

State of New Jersey
Executive Order #122

Governor James E. McGreevey

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WHEREAS, public authorities, agencies and commissions ("authorities") of the State of New Jersey oversee billions of dollars in public funds; and

WHEREAS, the independent auditing process is fundamental to the ability of those state authorities to oversee the public funds, to set appropriate financial policies, to ensure that management maintains effective internal controls and to ensure that financial statements are free from material misstatements; and

WHEREAS, boards of directors, management, internal auditors, and independent auditors each have an important role in the authorities' financial reporting and audit processes; and

WHEREAS, management is responsible for the financial reporting process and internal controls; and

WHEREAS, internal auditors are responsible for assessing whether internal controls established by management are functioning and effective; and

WHEREAS, independent auditors are responsible for publicly attesting to the fairness of financial statements, evaluating the effectiveness of internal controls and, through the issuance of management letters, making comments and recommendations which, when implemented, may improve the design or operation of internal control systems; and

WHEREAS, an audit committee is a fundamental component of an effective financial reporting and audit process, responsible for overseeing the other participants in the process, for proactively ensuring the quality and integrity of the authority's financial reports, and for reporting any audit findings and recommendations to the board of directors for appropriate corrective action; and

WHEREAS, as Governor, I have a responsibility to manage the operations of State government and its various authorities efficiently and effectively to secure public confidence;

NOW, THEREFORE, I, JAMES E. MCGREEVEY, Governor of the State of New Jersey, by virtue of the authority vested in me by the Constitution and by the Statutes of this State, do hereby ORDER and DIRECT:

1. For the purpose of this Order, "audit" shall mean an examination of the financial statements of each Authority by a certified public accounting firm in compliance with the generally accepted government auditing standards (GAGAS), issued by the Comptroller General of the United States, as may be periodically revised, and in accordance with all applicable federal rules, regulations, and circulars. Furthermore, for purposes of this Order, "Board of Directors" or "Board" shall mean the governing body of an Authority, and "relative" shall mean a person's spouse, child, parent or sibling residing in the same household or a person's domestic partner as defined in P.L. 2003, c.246 (N.J.S.A. 26:8A-3).
2. The Board of Directors of each Authority shall create an Audit Committee of no less than three members to assist in the oversight of the financial reporting and audit processes of the Authority. At least two of the members shall be members of the Board. At no time shall a member of the Authority's staff be a member of the Audit Committee.
3. Each of the members of the Audit Committee shall be independent of the Authority. Independence of a member is satisfied only under the following circumstances:

- a. the member has no financial relationship with the Authority, nor is the member a partner, shareholder or officer of an organization that has a financial relationship with the Authority;
 - b. neither the member nor any member's relative is an employee of the Authority;
 - c. neither the member nor any member's relative is currently employed by, or has in the past three years been affiliated with or employed by, a present or former auditor of the Authority;
 - d. neither the member nor any member's relative receives or has received in any of the past three years direct or indirect compensation from the Authority for consulting, legal or financial services, regardless of the amount received and regardless of whether it is or was paid to the member or to a firm with which the member or any member's relative was associated; and
 - e. the member is in compliance with all standards regarding independence of auditors as may appear in GAGAS or may be established by the United States General Accounting Office.
4. At least one of the Audit Committee members shall have accounting or related financial expertise. All of the members should have knowledge of the Authority's governmental functions, and sufficient time to accomplish the responsibilities of the Audit Committee. In the event the Board does not have sufficient members qualified or available to serve on the Audit Committee, or wishes to broaden the expertise on the Audit Committee, the Board may request that the State Treasurer recommend one or more qualified individuals to sit on the Committee.
5. The Audit Committee shall assist the Board in retaining an independent auditor to conduct an audit of the Authority's financial statements by making a recommendation to the Board after engaging in an auditor selection process described below. The auditor selection process shall be based upon public, competitive bidding principles and shall take place no less than once every five years. The Board shall award the contract based upon the Authority's governing statute and regulations.
6. In order to ensure the independence of the auditor selection process, the Audit Committee shall adhere to the following procedures when making a recommendation to the Board to award a contract to an auditor:
- a. An evaluation committee shall be established by the Board to conduct the solicitation and evaluation of eligible auditors. The evaluation committee shall consist of no less than three Board members.
 - b. The evaluation committee shall be responsible for drafting requests for proposals (RFPs), soliciting responses to such RFPs, accepting and evaluating proposals, and providing a final written report to the Audit Committee. The evaluation committee may draw upon the expertise of the Division of Purchase and Property to assist it in the drafting of the RFP, soliciting responses to the RFPs, and evaluating proposals. The role of staff of the Authority shall be limited to providing assistance with the RFP design.
 - c. The evaluation committee shall review all responses to RFPs for responsiveness and responsibility and shall evaluate such responses pursuant to criteria established by the Audit Committee, as described below, and shall rank the responses with respect to such criteria. The evaluation committee shall prepare a written report of such evaluation and shall forward the report to the Audit Committee.
 - d. Prior to the solicitation of the engagement of any auditor, the Audit Committee shall establish criteria for the selection of an auditor and may weigh the criteria established. The weighted criteria shall be used by the evaluation committee during the evaluation of proposals. In developing the criteria to be used by the evaluation committee, the Audit Committee shall include the following:

- i. proposed fee for services;
 - ii. quality of response to RFP package;
 - iii. demonstrated ability and qualifications to conduct governmental audits;
 - iv. quality of relevant service to the governmental entities in previous transactions; and
 - v. familiarity with federal laws, rules and regulations relevant to governmental audits.
- e. Upon receipt of the evaluation committee's report, the Audit Committee shall review the report and determine whether to re-rank the responses based upon interviews. In such event, the Audit Committee shall interview the firms responding to the RFP and rank the candidates after such interviews based upon the established evaluation criteria.
- f. The Audit Committee shall make a recommendation to the Board for award of an audit contract.
- g. The Board of Directors shall review the recommendation and make an award to a firm.
- h. The Audit Committee shall also issue a report to the State Treasurer within six months of making the recommendation to the Board that sets forth the steps taken to comply with these procedures for selection of an auditor.
7. The auditor selected shall report directly to the Audit Committee or the Board. At no time shall the auditor report to any staff member of the Authority.
8. At least twice each year, the Audit Committee shall hold a private meeting with the auditor. One of these meetings shall be held prior to commencement of the audit and the other upon issuance of the final audit report. If the Authority also has an internal auditor, the internal auditor shall meet with, and report to, the Audit Committee at least once a year. Additional meetings shall be held upon the request of an Audit Committee member, a Board member, or the auditor, and may include such staff members as the Audit Committee or Board determines necessary.
9. In carrying out its duties, the Audit Committee shall proactively assist the Board in overseeing: (i) the integrity and quality of the Authority's financial statements; (ii) the Authority's compliance with legal, regulatory, and ethical requirements; (iii) the auditor's performance and ability to perform; and (iv) the performance of the Authority's own internal audit and internal control functions. In addition, the Audit Committee shall:
- a. review and evaluate audit fees;
 - b. where the Committee believes that the auditor's performance is not adequate in quality or independence, recommend such steps as may be necessary to elicit appropriate performance, including replacement of the auditor;
 - c. review the annual management letter with the independent auditor;
 - d. review and approve all engagements of the auditor with the Authority, including non-audit engagements, giving specific consideration to their effect on the independence of the auditor;
 - e. at least once every three years, obtain and review a report of the independent auditor describing for the preceding year: (1) the independent auditor's internal quality control procedures; (2) any material issues raised by the most recent internal quality control peer review, or by reviews conducted by governmental or professional authorities; and (3) steps taken by the auditor to address such issues;

- f. regularly review with the independent auditor any audit problems, any risks of material statements due to fraud, difficulties with management's response (including restrictions or attempts to restrict the auditor's activities, restrictions on access to information, and significant disagreements with management) and responsibilities, budget and staffing of the Authority's internal audit and control functions;
 - g. review the audited financial statements and interim statements and discuss them with management and internal auditors. These discussions should include a review of particularly sensitive accounting estimates, reserves and accruals, judgmental areas, audit adjustments (recorded or not) and other such matters as the Audit Committee or independent auditor shall deem appropriate;
 - h. review internal control functions such as the planned scope of internal audit reviews; adequacy of staffing; actions to be taken as a result of internal audit findings; the adequacy of compliance with the Authority's Code of Ethics; the effectiveness of electronic data processing procedures and controls and related security programs; and
 - i. recommend policies with respect to risk assessment and risk management.
10. This Order shall apply to all State authorities, commissions, boards, and councils that utilize external auditors to assist them in overseeing public funds.
11. This Order shall take effect immediately, and shall supersede Executive Order No. 26 (Whitman) to the extent that the provisions of that Order governing the selection of accountants are inconsistent with this Order.

GIVEN, under my hand and seal this 23rd day
of July in the Year of Our Lord, Two Thousand
and Four, and of the Independence of the United
States, the Two Hundred and Twenty-Ninth.

/s/ James E. McGreevey

Governor

[seal]

Attest:

/s/ Michael R. DeCotiis

Chief Counsel to the Governor