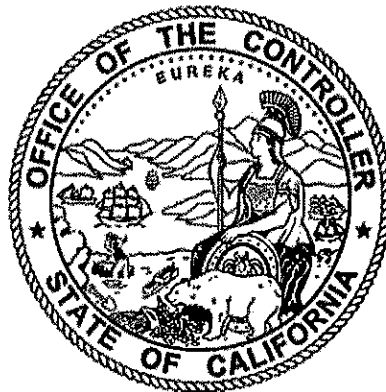


ANNUAL REPORT TO THE FIRST 5 CALIFORNIA COMMISSION

RESULTS OF AUDIT OVERSIGHT OF COUNTY COMMISSIONS

For the Period of July 1, 2016, through June 30, 2017



BETTY T. YEE
California State Controller

October 2018



BETTY T. YEE
California State Controller

October 31, 2018

Camille Maben, Executive Director
First 5 California Commission
2389 Gateway Oaks Drive, Suite 260
Sacramento, CA 95833

**SUBJECT: Annual Report to the First 5 California Commission
Results of Audit Oversight of County Commissions**

Dear Ms. Maben:

I am pleased to submit our annual report to the First 5 California Commission. The report summarizes the results of our review of the independent audits of the First 5 county commissions for fiscal year (FY) 2016-17. This report also summarizes the results of our review of the audit findings identified in the independent auditor's report to the county commissions.

This is the 11th report submitted in accordance with Senate Bill 35 (Chapter 243, Statutes of 2005), which mandated an expanded audit of every county commission funded by the California Children and Families Act of 1998. Each commission was required to adopt a range of policies including contracting and procurement, administrative expenditure limits, conflict of interest, staff compensation, and long-range financial planning. Each county commission is required to have an annual independent audit that is reviewed by the State Controller's Office.

Our review focused on the county commissions' compliance with program requirements (as reported by their independent auditors) specified in the California Health and Safety Code. We also verified the independent auditors' compliance with auditing standards and the expanded audit guidelines when performing the county commission audits. The audit findings and audit findings follow-up section of our report provide information related to the findings from each county commission's independent audit report. Lastly, where applicable, our report contains comparative statistics from the results of our desk reviews of the independent audits for FYs 2016-17, 2015-16, and 2014-15.

Camille Maben, Executive Director
October 31, 2018
Page 2

I hope that our report will be useful to you in assessing the county commissions' activities and compiling your annual report to the California State Legislature. Please direct any comments regarding the content of the report to Joel James, Chief of the Controller's Financial Audits Bureau, at jjames@sco.ca.gov or (916) 323-1573.

Sincerely,



GEORGE LOLAS
Chief Operating Officer

Enclosure

cc: James Gillies, Director, Fiscal Services Office, First 5 California Commission
George Halvorson, Commission Chair, First 5 California Commission
Lupe Jaime, Vice Chair, First 5 California Commission
Molly Munger, Commissioner, First 5 California Commission
Monica Fitzgerald, Commissioner, First 5 California Commission
Muntu Davis, Commissioner, First 5 California Commission
Alejandra Campoverdi, Commissioner, First 5 California Commission
Shana Hazan, Commissioner, First 5 California Commission
Michael Wilkening, Ex Officio Member, Health and Human Services Agency,
First 5 California Commission
Jim Suennen, Designee, First 5 California Commission

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Executive Summary

The California Children and Families Act was created in 1998 by the passage of Proposition 10. The California Children and Families Act was amended in 2005, giving the State Controller's Office (SCO) oversight responsibility for audits of the First 5 county commissions. The objective of the amendment was to provide the First 5 California Commission with independently verified fiscal and state compliance information obtained from audits performed in accordance with applicable standards and requirements.

SCO oversight responsibility includes providing audit guidelines, reviewing county commissions' annual audit reports for compliance with applicable auditing standards and guidelines, and following up on findings contained in the audit reports to ensure compliance with policies and practices specified in the California Health and Safety Code (HSC). SCO approves and makes substantive changes to the audit guide as necessary after consultation with an audit guide committee composed of representatives from the First 5 California Commission and county commissions.

Each year, SCO performs its oversight activities through a cycle of receiving, reviewing, and reporting on the auditors' reports for each county commission. This report summarizes the results of our review of independent auditors' reports for compliance with applicable standards and requirements. This report also summarizes the results of our review and follow-up on audit findings identified in the independent auditors' reports to the county commissions.

This is the eleventh report submitted in accordance with the expanded audit statutes chaptered into law in 2005; therefore, this report includes comparative results. Our report contains the following key observations we made during our review of the county commissions' independent audit reports:

- Of the 58 independent audit reports, 53 (91%) independent auditors complied with audit guide requirements and/or audit standards. In comparison, compliance was 81% in fiscal year (FY) 2015-16 and 97% in FY 2014-15.
- Of the 58 counties, 50 (86%) submitted the required audit reports by the November 1 deadline. In comparison, 78% of the audits in FY 2015-16 and 78% of the audits in FY 2014-15 were submitted by the deadline.

In addition to the observations we made during our review of the reports, the independent auditors identified a total of nine audit findings at eight county commissions; eight of the audit findings were categorized as “internal control” and one was categorized as “state compliance.” In comparison, four of the FY 2015-16 audit reports contained a total of four audit findings (three internal control and one state compliance), and seven of the FY 2014-15 audit reports contained a total of seven audit findings (six internal control and one state compliance).

We also noted that the independent auditors for two of the 58 county commissions issued qualified opinions on local commissions’ Governmental Activities. During the review cycle for FY 2015-16, two local commissions’ independent auditors issued qualified opinions. In FY 2014-15, the independent auditor for one local commission issued a qualified opinion.

Lastly, for FY 2016-17, SCO did not recommend withholding funding allocations from any commission for failure to correct (or provide a viable plan to correct) audit findings.

Introduction

Overview

SCO's Division of Audits is responsible for performing the oversight activities for independent audits of county commissions administering the First 5 program authorized by the California Children and Families Act. Oversight activities consist of:

- Developing an audit guide based on the HSC and applicable auditing standards;
- Verifying (via desk reviews/analysis) that independent audit reports, contracted for by the county commissions, complied with auditing standards and the audit guide; and
- Verifying county commission compliance with policies and practices (specified in the HSC) by reviewing and following up on audit findings reported in the independent audits.

HSC section 130151 (added by Chapter 243, Statutes of 2005) requires that SCO issue guidelines for annual expanded audits¹ that require independent auditors to review county commission compliance with policies and practices related to:

- Contracting and procurement
- Administrative costs
- Conflict of interest
- County ordinance(s)
- Long-range financial plans
- Financial condition of the commission
- Program evaluation
- Salaries and benefits policies

HSC section 130151 also requires that SCO:

- Determine, within six months of the state or county commission's response pursuant to subdivision 130151(d), whether the county commission has successfully implemented corrective action in response to the findings contained in its audit report;
- Recommend that the First 5 California Commission withhold funding allocations for county commissions unable to provide SCO with a viable plan to correct identified audit findings; and
- Submit to the First 5 California Commission, by November 1 of each year, a report summarizing the results of the reviews of the county commissions' audits for the preceding reporting cycle.

¹*Standards and Procedures for Audits of Local Entities Administering the California Children and Families Act (First 5 Audit Guide).*

Background

First 5 Program

The California Children and Families Act authorized the First 5 program. The California Children and Families Act requires that the First 5 program be funded by surtaxes imposed on the sale and distribution of cigarettes and tobacco products. The California Children and Families Act further requires that the funds be deposited into the California Children and Families Trust Fund, for the implementation of comprehensive early childhood and smoking-prevention programs.

SCO Oversight

Senate Bill (SB) 35 (Chapter 243, Statutes of 2005) added SCO oversight and reporting requirements (HSC section 130151). Prior to SB 35, existing law already included a fiscal/audit reporting component; therefore, the addition of SCO oversight was considered to be an expansion of those requirements. Consequently, the county commissions refer to SCO audit guidelines as “expanded” audit guidelines.

SCO—along with a committee composed of representatives from the First 5 California Commission, county commissions, the Government Finance Officers Association, county auditor-controllers, and independent auditors—developed the initial audit guide based on statutory requirements enumerated in HSC section 130151(b). The guide is updated as necessary by a committee composed of representatives from SCO, the First 5 California Commission, and the county commissions. HSC section 130151(b) specifies the scope of the independent audits.

Independent Audit Report Requirements

HSC requires the auditors for county commissions, or county commissions themselves², to submit an independent audit report to both SCO and the First 5 California Commission each year by November 1. The fiscal year ended June 30, 2017, was the eleventh year that the 58 county commissions were subject to SCO’s expanded audit guidelines; the resulting audit reports were due by November 1, 2017.

²The submission deadline is based on two statutory codes, one requiring the submission and one specifying the deadline:

- HSC section 130151(c) requires that “the auditor for the state commission or the county commission shall submit each audit report, upon completion, simultaneously to both the Controller and to the state commission or applicable county commission.”
- HSC section 130150(a) requires that “On or before November 1 of each year, each county commission shall submit its audit and report to the state commission.”

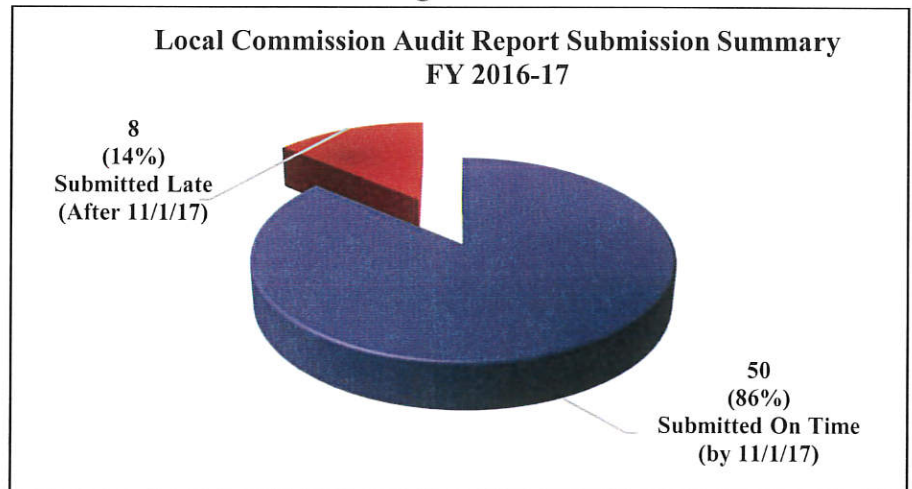
Results of Oversight Activities

Audit Report Submissions

Independent auditors' reports for each county commission for the preceding fiscal year must be submitted to SCO by November 1 of the current fiscal year. As noted in Figure 1, for FY 2016-17, 50 of 58 (86%) county commission audit reports were submitted by the required deadline, while eight (14%) were submitted after the required deadline. Of the eight reports submitted after the required deadline, three (5%) were submitted within 30 days of the deadline, while the remaining five audit reports (9%) were submitted more than 30 days late.

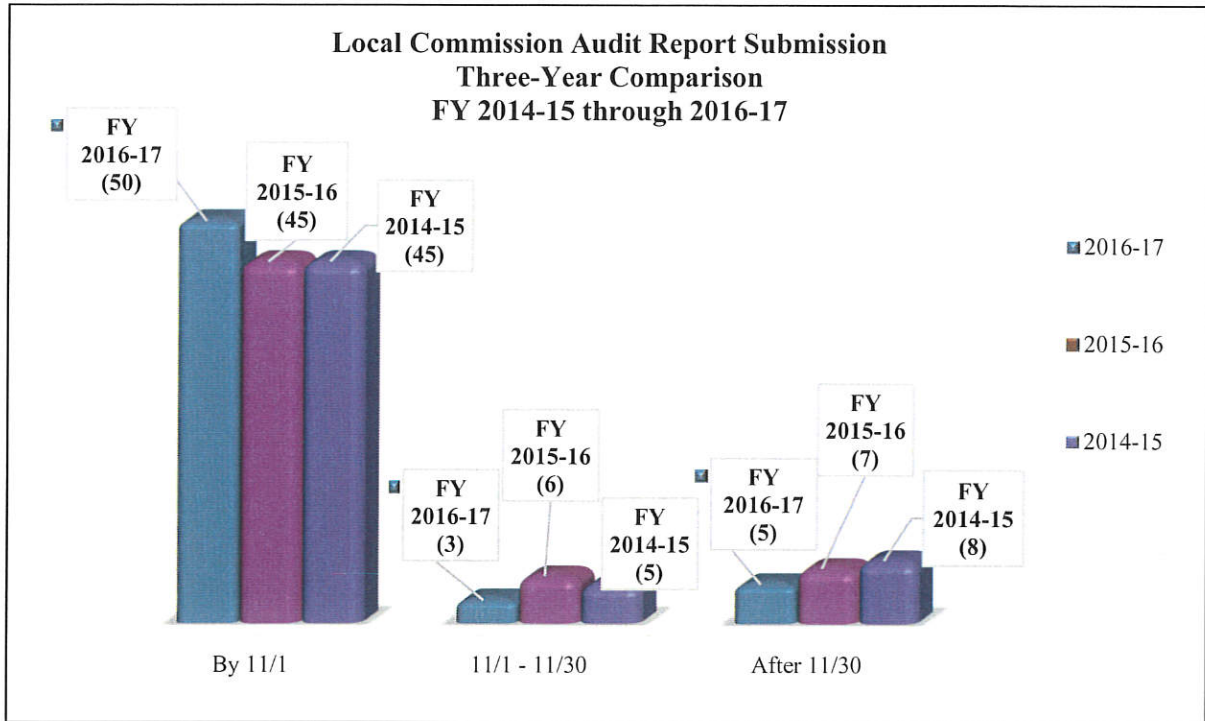
Three of the five county commissions stated that the reports were more than 30 days late due to the reporting requirements in Governmental Accounting Standards Board Statement No. 68 (GASB Statement No. 68). These county commissions experienced delays in obtaining the required financial documentation from the agency that manages pension benefits. One of the five county commissions submitted its report more than 30 days late as a result of local fires. The remaining county commission submitted its report more than 30 days late due to its new auditor's confusion about the audit report submission process.

Figure 1



Compared with the FY 2015-16 and 2014-15 audit review cycle, in FY 2016-17 there was an increase in audit reports submitted on time (50). The same number of reports (45) were submitted on time during both the FY 2015-16 and FY 2014-15 audit review cycles. For the FY 2016-17 review cycle, five audit reports were submitted more than 30 days late. See Figure 2 for comparative data on report submissions.

Figure 2



Audit Review and Certification Process

In accordance with HSC section 130151, SCO reviews and certifies the annual independent audit reports issued by the auditors for each county commission for compliance with applicable auditing standards and the audit guidelines set forth in the First 5 Audit Guide.

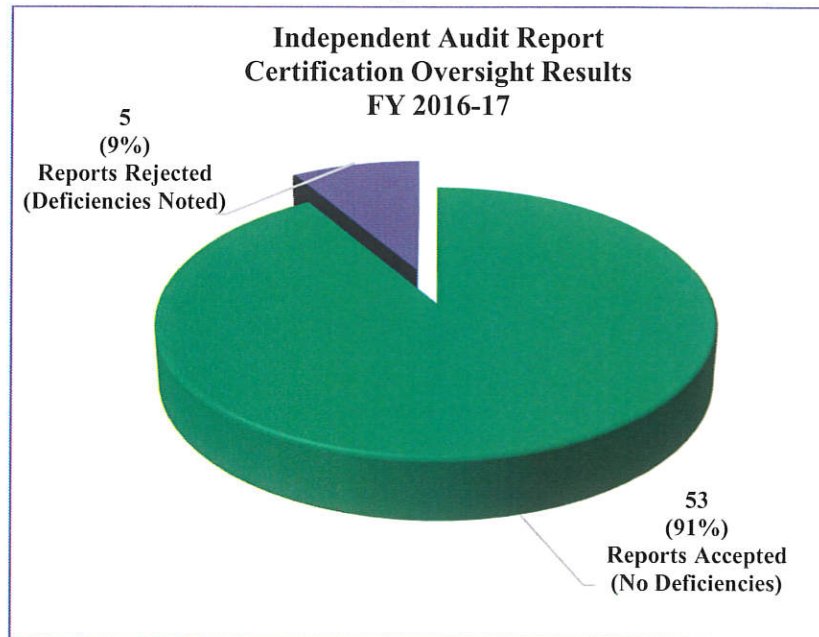
To facilitate the consistent review and certification of each audit report, SCO created a comprehensive desk review checklist that details and categorizes the program requirements specified in the First 5 Audit Guide. The desk review checklist also includes the required components of an audit report based on auditing standards generally accepted in the United States and government auditing standards. The desk review checklist is also annually updated in response to changes in auditing standards and program requirements. This report summarizes the instances of non-compliance that we found within the independent auditors' reports.

Audit Report Deficiencies

A deficiency is an instance of an independent auditor's non-compliance with auditing standards and/or the First 5 Audit Guide issued by SCO. Independent auditors, not county commissions, are responsible for addressing deficiencies in their reports on the county commissions. Based on our desk reviews of the FY 2016-17 county commission audits, we found that five of the 58 independent audits (Figure 3) contained deficiencies. SCO

notified each independent auditor and county commission in writing that the audit report required correction(s). The rejection letters identified the deficiency/deficiencies noted during our review, and the criteria used to determine non-compliance.

Figure 3



Notable Audit Report Deficiencies

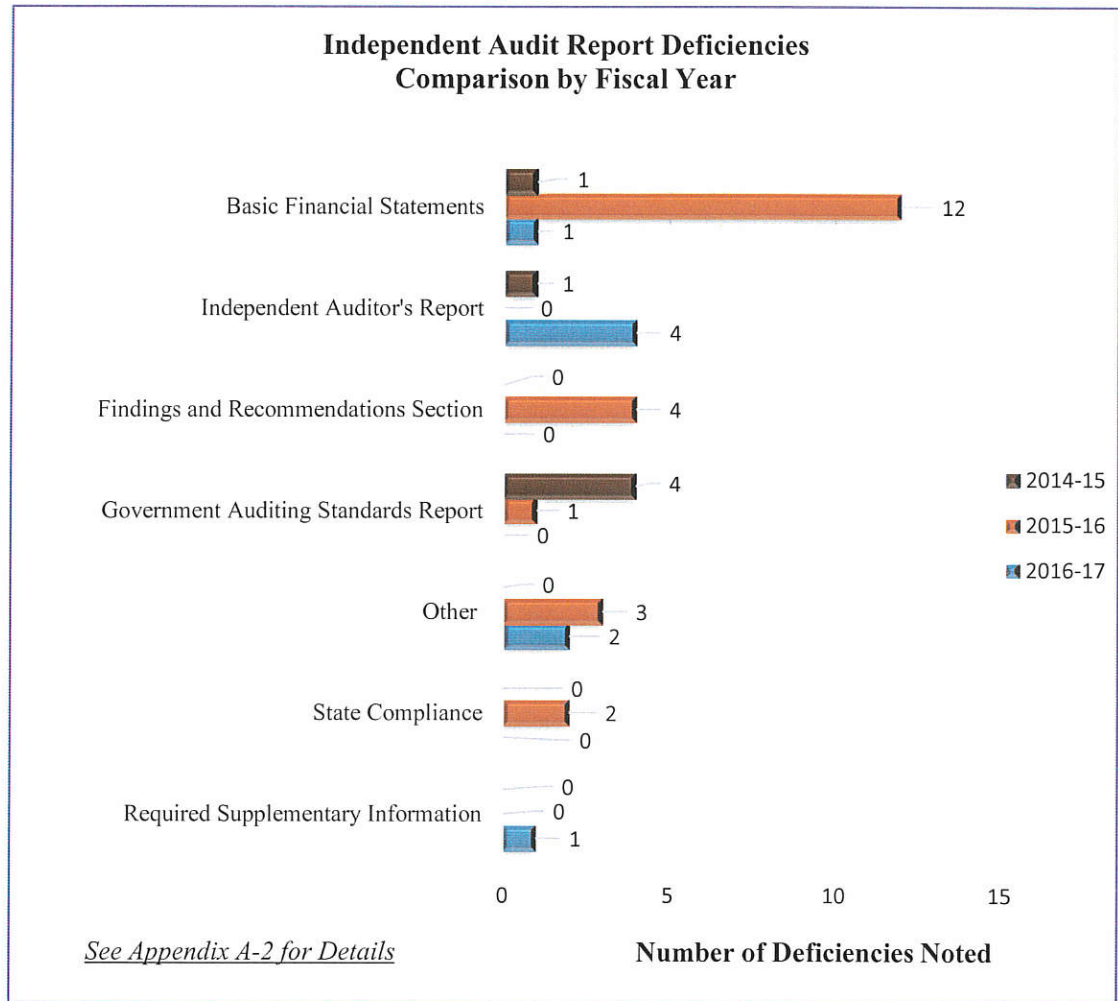
As detailed in Figure 4, during our review and certification cycle, we identified eight deficiencies in five rejected reports. The audit report deficiencies were related to the independent auditor’s report, basic financial statements, and required supplementary information. The majority of the deficiencies that we identified during our review pertained to non-compliant language in the Independent Auditor’s Report. Specifically, the report did not contain the complete statement that the audit was conducted in accordance with standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Deficiencies that we identified during our review are described in detail in Appendix A-1 and comparatively in Appendix A-2.

Other notable deficiencies that we identified were:

- The Independent Auditor’s Report, the Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards, and the State Compliance Reports were missing the name of the city and state where the auditor practices;
- The Basic Financial Statements did not total correctly; and

- The Required Supplementary Information did not total correctly.

Figure 4



***Comparison of
Independent Audit
Report Deficiencies
by Fiscal Year***

During this review cycle (FY 2016-17), we found eight independent audit report deficiencies (see Appendix 1-A for detailed category breakdown). This represents a decrease from the prior year; there were 23 deficiencies in FY 2015-16. In FY 2014-15, we identified six deficiencies. Of the eight independent audit report deficiencies identified for FY 2016-17, four (50%) were related to the Independent Auditor's Report. None of the four county commissions' independent auditors' reports were prepared in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

During this review cycle, SCO did not identify any independent audit reports that contained recurring deficiencies previously identified during the FY 2015-16 review cycle. There were also no

recurring previously identified audit report deficiencies in the FY 2015-16 or FY 2014-15 review cycles.

Figure 5 provides a breakdown by category of independent audit report deficiencies for the current and previous reporting periods. Appendix A-2 provides additional detail for each category for the three audit fiscal years.

Figure 5

Independent Audit Report Deficiencies – Comparison by Fiscal Year			
Category	Number of Occurrences		
	FY 2016-17	FY 2015-16	FY 2014-15
Independent Auditor’s Report	4	0	1
Basic Financial Statements	1	12	1
Required Supplementary Information	1	1	0
Government Auditing Standards (GAS) Report	0	1	4
State Compliance Report	0	2	0
Findings and Recommendations Section	0	4	0
Other	<u>2</u>	<u>3</u>	<u>0</u>
Total	<u>8</u>	<u>23</u>	<u>6</u>

Findings Reported by the Independent Auditors

The independent auditors for eight of the 58 county commissions reported a total of nine audit findings (Figure 6A): eight categorized as internal control, and one categorized as state compliance (Figure 6B).

Figure 6A

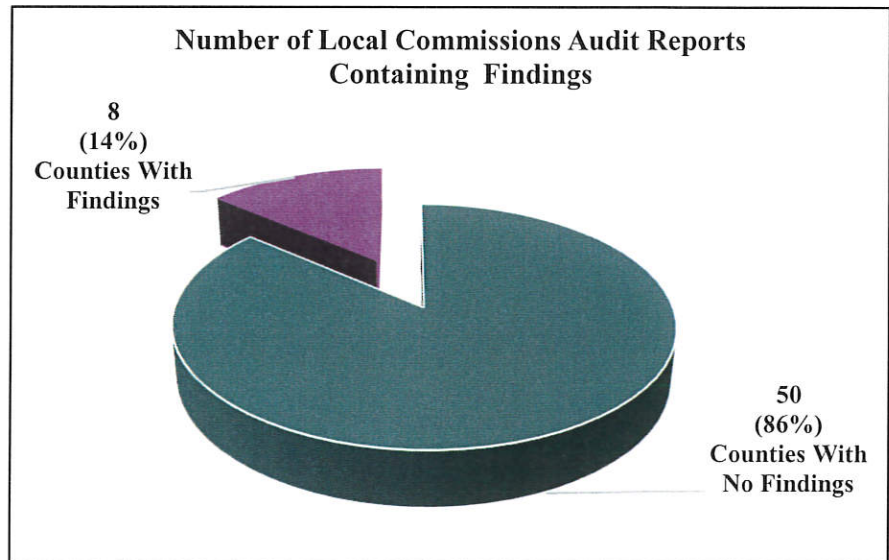
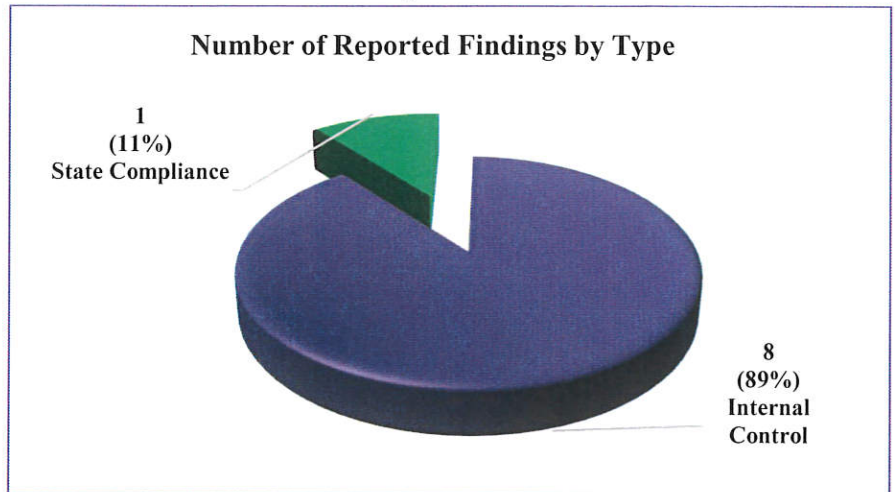


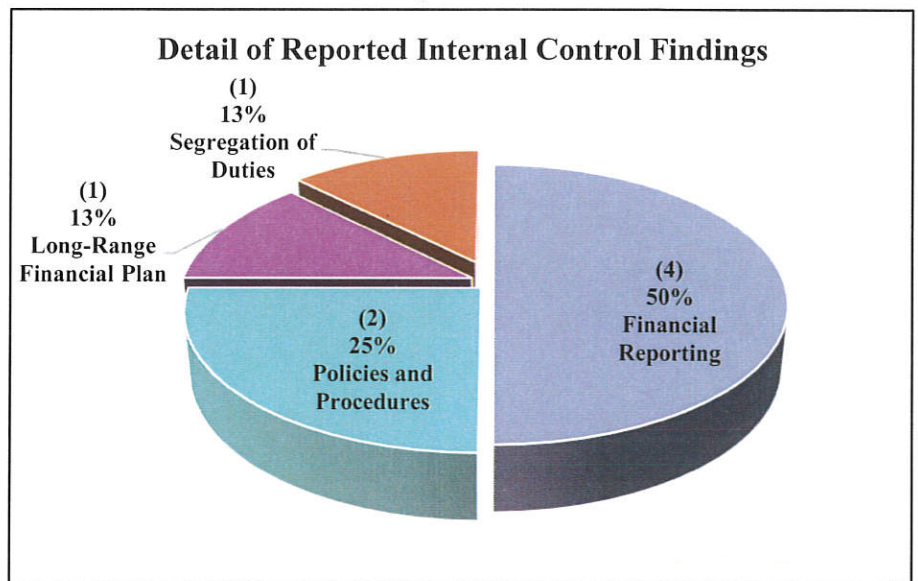
Figure 6B



Breakdown of Reported Internal Control Findings

During the FY 2016-17 review cycle, we identified four functional areas in the eight internal control findings reported for FY 2016-17, as summarized in Figure 7.

Figure 7



Three of the four internal control findings are in the financial reporting category, and are related to a recurring situation that is not readily corrected in one reporting cycle. Specifically, these findings address the county commissions' reliance on their independent auditors to draft financial statements and/or accompanying notes to the financial statements.

Consistent with Statements of Auditing Standards No. 122, section AU-C 200.05, management has acknowledged responsibility for financial statements and accompanying notes. Therefore, when an independent auditor prepares (or significantly

assists in preparing) these documents, it must be reported as an internal control finding under auditing standards applicable to FY 2016-17. Findings of this nature in all three county commissions' reports indicate that the commissions do not find it feasible to hire additional staff, or to hire an additional independent auditor to prepare financial statements and/or accompanying notes.

Based on our follow-up of the audit findings, our review of corrective action plans included in commission meeting minutes, and the county commissions' responses to audit findings, we noted that all three county commissions indicated that it is cost-prohibitive to hire staff or retain a public accountant to prepare the financial statements, but that the commissions are working with their respective county auditor-controller to assist in preparing the financial statements and/or accompanying notes.

Our review of county commissions' board meeting minutes indicated that all three county commissions apprised their governing commissions of attempts to take corrective action or implement mitigating procedures. These issues with the preparation of financial statements are not easily remedied due to a number of factors, including limited resources and options for smaller or remote county commissions. The repeat finding from FY 2015-16 is a result of the county commissions' reliance on their auditors to prepare financial statements and accompanying notes.

Breakdown of Reported State Compliance Findings

For FY 2016-17, there was one state compliance finding. There was also one state compliance finding for the FY 2015-16 and FY 2014-15 review cycles. Fiscal-year comparison by year is summarized in Figure 8.

Figure 8

Comparative Detail of Audit Findings—State Compliance			
	<u>FY 2016-17</u>	<u>FY 2015-16</u>	<u>FY 2014-15</u>
Policies and Procedures	1	1	0
Conflict of Interest	0	0	1
Total Findings	<u>1</u>	<u>1</u>	<u>1</u>

Qualified Opinion on Governmental Activities

For FY 2016-17, the independent auditors for two of the 58 county commissions issued qualified opinions on the local commissions' Governmental Activities. Specifically, neither of the two local commissions complied with reporting requirements per GASB Statement No. 68. Except for the effects of these qualified opinions, the independent auditors for the two local commissions issued unmodified opinions on the basic financial statements and

the respective financial positions of the local commissions' governmental activities. During the review cycle for FY 2015-16, two local commissions' independent auditors issued qualified opinions due to failed implementation of GASB Statement No. 68. During FY 2014-15, one qualified opinion was issued.

SCO Follow-up of Reported Audit Findings

In addition to performing our desk review of the county commission audits, SCO is required to follow up on findings reported in the county commission audits. Specifically, HSC section 130151(e) requires:

Within six months of the state or county commission's response pursuant to subdivision (d), the Controller shall determine whether a county commission has successfully corrected its practices in response to the findings contained in the audit report. The Controller may, after that determination, recommend to the state commission to withhold the allocation of money that the county commission would otherwise receive from the California Children and Families Trust Fund until the Controller determines that the county commission has a viable plan and the ability to correct the practices identified in the audit.

In accordance with HSC section 130151(d) and *Government Auditing Standards* paragraphs 4.33 through 4.36, county commissions are required to submit responses to findings in their audit reports. Audit finding follow-up is accomplished in three ways:

1. Review of evidence that the county commission has adopted a corrective action plan and/or resolved any findings. Evidence reviewed includes commission minutes, signed commission meeting agenda item documentation, and commission-approved audit finding responses;
2. Review of the subsequent fiscal year financial and compliance audit. Audit standards require that the independent auditor or auditor-controller determine the status of previously reported audit findings; and
3. Onsite visits or telephone conference by SCO staff with county commissions with audit findings.

For the FY 2016-17 audit review cycle, SCO performed follow-up of the audit findings via telephone conference with two of the eight county commissions whose independent audit reports contained findings. Our follow-up resulted in a review of 22% of the total reported findings for all eight county commissions. The two county commissions provided corrective action plans and other documentation to substantiate resolution of their FY 2016-17 audit findings.

Based on our desk reviews of commission meeting minutes and telephone conference follow-up of audit findings, SCO did not recommend withholding funding allocations from any commission for failure to correct or to provide a viable plan to correct audit findings.

Compliance with Requirement for Public Discussion of Reported Audit Findings

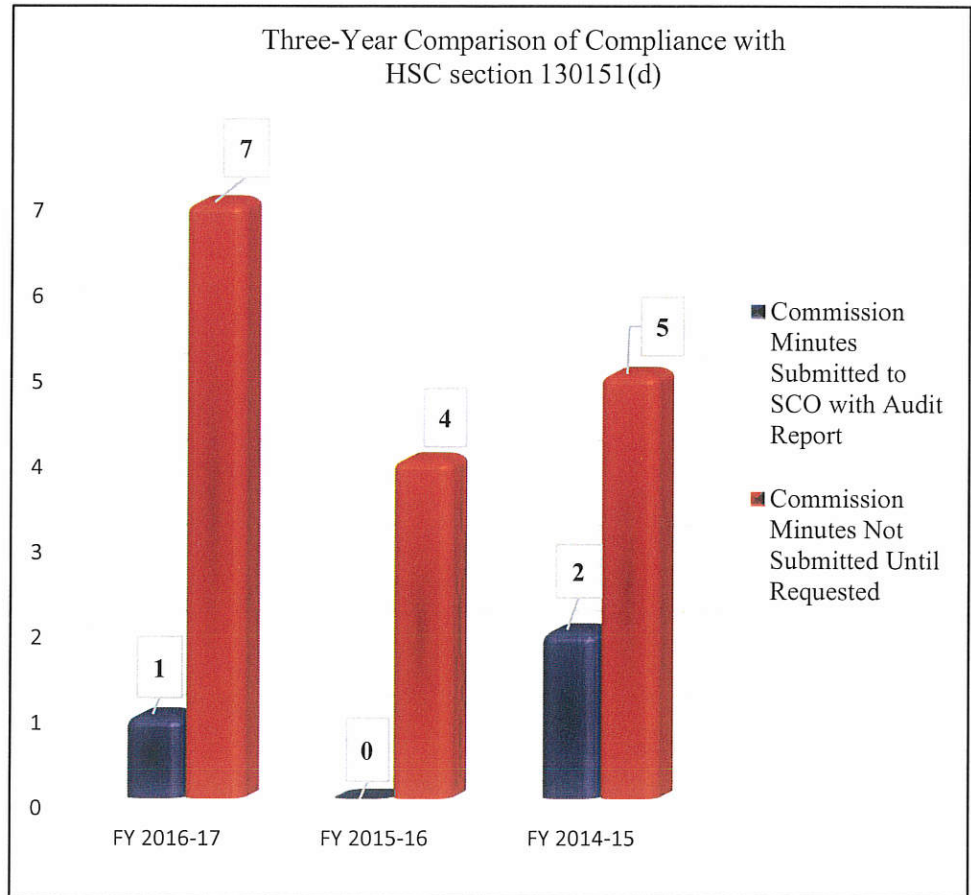
The county commissions are required to discuss their audit findings in a public hearing, and submit to the Controller a response to the audit findings. Specifically, HSC section 130151(d) states, in part, that:

...each respective county commission shall schedule a public hearing within two months of receipt of the audit to discuss findings within the report and any response to the findings. Within two weeks of the public hearing, the state or county commission shall submit to the Controller a response to the audit findings.

In September 2009, SCO issued an advisory requesting that county commissions submit evidence (e.g., commission minutes and signed commission meeting agenda item documentation) of public discussion of audit findings and any related corrective action plans with their independent audit reports. However, for the last 11 review cycles, multiple county commissions failed to submit the required documentation until requested to do so by SCO.

For FY 2016-17, only one of the eight county commissions whose independent audit contained a finding submitted public discussion-related documentation to the SCO with their audit report (Figure 9). Upon request, the remaining seven county commissions submitted the required documentation. Based on the SCO review of the documentation submitted, all eight county commissions with audit findings held public hearings discussing the findings and related corrective action plans as required by HSC section 130151(d).

Figure 9



Appendix A-1 Summary of Independent Audit Report Deficiencies Fiscal Year 2016-17

Description of Audit Report Deficiency	Number of Occurrences
<p><u>Independent Auditor’s Report</u></p> <p>The Independent Auditor’s Report – The report did not include the reference to government auditing standards in the statement that the audit was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in <i>Government Auditing Standards</i>, issued by the Comptroller General of the United States.</p>	4
<p><u>Basic Financial Statements</u></p> <p>The Basic Financial Statements – <i>The Governmental Statement of Revenues, Expenditures, and Changes in Fund Balance</i> did not total correctly and/or the auditor submitted an incorrect version of the financial statements.</p>	1
<p><u>Required Supplementary Information</u></p> <p>The Required Supplementary Information – The schedule of budgetary comparison data for the general fund and any major special revenue funds that have legally adopted budgets did not total correctly.</p>	1
<p><u>Other</u></p> <p>One or more of the auditor’s reports did not include the manual or printed signature of the auditor’s firm, the firm’s city and state, and the date of the auditor’s report.</p>	2
<p>Total</p>	<hr style="width: 100%;"/> <p style="text-align: center;">8</p>

Appendix A-2
Summary of Independent Audit Report Deficiencies
Three-Year Comparison

Description of Audit Report Deficiency	Number of Occurrences		
	FY 2014-15	FY 2015-16	FY 2016-17
<u>Independent Auditor's Report</u>			
The Independent Auditor's Report did not include the reference to government auditing standards in the statement that the audit was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in <i>Government Auditing Standards</i> , issued by the Comptroller General of the United States.	0	0	4
The Independent Auditor's Report contained an inaccurate or inconsistent reference to a separate report.	1	0	0
<u>Basic Financial Statements</u>			
The <i>Statement of Net Position</i> title and/or line items did not conform with the requirements set forth by GASB and/or did not total correctly.	0	1	0
The <i>Statement of Activities</i> was not included with the financial statements as required by GASB, did not total correctly, and/or the auditor submitted an incorrect version of the financial statements.	0	2	0
The <i>Balance Sheet – Governmental Funds</i> did not total correctly, and/or the auditor submitted an incorrect version of the financial statements.	0	2	0
The <i>Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position</i> did not conform to GASB requirements, did not total correctly, and/or the auditor submitted an incorrect version of the financial statements.	0	2	0
The <i>Governmental Statement of Revenues, Expenditures, and Changes in Fund Balance</i> did not total correctly and/or the auditor submitted an incorrect version of the financial statements.	1	3	1
The <i>Reconciliation of the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities</i> did not total correctly and/or the auditor submitted an incorrect version of the financial statements.	0	2	0

Appendix A-2 (continued)

Description of Audit Report Deficiency	Number of Occurrences		
	FY 2014-15	FY 2015-16	FY 2016-17
<u>Required Supplementary Information</u>			
The Required Supplementary Information of budgetary comparison data for the general fund and any major special revenue funds did not total correctly.	0	1	1
<u>Government Auditing Standards Report</u>			
The GAS Report included erroneous dates that result in ambiguity in the independent auditor’s opinion.	1	0	0
The GAS Report did not include a section with the heading “Response to Findings” in which material weaknesses, significant deficiencies, or reportable instances of noncompliance or other matters are identified.	1	0	0
The GAS Report did not include a statement that identifies whether the results of tests disclosed instances of noncompliance or other matters that are required to be reported under government auditing standards.	0	1	0
The GAS Report did not include a section with the heading “Response to Findings” in which material weaknesses, significant deficiencies, or reportable instances of noncompliance or other matters are identified.	1	0	0
The GAS Report did not include a statement that the audited entity’s response to the findings identified in the audit are described in the accompanying schedule or in the body of the report.	1	0	0
<u>Auditor’s Report on State Compliance (State Compliance Report)</u>			
The State Compliance Report’s reference to the list of procedures (by compliance area) as required by the audit guide was incorrect.	0	2	0
<u>Findings and Recommendations</u>			
The audit report did not include the views of responsible officials representing the auditee concerning findings, conclusions, recommendations, and planned corrective actions.	0	1	0
The audit report did not include the auditee’s corrective action plan to eliminate noncompliance with state and federal laws or internal control weaknesses.	0	1	0
The audit report did not include a Schedule of Prior Audit Findings and/or the Status of Findings.	0	2	0

Appendix A-2 (continued)

Description of Audit Report Deficiency	Number of Occurrences		
	<u>FY 2014-15</u>	<u>FY 2015-16</u>	<u>FY 2016-17</u>
<u>Other</u>			
One or more of the auditor's reports did not include the manual or printed signature of the auditor's firm, the firm's city and state, and the date of the auditor's report.	0	2	2
The sequence of the independent audit report did not follow the GASB Statement No. 34 reporting model.	0	1	0
Total	<u>6</u>	<u>23</u>	<u>8</u>

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250**

www.sco.ca.gov