regulations and the provisions of contracts and grant agreements applicable to major federal programs. My procedures in those cases will consist of tests of transactions and other applicable procedures described in OMB Circular A-133 Compliance Supplement for the types of compliance requirements that could have a direct and material effect on each of the City's major programs. The purpose of those procedures will be to express an opinion on the City's compliance requirements applicable to each of its major programs in our report issued on compliance pursuant to OMB Circular A-133

AUDIT ADMINISTRATION, FEES AND OTHER MATTERS

We understand that your employees will prepare all cash, investment, accounts receivable, and other confirmations we request and will locate any documents selected by us for testing.

When a Single Audit is required, at the conclusion of the engagement we will complete the appropriate sections of and sign the Data Collection Form that summarizes our audit findings. We will provide 25 bound copies of the City's Comprehensive Annual Financial Report (CAFR).

It is management's responsibility to submit a reporting package (for years in which a Single Audit is required) including the City's CAFR, schedule of expenditures of federal awards, a summary schedule of prior audit findings, auditors reports, and a corrective action plan along with the Data Collection Form to the designated federal clearinghouse and, if appropriate, to pass-through grantor agencies. The Data Collection Form and the reporting package must be submitted within the earlier of 30 days after receipt of the auditors reports or nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audits. At the conclusion of the engagement, we will provide information to management as to where the reporting packages should be submitted and the number to submit.

The audit documentation for this engagement is the property of Terry E. Krieg, CPA and constitutes confidential information. However, pursuant to authority given by law or regulation, I may be requested to make certain audit documentation available to a federal agency providing direct or indirect funding or the U.S. GAO for purposes of quality review of audit, to resolve audit findings, or to carry out oversight responsibilities. I will notify you of any such request. If requested, access to such audit documentation will be provided under the supervision of Terry E. Krieg. Further, upon request, we may provide copies of selected audit documentation to the aforementioned parties. These parties may intend, or decide, to distribute the copies or information to other, including other governmental agencies.

Mr. David Spillman
May 1, 2008
Page 7

The audit documentation for this engagement will be retained for a minimum of five years after the report release or for an additional period requested by an applicable federal or pass-through entity. If I am aware that a federal awarding agency, pass-through entity, or auditee is contesting an audit finding, we will contact the parties contesting the audit finding for guidance prior to destroying the audit documentation

We expect to begin the audit at a mutually agreeable date and to issue our reports no later than December 31 of each year. Our fees for these services shall be

Fiscal Year Ended June 30	Service Level	Total Fee
2008	Basic audit and drafting financial statements	\$ 14,000
2008	Single audit	\$ 3,000
2008	City's CAFR assistance	\$ 3,000
Totals		<u>\$20,000</u>

Our invoices for such work will be rendered each month as the work progresses and are payable upon presentation. In accordance with standard practice, work may be suspended if your account becomes two weeks or more past due and may not be resumed until your account is paid in full.

The above fee is based upon anticipated cooperation from your personnel, the assumption that unexpected circumstances will not be encountered during the audit, and the assumption that this will be a normal governmental audit. If significant additional time is required because of extraordinary circumstances not anticipated by us or the City, we will discuss it with you and will not perform any such additional work until we have obtained the City's written approval to perform such additional work.

Government Auditing Standards require that we provide you with a copy of my most recent external peer review report and letter of comment, and any subsequent peer review reports and letter of comments received during the period of our arrangement. A peer review report dated May 5, 2005 is attached to this letter. The most recent Peer Review was completed January 16, 2008, and that report has not yet been formally accepted and cleared for release. Upon its formal acceptance, I will forward a copy to you.

We appreciate this opportunity to serve the City of Calistoga and believe that this letter accurately summarizes the significant terms of the audit engagement. If you have any questions, please call me. If you agree with the terms of this engagement as described in this letter, please sign in the space provided below and return a signed copy to us as authorization to perform the work specified herein.

Sincerely yours,


Terry E. Krieg, CPA

Accepted By: _____

Title: _____

Date: _____

HEIDENREICH & HEIDENREICH

CERTIFIED PUBLIC ACCOUNTANTS

12020 S. Warner-Elliott Loop #121
Phoenix, AZ 85044-2700
(480)704-6301 fax 785-4619

15545 Bear Valley Rd. #B
Hesperia, CA 92345
(760) 948-2899 fax 948-7712

sheldenreich@att.net

May 10, 2005

To Terry E. Krieg
Certified Public Accountant

We have reviewed the system of quality control for the accounting and auditing practice of Terry E. Krieg, CPA (the firm) in effect for the year ended August 31, 2004. A system of quality control encompasses the firm's organizational structure, the policies adopted and procedures established to provide it with reasonable assurance of conforming with professional standards. The elements of quality control are described in the Statements on Quality Control Standards issued by the American Institute of CPAs (AICPA). The firm is responsible for designing a system of quality control and complying with it to provide the firm reasonable assurance of conforming with professional standards in all material respects. Our responsibility is to express an opinion on the design of the system of quality control and the firm's compliance with its system of quality control based on our review.

Our review was conducted in accordance with standards established by the Peer Review Board of the AICPA. During our review, we read required representations from the firm, interviewed firm personnel and obtained an understanding of the nature of the firm's accounting and auditing practice, and the design of the firm's system of quality control sufficient to assess the risks implicit in its practice. Based on our assessments, we selected engagements and administrative files to test for conformity with professional standards and compliance with the firm's system of quality control. The engagements selected represented a reasonable cross-section of the firm's accounting and auditing practice with emphasis on higher-risk engagements. The engagements selected included among others, engagements performed under Government Auditing Standards. Prior to concluding the review, we reassessed the adequacy of the scope of the peer review procedures and met with firm management to discuss the results of our review. We believe that the procedures we performed provide a reasonable basis for our opinion.

In performing our review, we obtained an understanding of the system of quality control for the firm's accounting and auditing practice. In addition, we tested compliance with the firm's quality control policies and procedures to the extent we considered appropriate. These tests covered the application of the firm's policies and procedures on selected engagements. Our review was based on selected tests therefore it would not necessarily detect all weaknesses in the system of quality control or all instances of noncompliance with it. There are inherent limitations in the effectiveness of any system of quality control and therefore noncompliance with the system of quality control may occur and not be detected. Projection of any evaluation of a system of quality control to future periods is subject to the risk that the system of quality control may become inadequate because of changes in conditions, or because the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the system of quality control for the accounting and auditing practice of Terry E. Krieg, CPA in effect for the year ended August 31, 2004, has been designed to meet the requirements of the quality control standards for an accounting and auditing practice established by the AICPA and was complied with during the year then ended to provide the firm with reasonable assurance of conforming with professional standards.

Heidenreich & Heidenreich

Heidenreich & Heidenreich
Certified Public Accountants