

Engagement Letters, Continued

The auditee (project) is responsible for preparing the financial statement. This portion can be delegated to the auditor. In my opinion this is a wise choice because of the complexity of preparing a financial statement correctly and accurately. Although you can delegate this to your CPA, you are still responsible for the content of the financial statement. This means you supply the CPA with the information and verify that the information is accurate.

The bottom line is to read the engagement letter. It is a legal document that outlines what you and your CPA are accountable for during the audit process. It is important that you understand what you are signing. Your CPA is available to explain any areas that you need clarification on.

Below is an example of an engagement letter for a HUD audit.

November 8, 2011

Mr. John Smith

123 Happy Lane

Akron OH 44333

Dear Mr. Smith,

We are pleased to confirm our understanding of the services we are to provide for Smith House, Inc. for the year ended September 30, 2011. We will audit the statements of financial position of Smith House, Inc. as of September 30, 2011 and the related statements of activities and cash flows for the year then ended. Also, the supplementary financial information required by HUD's *Uniform Financial Reporting Standards for HUD Housing Programs* will be subjected to the auditing procedures applied in our audit of the financial statements.

We will also prepare the federal and state information returns for the year ended September 30, 2011.

AUDIT OBJECTIVES

The objective of our audit is the expression of an opinion about whether your 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 supplementary information referred to in the first paragraph when considered in relation to the financial statements taken as a whole. The objective also includes reporting on Smith House, Inc.'s:

- Internal control related to the financial statements and compliance with laws, regulations, and the provisions of contracts or grant agreements, noncompliance with which could have a material effect on the financial statements in accordance with *Government Auditing Standards*.
- 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 solely for the information and use of management, the body or individuals charged with governance, others within the entity, 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 other than these specified parties.

Our audit will be conducted in accordance with generally accepted auditing standards established by the Auditing Standards Board (United States); 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 your accounting records, a determination of major program(s) in accordance with OMB Circular A-133, and other procedures we consider necessary to enable us to express such an opinion and to render the required reports.^m If our opinion on the financial statements or the Single Audit compliance opinion is other than unqualified, we will discuss the reasons with you in advance. If, for any reason, we are unable to complete the audit or are unable to form or have not formed an opinion, we may decline to express an opinion or to issue a report as a result of this engagement

MANAGEMENT RESPONSIBILITIES

Management is responsible for the basic financial statements and all accompanying information as well as all representations contained therein. As part of the audit, we will prepare a draft of your financial statements, schedule of expenditures of federal awards, and related notes. You

are responsible for making all management decisions and performing all management functions relating to the financial statements, schedule of expenditures of federal awards, and related notes and for accepting full responsibility for such decisions. You will be required to acknowledge in the management representation letter that you have reviewed and approved the financial statements, schedule of expenditures of federal awards, and related notes prior to their issuance and have accepted responsibility for them. Further, you are required to designate an individual with suitable skill, knowledge, or experience to oversee any nonaudit services we provide and for evaluating the adequacy and results of those services and accepting responsibility for them.

Management is also responsible for establishing and maintaining internal controls, including monitoring ongoing activities; for the selection and application of accounting principles; for the fair presentation in the financial statements of financial position, changes in net assets, and 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 also responsible for making all financial records and related information available to us, including identifying significant vendor relationships in which the vendor has responsibility for program compliance and for the accuracy and completeness of that information. Your responsibilities include adjusting the financial statements to correct material misstatements and confirming to us in the management 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.

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 Smith House, Inc. 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 Smith House, Inc. received in communications from employees, former employees, grantors, regulators, or others. In addition, you are responsible for identifying and ensuring that the entity complies with applicable laws, regulations, contracts, agreements, and grants. 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 available for our review on Smith House, Inc.

Management is responsible for establishing and maintaining 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 other 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.

Management is also responsible for assuring that the electronic submission of required annual financial statement, audit, and other financial information to HUD's Real Estate Assessment Center (REAC) is complete, accurate, and timely, in accordance with your regulatory and

contractual obligations to HUD. Performance of the agree-upon procedure required by HUD relating to the electronic submission of your financial information will be addressed in a separate letter and is subject to a separate fee.

AUDIT PROCEDURES—GENERAL

An audit includes examining, on a test basis, evidence supporting the 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 about whether the financial statements are free of material misstatement, whether caused by (1) errors, (2) fraudulent financial reporting, (3) misappropriations of assets, or (4) violations of laws or governmental regulations that are attributable to the project owner or to acts by management or employees on behalf of the project owner. Because the determination of abuse is subjective, *Government Auditing Standards* do not expect auditors to provide reasonable assurance of detecting abuse. As required by the Single Audit Acts Amendments of 1996 and OMB Circular A-133, our audit will include tests of transactions related to major federal awards programs for compliance with applicable laws and regulations and the provisions of contracts and agreements.

Because an audit is designed to provide reasonable, but not absolute, assurance and because we 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 us. In addition, an audit is not designed to detect immaterial misstatements or violations of laws or governmental regulations that do not have a direct and material effect on the financial statements or major programs. However, we will inform you of any material errors that come to our attention, and we will inform you of any fraudulent financial reporting or misappropriation of assets that comes to our attention. We will also inform you of any other illegal acts that come to our attention, unless clearly inconsequential. We will include such matters in the reports required for a Single Audit. Our responsibility as auditors is limited to the period covered by our audit and does not extend to matters that arise during 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 direct confirmation of receivables and certain other assets and liabilities by correspondence with selected funding sources, creditors, and financial institutions. We will also 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 your audit, we will require certain written representations from you about the financial statements and related matters.

AUDIT PROCEDURES—INTERNAL CONTROLS

Our audit will include obtaining an understanding of the entity 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 we 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. Our tests, performed, will be less in scope than would be necessary to render an if opinion on internal control and, accordingly, no opinion will be expressed in our report on internal control issued pursuant to *Government Auditing Standards*.

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. However, during the audit, we will communicate to you and those charged with governance internal control related matters that are required to be communicated under AICPA professional standards, *Government Auditing Standards*, and OMB Circular A-133.

AUDIT PROCEDURES—COMPLIANCE

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we will perform tests of Smith House, Inc.'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 we will not express such an opinion in our report on compliance issued pursuant to *Government Auditing Standards*.

OMB Circular A-133 requires that we also plan and perform the audit to obtain reasonable assurance about whether the auditee has complied with applicable laws and regulations and the provisions of contracts and grant agreements applicable to major programs. Our procedures will consist of tests of transactions and other applicable procedures described in the *OMB Circular A-133 Compliance Supplement* for the types of compliance requirements that could have a direct and material effect on each of the Smith House, Inc.'s major programs. The purpose of these procedures will be to express an opinion on Smith House, Inc.'s compliance with requirements applicable to each of its major programs in our report on compliance issued pursuant to OMB Circular A-133.

AUDIT ADMINISTRATION, FEES, AND OTHER

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

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 the auditor's to you; however, it is management's responsibility to submit the reporting package (including financial statements, schedule of expenditures of federal awards, summary schedule of prior audit findings, auditor's reports, and corrective action plan) along with the Data Collection Form to the

designated federal clearinghouse and, if appropriate, to pass-through entities. The Data Collection Form and the reporting package must be submitted within the earlier of 30 days after receipt of the auditor's 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 audit. 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 Wagner and Company CPA, LLC and constitutes confidential information. However, pursuant to authority given by law or regulation, we may be requested to make certain audit documentation available to the Secretary of Housing and Urban Development, the HUD Inspector General, and the Government Accountability Office or their representatives for purposes of a quality review of the audit, to resolve audit findings, or to carry out oversight responsibilities. We will notify you of any such requests. If requested, access to such audit documentation will be provided under the supervision of Wagner and Company CPA, LLC personnel. Furthermore, upon request, we may provide copies of selected audit documentation to HUD or the Government Accountability Office representatives. HUD or the Government Accountability Office representatives may intend, or decide, to distribute the copies or information contained therein to others, including other governmental agencies.

The audit documentation for this engagement will be retained for a minimum of three years after the date the auditor's report is issued or for any additional period requested by HUD. If we are aware that a federal awarding agency, pass-through entity, or auditee is contesting an audit finding, we will contact the party(ies) contesting the audit finding for guidance prior to destroying the audit documentation.

We expect to begin our audit in October 2011 and to complete your information returns and issue our reports during the final week of December 2011.

We estimate that our fees for these services will be \$0,000.00 for the audit and the information returns. You will also be billed for travel and other out-of-pocket costs such as report production, word processing, postage, etc. The fee estimate is based on anticipated cooperation from your personnel and the assumption that unexpected circumstances will not be encountered during the audit. If significant additional time is necessary, we will discuss it with you and arrive at a new fee estimate before we incur the additional costs. Our invoices for these fees will be rendered each month as work progresses and are payable on presentation. In accordance with our firm policies, work may be suspended if your account becomes 90 days or more overdue and will not be resumed until your account is paid in full. If we elect to terminate our services for nonpayment, our engagement will be deemed to have been completed upon written notification

of termination even if we have not completed our report. You will be obligated to compensate us for all time expended and to reimburse us for all out-of-pocket expenditures through the date of termination.

Government Auditing Standards require that we provide you with a copy of our most recent external peer review report and any letter of comment, and any subsequent peer review reports and letters of comment received during the period of the contract. Our most recent peer review is attached.

We appreciate the opportunity to be of service to you and believe this letter accurately summarized the significant terms of our engagement. If you have any questions, please let us know. If you agree with the terms of our engagement as described in this letter, please sign the enclosed copy and return it to us.

Sincerely,

Wagner and Company CPA, LLC

RESPONSE:

This letter correctly sets forth the understanding of Smith House, Inc.

Signature: _____

Title: _____

Date: _____
