JOSEPH M. MAESTAS, P.E.
STATE AUDITOR

RICKY A. BEJARANO, CPA, CGMA
DEPUTY STATE AUDITOR

State of New Mexico
Office of the State Auditor

RULEMAKING RECORD

Pursuant to the State Rules Act, NMSA 1978, Section 14-4-1, *et. seq.*, and in conclusion of the rulemaking for the 2024 Audit Rule, 2.2.2 NMAC, effective July 16, 2024, the Office of the State Auditor provides this rulemaking record.

Publications in the New Mexico register relating to the 2024 Audit Rule, which amended the 2023 Audit Rule:

- 2024 Audit Rule, 2.2.2 NMAC, which had an effective date of July 16, 2024
    a. Adopted Rules, New Mexico Register, Volume XXXV, Issue 13 | New Mexico State Records Center and Archives: https://www.srca.nm.gov/nmac/nmregister/xxxv/2.2.2amend.html
    b. 2024 Audit Rule Direct Link: https://www.osa.nm.gov/wp-content/uploads/2024/08/2.2.2-NMAC-Integrated_2024.pdf
- 2024 Notice of Proposed Rulemaking and Public Hearing
    a. Notices of Rulemaking, New Mexico Register, Issue 3 | New Mexico State Records Center and Archives: https://www.srca.nm.gov/nmac/nmregister/xxxv/OSAnotice_xxxv03.pdf
- 2024 Amended Notice of Proposed Rulemaking and Public Hearing
    a. Notices of Rulemaking, New Mexico Register, Issue 8 | New Mexico State Records Center and Archives: https://www.srca.nm.gov/nmac/nmregister/xxxv/OSA%20notice_xxxv08.html
- 2023 Audit Rule, 2.2.2 NMAC, which had an effective date of March 28, 2023
    a. Adopted Rules, Issue 6 | New Mexico State Records Center and Archives https://www.srca.nm.gov/nmac/nmregister/xxxiv/2.2.2.html
    b. 2023 Audit Rule Direct Link: https://www.osa.nm.gov/wp-content/uploads/2023/03/Audit-Rule-2023.pdf

Technical information relied upon in formulating the Audit Rule:

- To the extent applicable, the full text for relevant technical information that served as a basis for proposed changes is available at the following sites:
    a. American Institute of Certified Public Accountants (AICPA) Standards – https://us.aicpa.org/research/standards
    b. Government Accounting Standards Board (GASB) – https://gasb.org/page/PageContent?pageId=/standards-guidance/pronouncements.html

2540 Camino Edward Ortiz, Suite A, Santa Fe, New Mexico 87507
Phone (505) 476-3800 * Fax (505) 827-3512
www.osanm.org * 1-866-OSA-FRAUD

c. U.S. Government Accountability Office (GAO) – Government Auditing Standards, (Yellow Book) 2018 Revision, April 2021 Technical Update – https://gaoinnovations.gov/yellowbook/GAO-21-368G_713761.pdf
d. NMSA 1978, 61-28B-1, *et. seq.*, the New Mexico Public Accountancy Act – https://nmonesource.com/nmos/nmsa/en/item/4397/index.do#!b/a28B
e. Office of Management and Budget - Circulars | The White House – https://www.whitehouse.gov/omb/information-for-agencies/circulars/

Video recording of the hearing:

- The public hearing on May 29, 2024, at 11:00 a.m. was recorded and can be viewed from the following links:
  a. https://www.osa.nm.gov/auditing/financial-audits/audit-rule/
  b. Direct link – https://www.youtube.com/watch?v=mcbqLr5WoJ4

Comments received during the public comment period and at the public hearing:

- The Office of the State Auditor received twenty-four public comments during the public comment period from April 23, 2024, to May 30, 2024, which can be found here and are attached as **Exhibits 1-24**.
- There were two comments made during the public hearing; a transcription of those comments is attached as **Exhibit 25**.

Full text of the initial proposed rule, full text of the final adopted rule, and the concise explanatory statement filed with the state records administrator:

- Full text of the initial proposed rule is available on the OSA website at https://www.osa.nm.gov/auditing/financial-audits/audit-rule/
  a. Direct link – https://www.osa.nm.gov/wp-content/uploads/2024/04/2024_0423_Amended-NOPR.pdf
- Full text of the final adopted rule is available on the OSA website at https://www.osa.nm.gov/auditing/financial-audits/audit-rule/
  a. Direct link – https://www.osa.nm.gov/wp-content/uploads/2024/08/2.2.2-NMAC-Integrated_2024.pdf
- Concise Explanatory Statement is attached as **Exhibit 26**.

Corrections made by the state records administrator pursuant to Section 14-4-3 NMSA 1978:

- One minor, non-substantive correction, was made, which is attached as **Exhibit 27**.

PERA
Public Employees
Retirement Association
of New Mexico

INVESTED IN TOMORROW.

Paula Fisher
Chair, State Member
Greg Trujillo
Executive Director

Phone: (505) 476-9300
Fax: (505) 476-9401
Toll Free: 1(800) 342-3422
Website: www.nmpera.org

EXHIBIT 1

March 11, 2024

New Mexico Office of the State Auditor
Attn: Christopher Hall
2540 Camino Edward Ortiz, Suite A
Santa Fe, New Mexico 87507

RE: Proposed 2024 State Audit Rule Public Comments

Dear Mr. Hall,

Thank you for providing an opportunity to comment on the New Mexico State Audit Rule. The Public Employees Retirement Association of NM (PERA) has reviewed the proposed 2024 New Mexico State Audit Rule and is providing public comments below.

<u>Section 2.2.2.8 F (3) and Section 2.2.2.8 G (1) (b)</u>

Please consider removing the changes in Section 2.2.2.8.F(3) and Section 2.2.2.8.G(1)(b) amending and shortening the auditor rotation rule from eight years to six. The possible benefit of the proposed change may assist with a freshness in perspective; however, this potential benefit does not seem to outweigh the anticipated costs. Listed below are our concerns related to a shortened auditor rotation rule.

Decreased audit quality: Allowing for an eight-year contract period allows auditors to gain a more in-depth understanding of processes and systems in place at an agency resulting in a higher quality audit. PERA is a public pension plan with $17.2 billion in investments and tracks activity for approximately 125,000 members' accounts. While PERA has many common processes for public pension plans, each public pension plan is unique. Retaining auditors for eight years allows auditors to gain additional experience with PERA's processes and systems to help ensure a high-quality audit.

Increased costs: Decreasing the auditor rotation period to six years will likely increase costs for both agencies and auditors. The first year of an audit represents a steep learning curve and requires an investment of resources which may be factored into responses to requests for proposals. If auditors are required to rotate more often, these costs may increase as the investment is for a shorter period. Agencies must also spend additional resources educating auditors on processes and systems in place, adding to the current workload. Additionally, responses to requests for proposals can vary greatly based on current economic conditions. It is more beneficial for agencies to receive a cost proposal for four years to help ensure stability in audit costs and budget accordingly.

Increased administrative burden: Shortening the auditor rotation rule to six years will require more frequent procurements placing an increased administrative burden on agencies. Requests for proposals require significant time and resources for an agency to ensure compliance with the NM Procurement Code. Requiring agencies to complete procurements more often places an additional strain on agencies' limited resources.

Transition concerns: The proposed change in the auditor rotation rule may cause transition issues. PERA currently has a four-year cost proposal in place. If PERA completes the current four-year cost proposal, we will need to solicit an RFP for a two-year cost proposal for future years, which may deter qualified firms from submitting proposals.

Allowing an eight-year audit contract period will assist with efficiencies for auditors and agencies, supporting a more sustainable audit model. We appreciate the opportunity to provide feedback on the proposed change and hope the information above is useful in weighing potential benefits and costs. Professional standards on independence and OSA's oversight have proven effective tools to help ensure fresh perspectives on audits. If concerns with an eight-year auditor rotation rule remain, we respectfully request that OSA explore additional tools to implement prior to changing the auditor rotation rule. Additional tools may include required trainings specific to New Mexico State Audit Rule and additional collaboration with auditors.

Section 2.2.2.10.Y(1)(f)

Please consider updating this section. GASBS 68 has been effective for nine fiscal years and agencies have tailored their notes to reflect pertinent information required for the standard. We believe providing template notes for agencies is no longer necessary and are proposing the following markup changes.

PERA and ERB shall each prepare an employer guide that illustrates the ~~correct use of their respective schedule of employer allocations report by their participant employers~~ use of their respective schedule of employer allocations report to create journal entries generally required by GASBS 68. ~~The guides shall explicitly distinguish between the plan-level reporting and any employer-specific items.~~ The calculations ~~and record keeping necessary~~ at the employer level (for adjusting journal entries, amortization of deferred amounts, etc.) shall be described and illustrated. The employer guides shall be made available to the participant employers by June 30 of the subsequent fiscal year. Stand-alone state agency financial statements that exclude the proportionate share of the collective net pension liability of the state of New Mexico shall include note disclosure referring the reader to the statewide comprehensive annual financial report for the state's net pension liability and other pension-related information.

We appreciate the opportunity to provide feedback on the proposed rule changes and greatly appreciate your consideration.

Sincerely,

Lynette Sanders

Lynette Sanders, CPA, CGFM

ASD Director/CFO

Exhibit 2

Administrative Office of the Courts

Supreme Court of New Mexico

Arthur W. Pepin, Director
Celina Jones, General Counsel
Dimple Tafoya, CFO

202 E. Marcy St.
Santa Fe, NM 87501

www.nmcourts.gov

March 11, 2024

Mr. Joseph M. Maestas, P.E., State Auditor
Office of the State Auditor
2540 Camino Edward Ortiz
Ste A
Santa Fe, NM 87507

RE: REQUEST FOR PUBLIC COMMENT ON 2024 NOTICE OF CHANGES TO THE STATE AUDIT RULE

Dear Mr. Maestas:

The Administrative Office of the Courts (AOC) would like to provide the following comments regarding the proposed change to the auditor rotation rule from eight years down to six years:

<u>Lower Quality</u>
The AOC believes this change would place an undue burden on state agencies and IPAs. We believe frequent audit rotations tend to lower the quality of the audits. More time, effort and money is spent on the initial learning and understanding of the agency's operations as opposed to providing an efficient, effective and thorough audit. Longer term relationships offer a deeper, historical understanding of operations which enhance the audit quality.

<u>Independence</u>
We do not adhere to the thought that less frequent audit rotations adversely affect auditor independence standards. There are several standards and mechanisms in place, including those at OSA & DFA that ensure the quality of audits remain uncompromised.

Thank you for the opportunity to comment on this potential rule change. If you have any questions, please feel free to contact me at (505) 819-9297.

Respectfully,

Dimple Tafoya

Dimple Tafoya
Chief Financial Officer
Administrative Office of the Courts

From:	Filemon Gonzalez
To:	Christopher Hall
Cc:	Henry Valdez; Crystal Funes
Subject:	Administrative Office of the District Attorney"s Viewpoint Regarding OSA"s 2024 Proposed Auditor Rotation Rule Change
Date:	Thursday, March 7, 2024 11:00:44 AM
Importance:	High

Exhibit 3

Mr. Hall,

We wish to express our perspective on the proposed adjustment of the auditor rotation mandate, reducing it from eight years to six years.

As a small State Agency, we encounter considerable difficulties in engaging audit firms willing and equipped to conduct our annual audits. Historically, our solicitations have yielded minimal to no responses from accredited audit firms. Furthermore, with prior auditors no longer listed, our pool of potential firms has significantly dwindled.

Moreover, the increased frequency of transitioning to new auditing firms is anticipated to inflate audit costs. Each new auditor would face heightened workloads in the initial years, necessitating familiarization with our operations. This could potentially compromise audit quality due to resource constraints and deadline pressures.

We firmly believe that sustained audit quality stems from a deep understanding of our operations, which is cultivated over multiple audit cycles.

To conclude, we oppose the proposed reduction in the auditor rotation rule, foreseeing adverse implications for our agency. Your attention and deliberation on this matter are greatly appreciated.

Regards,

Filemon Gonzalez
Chief Financial Officer
Administrative Office of
the District Attorneys
2929 Coors Blvd Suite 310
Albuquerque NM 87120
Ph:(505) 827-3789

Exhibit 4

CRI CARR RIGGS & INGRAM
CPAs and Advisors

Carr, Riggs & Ingram, LLC
2424 Louisiana Boulevard NE
Suite 300
Albuquerque, NM 87110

505.883.2727
505.884.6719 (fax)
CRIcpa.com

March 13, 2024

Joseph M. Maestas, P.E., CFE
New Mexico State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, NM 87507

Re: Public Comment on 2024's Notice of Changes to the State Audit Rule

Dear State Auditor Maestas,

Carr, Riggs & Ingram, LLC (CRI), a New Mexico CPA firm with offices throughout New Mexico and the southeastern United States appreciates the opportunity to submit the following comments related to the proposed 2024 Audit Rule. Below are our proposed amendments and requests for clarification regarding the draft Audit Rule.

2.2.2.8(F)(3) NMAC – *Auditor Rotation Rule*. CRI believes this change will put an undue burden on agencies and local public bodies of the state of New Mexico. We believe that changing the mandatory rotation from eight (8) years to six (6) years will affect both the governmental entities and the auditing profession in the following ways.

- **Inconsistencies with the Contracting Process.** Revising this section of the Audit Rule will cause the audit contracting process to no longer align with 13-1-150 NMSA 1978 (multi-term contracts; specified period), which requires contracts for professional services to not exceed four years, including all extensions and renewals. The proposed change in the rotation rule would increase the frequency of the RFPs impacting the entities as well as IPAs. The RFP process is a time-consuming and involved process and would require resources on the entities to administer the RFP and the IPA to prepare proposals which could lead to increased cost and reduction of competitiveness.

- **Inefficiencies and Cost Implications.** The initial year of an audit involves a significant learning curve as the auditor obtains an understanding of the operations, systems, and processes. This could lead to increased costs, not limited to audit contract fees, but time and resources of the government to work with the auditor on gaining the understanding necessary that is required by audit standards.

- **Implementation Date.** Modifying the Audit Rule would require agencies and local public bodies going into their seventh year of an audit contract to complete the contracting process to procure a new auditor and complete the necessary contracting requirements of the State Auditor's office by as early as April 15th for some local public bodies. This appears to not be in the best interest of New Mexico agencies and local public bodies. In addition, the rule, as currently drafted, would require implementation for FY 24 which would cause a delay in the procurement process, contract process and timing of audits leading to an increase in late audits.

CRI respectively requests the Office of the State Auditor defer any modification of the auditor rotation rule at this time and to evaluate the implications of a proposed change with various individuals in government and independent public accountants prior to implementing a change to auditor rotation.

2.2.2.10(J)(21) NMAC – *The New Mexico Opioid Allocation Agreement*. CRI asks for additional clarification as to the compliance expectations and requests of the proposed rule.

Thank you very much for the opportunity to submit a comment regarding these matters for your consideration.

Alan D. "A.J." Bowers, Jr, CPA, CITP
Partner

Exhibit 5

CRI CARR RIGGS & INGRAM
CPAs and Advisors

Carr, Riggs & Ingram, LLC
2424 Louisiana Boulevard NE
Suite 300
Albuquerque, NM 87110

505.883.2727
505.884.6719 (fax)
CRIcpa.com

May 30, 2024

Joseph M. Maestas, P.E., CFE
New Mexico State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, NM 87507

Re: Amended Notice of Proposed Rulemaking and Public Hearing

Dear State Auditor Maestas,

Carr, Riggs & Ingram, LLC (CRI), a New Mexico CPA firm with offices throughout New Mexico and the southeastern United States appreciates the opportunity to submit the following updated comments to the proposed amendments to the 2024 Audit Rule as well as our previous letter dated March 13, 2024. Below are our additional or amended comments regarding the draft Audit Rule:

2.2.2.8(F)(3) NMAC – *Auditor Rotation Rule*. CRI believes this change will put an undue burden on agencies and local public bodies of the state of New Mexico. We believe that changing the mandatory rotation from eight (8) years to six (6) years will affect both the governmental entities and the auditing profession in the following ways.

- **Inconsistencies with the Contracting Process and Administrative Burden.** Revising this section of the Audit Rule will cause the audit contracting process to no longer align with 13-1-150 NMSA 1978 (multi-term contracts; specified period), which requires contracts for professional services to not exceed four years, including all extensions and renewals. The proposed change in the rotation rule would increase the frequency of the RFPs impacting the entities as well as IPAs. The RFP process is a time-consuming and involved process and would require resources on the entities to administer the RFP and the IPA to prepare proposals which could lead to increased cost and reduction of competitiveness.

- **Inefficiencies and Cost Implications.** The initial year of an audit involves a significant learning curve as the auditor obtains an understanding of the operations, systems, and processes of the entity. This initial time, effort and cost is offset by efficiencies in future years. The reduction of potential future years would decrease the efficiencies in future years leading to increased costs, not limited to audit contract fees, but time and resources of the government to work with the auditor on gaining the understanding necessary that is required by audit standards.

- **Staffing Shortage, Delays and Untimely Audits.** The accounting industry nationwide, both entities and IPAs, is facing significant staffing shortages. These staffing shortages are currently affecting the entities in the ability to perform their daily operations. By requiring additional frequency to administer RFPs as well as to change IPAs more frequently reduces the entities ability to perform their daily operations leading to delays and potentially untimely audits. These staffing shortages are currently affecting IPAs by determining which RFPs in which to respond leading to lack of competitiveness or response to RFPs for the entities which can increase delays, costs, and untimely audits. In addition, the RPF process extends the timing for fully executing a contract which reduces or eliminates the ability to perform interim work until after the end of the fiscal year. This interim work is a vital component in the performance of an audit and more frequent RFPs could result in an increased delay and untimely audits.

CRI respectively requests the Office of the State Auditor to reconsider changing the mandatory rotation from eight (8) years to six (6) years.

2.2.2.10(J)(21) NMAC – *The New Mexico Opioid Allocation Agreement*. CRI asks for additional clarification as to the compliance expectations and requests of the proposed rule.

Thank you very much for the opportunity to submit a comment regarding these matters for your consideration.

Alan D. "A.J." Bowers, Jr, CPA, CITP
Partner

FINANCE DEPARTMENT
200 E. Broadway
Hobbs, NM 88240
575-397-9235 bus
575-397-9227 fax

Exhibit 6

February 26, 2024

Joseph M. Maestas, P.E., State Auditor
2540 Camino Edward Ortiz, Suite A,
Santa Fe, New Mexico 87507

Re: Request for Public Comment on 2024's Notice of Changes to the State Audit Rule.

In reviewing changes to the State Audit Rule, the City of Hobbs noted that the State Auditor's office is proposing the following amendment; "amend and shortens the auditor rotation rule from eight (8) to six (6) years. The City of Hobbs would like to provide viewpoint from the auditee's perspective.

The shorter the rotation rule, the following adverse issues would occur: risks associated with the changeover in audit team, ever-changing procedures with the audit profession, GASB reporting changes, legislative enactments (both federal and state), timeliness and staff turnover. Rotating earlier would cause the audit firm to increase risk due to the factors mentioned above, which in turn, would increase costs, staff time and instability.

The City of Hobbs believes no independence would change if the State Audit Rule remains the same at an 8 year rotation. The City of Hobbs also believes that an 8 year rotation provides a definite stable advantage to the municipality and audit firm.

By continuing the 8 year rule, quality and timeliness of future audits would be maintained for the City of Hobbs.

Cordially,

Toby Spears, CPA, CFE
Finance Director

Des Moines Municipal Schools
P.O. Box 38
Des Moines, New Mexico 88418
http://www.desmoines.k12.nm.us
Phone: 575-278-2611 • Fax: 575-278-2617

Exhibit 7

Creating Success Together . . . One Student at a Time

February 27, 2024

New Mexico Office of the State Auditor
Attn: Christopher Hall
2540 Camino Edward Ortiz, Suite A
Santa Fe, NM 87507

RE: Proposed Change to the Auditor Rotation Rule

Dear Mr. Hall:

I am reaching out to you regarding the proposed change to the Auditor Rotation Rule from an 8-year rotation, back to a 6-year rotation. Des Moines School is in the 8^{th} year of our Audit Rotation. We are asking permission to go ahead and finish out our 8 years with our current Auditor. We are a very remote school district, and it is a challenge to get responses when the district goes out for an RfP for Audit Contracts. At times, the bids can come in exceedingly high due to this challenge. After completing this 8^{th} year, it would be easier for our district to be put on the 6-year rotation.

I think this would be a benefit for all small school districts that are looking at the same situation.

Sincerely,

Debbie Martinez

Debbie Martinez, Business Manager
Des Moines Municipal School

Exhibit 8

March 8, 2024

Joseph M. Maestas, P.E., State Auditor

State of New Mexico, Office of the State Auditor

2540 Camino Edward Ortiz, Suite A,

Santa Fe, New Mexico 87507

Re: Request for Public Comment on 2024's Notice of Changes to the State Audit Rule

During review of the Notice of Changes to the State Audit Rule, it was noted that the State Auditor's Office is proposing the following amendment; "amend and shortens the auditor rotation rule from eight (8) to six (6) years". We would like to provide our viewpoint and comment on this proposed change.

We request that the State Audit Rule does not change the rotation rule. Regardless, our auditors will still have to go out to bid this fiscal year. However, if the rotation rule changes, they will not be able to bid. This change will cause a great burden on finance staff to change auditors frequently.

Changing the Rotation Rule from an 8-year Interval to a 6-year Interval can contribute to the following adverse issues

- Lower quality audits
- Increase in late audits
- Higher costs

Maintaining the 8-year Rotation Rule will continue the following advantages

- Stability fostering audit quality
- Timely audits

Thank you for the opportunity to submit a comment regarding this matter for your consideration.

Thank you,

Asma Dawood

Financial Services Director
Doña Ana County | 845 N. Motel Blvd. | Las Cruces, NM 88007
Phone: (575) 525-5974 | E-mail: asmad@donaanacounty.org

Exhibit 9

Dianna Luce
District Attorney
Fifth Judicial District
Lea, Eddy & Chaves Counties

March 5, 2024

Joseph M. Maestas, P.E., State Auditor
State of New Mexico, Office of the State Auditor
2540 Camino Edward Ortiz, Suite A,
Santa Fe, New Mexico 87507

Re: Request for Public Comment on 2024's *Notice of Changes to the State Audit Rule*

During our review of the Notice of Changes to the State Audit Rule, we noted that the State Auditor's Office is proposing the following amendment; "amend and shortens the auditor rotation rule from eight (8) to six (6) years". We would like to provide our viewpoint and comment on this proposed change.

Changing the Rotation Rule from an 8-year Interval to a 6-year Interval will Contribute to the Following Adverse Issues

Our agency had a turnover in our CFO position 5 years ago and we believe the established working relationship that was in place with our auditor lowered the risk associated with first year audits. Having the same auditor for several years has streamlined the process to complete the audit in a timely manor because they are familiar with our agencies practices and the working relationship to complete our audit has enabled our agency to have our audit submitted on or before the deadline.

We are concerned that if this rule were to change it would cause the yearly cost of our audit's to go up because of the increased work it would take to review and audit our agency by being a first time auditor for our agency. This is not a cost effective rule change for our State because it would be Statewide and therefore be more costly for the citizens to bear. We need to be fiscally responsible to our constituents and keep the costs level and not increased.

We feel the 8-year Rotation Rule has many advantages both for private auditing firms and State Agencies that need to be reviewed before a decision is made to change to the 6 year audit rule.

We thank you for the opportunity to submit a comment regarding this matter.

Sincerely,

Dianna Luce
Fifth Judicial District Attorney

Diana Switzer
Diana Switzer
CFO/Financial Manager

LEA COUNTY
313 E. Central Ave, Suite 203
Lovington, NM 88260
Phone: 575-397-2471
Fax: 575-397-6484

EDDY COUNTY
102 N. Canal Street, Suite 200
Carlsbad, NM 88220-5750
Phone: 575-885-8822
Fax: 575-887-3516

CHAVES COUNTY
400 N. Virginia Avenue, Suite G-2
Roswell, NM 88201-6222
Phone: 575-622-4121
Fax: 575-622-4126

Exhibit 10

February 21, 2024

Joseph M. Maestas, P.E., State Auditor
State of New Mexico, Office of the State Auditor
2540 Camino Edward Ortiz, Suite A,
Santa Fe, New Mexico 87507

Re: Request for Public Comment on 2024's *Notice of Changes to the State Audit Rule*

During our review of the Notice of Changes to the State Audit Rule, we noted that the State Auditor's Office is proposing the following amendment; "amend and shortens the auditor rotation rule from eight (8) to six (6) years". We would like to provide our viewpoint and comment on this proposed change.

Changing the Rotation Rule from an 8-year Interval to a 6-year Interval will Contribute to the Following Adverse Issues

- Lower quality audits — Shorter rotation rules increase the risks associated with first-year audits. Auditors adhere to rigorous standards and the transition period during the initial year will pose additional challenges. With a shorter rotation period, the frequency of first-year audits will increase and audit firms will have more first year engagements in their total book of business. Therefore, firms will be required to do more work in the same amount of time due to state audit rule deadlines. This will put pressure on audit firms and incentivize lower quality audit work.

- Increase in late audits — The increase in workload by both the Agency and audit firms will not only increase the likelihood of substandard audits due to the learning curve involved but will prolong the audit process, heightening the risk of delays, regulatory penalties, and erosion of stakeholder confidence.

- Higher costs — Initial procedures to "understand the entity" such as gaining information about its systems and processes require more time and effort. This extra time by the Agencies to provide information and extra time for the Audit Firm to document the information, translates into higher costs. These initial costs are usually considered to be investments by the audit firm. Shortening the rotation rule will result in firms having to pass on the costs to the Agency.

Maintaining the 8-year Rotation Rule will Continue the Following Advantages

- Stability fostering audit quality — A longer tenure, yet there is still rotation, will allow auditors to develop a solid understanding of the organization's intricacies, fostering stability and continuity, essential for maintaining audit quality. Economically, continuing the 8-year rotation period proves advantageous, for both the auditor and Agency, as it curtails the initial start-up costs associated with new auditors acquainting themselves with the organization. This move towards cost efficiency is particularly crucial given the resource-intensive nature of audits, on both the auditor and the Agency.

- Timely audits — Finally, fewer first-year audits will lower the risk of late audits. Late audits can have serious implications, including regulatory penalties and a loss of stakeholder confidence. By continuing the existing 8-year rotation period, the frequency of higher-risk first-year audits is reduced, thereby enhancing the overall reliability and timeliness of the audit process.

Mitigating Risks and Ensuring Quality and Independence

There have been some strong arguments for rotation of audit firms, which are motivated by the public's desire for high quality independent audits. The fundamental arguments are:

1. Extended auditor tenure encourages complacency between the audit firm and the Agency, thereby diminishing the independence, objectivity, and professional skepticism of the audit team.

    - This risk is mitigated by robust oversight mechanisms such as the Office of the State Auditor's workpaper and report reviews and Department of Finance and Administration's report reviews. These measures, along with rigorous auditor independence standards, ensure that audit quality remains uncompromised over time.

- Additional steps can be taken to reduce the risk:
  - Further emphasis on training Agencies in the adoption of internal control best practices, including documentation of these controls so they can be easily referenced by the Agency and their auditors.
  - Further training of Agencies in understanding their responsibilities in overseeing non-attest services, such as cash to accrual conversions and preparation of financial statements and note disclosures.
  - Further emphasis on establishing audit committees that meet directly with auditors.
  - Encourage and incentivize audit firms and Agencies to perform higher quality audits.

2. Higher frequency of rotation will spur competition between audit firms that will improve audit quality.
   - This argument has not been substantiated. On the contrary, higher rotation rules also carry the risk that audit fees will be undercut due to competition, which leads to lower quality audits.

Research Supports the Drawbacks of High Frequency Rotation

Several studies and articles shed light on the drawbacks of frequent auditor rotation and independence.

- A study published in the American Accounting Association Journal '*Auditing: A Journal of Practice and Theory*' found no significant improvement in audit quality in the first year or two following rotations. In fact, some evidence even suggested a decline in audit quality with a new engagement partner, possibly due to a decrease in knowledge about the client.[1]

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[1] https://www.cpapracticeadvisor.com/2020/09/24/should-u-s-broaden-mandate-on-auditor-rotation/40389/ and Kuang, Huan and Li, Huimin and Sherwood, Matthew and Whited, Robert Lowell,

- Opponents of mandatory rotation argue that substandard audits occur more frequently for newer clients because auditors have less information about these organizations[2]. Additionally, newly appointed auditors, concerned with recovering startup costs, may be more easily influenced by the client during the early years of an audit engagement[3].
- A report by the U.S. Government Accountability Office (GAO) found that almost all of the largest public accounting firms and Fortune 1000 publicly traded companies believe that the costs of mandatory audit firm rotation are likely to exceed the benefits.[4]
- A study conducted in 2004 by professors Joseph Carcello and Albert Nagy noted they failed to find evidence that fraudulent financial reporting is more likely given long auditor tenure. They noted their results were consistent with the argument that mandatory audit firm rotation could have adverse effects on audit quality.[5]
- Academic studies also show that the risks to audit quality tend to be higher in the initial one or two years of an engagement and the likelihood of restatements diminish as auditor tenure increases. [6] [7]

Mandatory Audit Partner Rotations and Audit Quality in the United States. Auditing: A Journal of Practice & Theory, 2020, Vol. 39, No. 3, 161-184, Available at SSRN: https://ssrn.com/abstract=4015561

[2] Randal J. Elder, Suzanne Lowensohn, Jacqueline L. Reck; Audit Firm Rotation, Auditor Specialization, and Audit Quality in the Municipal Audit Context. *Journal of Governmental & Nonprofit Accounting* 1 December 2015; 4 (1): 73–100. https://doi.org/10.2308/ogna-51188

[3] https://www.cpapracticeadvisor.com/2020/09/24/should-u-s-broaden-mandate-on-auditor-rotation/40389/

[4] United States Government Accountability Office, Report to the Senate on Committee on Banking, Housing, and Urban Affairs and the House Committee on Financial Services: Required Study on the Potential Effects of Mandatory Audit Firm Rotation, GAO-04-216 (Nov. 2003)

[5] J.V. Carcello & A.L. Nagy, *Audit Firm Tenure and Fraudulent Financial Reporting*. AUDITING: A JOURNAL OF PRACTICE AND THEORY, Vol. 23, Issue 2 (Sept. 2004).

[6] See, e.g., A. Ghosh and D. Moon Auditor Tenure and Perceptions of Audit Quality, THE ACCOUNTING REVIEW, Vol. 8, No. 2. (2005); J. Blouin, B. Grein, & B. Rountree, An Analysis of Forced Auditor Change: The Case of Former Arthur Andersen Clients, THE ACCOUNTING REVIEW, Vol. 82, No. 3 (May 2007).

[7] J. Stanley & F. DeZoort, Audit Firm Tenure and Financial Restatements: An Analysis of Industry Specialization and Fee Effects, JOURNAL OF ACCOUNTING AND PUBLIC POLICY (Mar. 2007).

In conclusion, maintaining the auditor rotation period at 8 years presents a compelling case for enhanced stability, quality, timeliness, and cost efficiency in audits. By continuing the 8-year frequency of rotation, New Mexico's audit system stands to preserve many advantages in its effectiveness and uphold the standards of audit quality. Furthermore, it can explore enhancements in training and oversight, thereby increasing the overall quality of audits.

We thank you for the opportunity to submit a comment regarding this matter.

Hinkle & Landers, P.C.

Hinkle + Landers, P.C.

Exhibit 11

Lea County Finance Dept
100 North Main, Suite 11
Lovington, NM 88260

Phone: (575) 396-8521
Fax: (575) 396-2093

February 26, 2024

Joseph M. Maestas, P.E., State Auditor
State of New Mexico, Office of the State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, New Mexico 87507

RE: Request for Public Comment – 2024 Proposed New Mexico State Audit Rule

During our review of the proposed 2024 Audit Rule, it was noted that the State Auditor is proposing in Section 2.2.2.8(F)(3) to lower the required auditor rotation rule from eight (8) to six (6) years. Lea County has reviewed numerous studies and reports on the benefits and drawbacks associated with required auditor rotation. Our findings are as follows:

Lower Quality Audits - Numerous studies show that more frequent audit rotation generally results in lower quality audits. In his study on frequent auditor switching, Ryan Decker found that "mandated auditor rotation, resulting in more auditor switching, may decrease audit quality and the efficiency of audits by delaying audit opinions" (Decker, 2021). Delays in completing audits could cause many entities to submit late audits resulting in unintended audit findings. The GAO believes that "mandatory audit firm rotation may not be the most efficient way to strengthen auditor independence and improve audit quality" (GAO - Report to the Senate Committee on Banking, November 2003). Some of the concerns noted in most studies was the lack of new auditor familiarity with the client's business and the potential for audit failure during the intial years.

Increased Audit Costs – Decker found in his study "that frequently switching between non-Big 4 auditors is accompanied by higher fees" (Decker, 2021). Numerous other studies reviewed agree that mandatory auditor switching does increase audit costs, but the how and why is subject to discussion. A major portion of the increase can be traced to the extra time and effort that the new auditor has to invest in gaining an understanding of the client. This also increases the cost to the client since they will have to spend more time and effort educating the new auditor and providing the documentation necessary to meet auditing standards.

The AICPA Code of Professional Conduct rule 0.300.050 Objectivity and Independence states that "a member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities" (Accountants, 2014). The rule also requires members to continually assess their client relationships in order to ensure the public that there are no conflicts of interest. In effect, the required adherence to this rule provides the assurance that auditors are maintaining objectivity in performing audits. Therefore, the belief that a longer term auditor client relationship becomes tainted is greatly reduced by the professional conduct of the auditor.

In conclusion, the change in auditor rotation from eight years (8) to six (years) will only result in higher fees and a potential decrease in audit quality. It also has the potential to cause chaos in the first year with many local governments needing to change auditors. Partners with two separate firms have indicated that they will have to replace anywhere from 10-14 audit clients for FY 24. With the number of audit firms willing to do governmental audits decreasing, the potential for serious issues in audit performance and delivery will be the result.

Respectfully submitted,

Chip Low, CPA CGMA
Lea County Finance Director

References

Accountants, A. I. (2014, December). *AICPA professional standards: Code of professional conduct and bylaws as of December 15, 2014.*

Decker, R. (2021). *Retain or Rotate: Outcomes of Frequent Auditor Switching.* University of Arkansas, Fayetteville: Accounting Undergraduate Honors Thesis Retrieved from https://scholarworks.uark.edu/acctuht/47.

GAO - Report to the Senate Committee on Banking, H. a. (November 2003). *Public Accounting Firms - Required Study on the Potential Effects of Mandatory Audit Firm Rotation GAO-04-216.*

From:	Sara Keeler	Exhibit 12
To:	Christopher Hall	
Subject:	Proposed Rulemaking - Auditor Rotation	
Date:	Monday, March 4, 2024 11:12:05 AM	
Importance:	High	

Good Morning, Mr. Hall:

McKinley County is respectfully requesting that the audit rule be left at an 8-year rotation for FY24. FY24 will be our 8th year with our existing auditor and would like to finish our contract with them. If not allowed to do this, we would need 30 days to advertise an RFP and select a new auditor, which may cause us to miss the May 1st, 2024, deadline to submit an audit contract on the osa-connect website. It would, however, be helpful if the change is going to take place, to start with FY25.

Your consideration to our request is greatly appreciated.

Respectfully submitted,

Sara Anne Keeler
NMCPO, NMCPS, NMCPFP
McKinley County
Finance Director
Office: 505.488.7408
Cell: 505.488.8636

Office Hours: 8am to 5pm Monday to Friday

Manning Accounting and Consulting Services, LLC
MACS

Exhibit 13

March 11, 2024

Joseph M. Maestas, P.E., State Auditor
State of New Mexico, Office of the State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, New Mexico 87507

Re: Public Comment on 2024's Notice of Changes to the State Audit Rule

We have reviewed the proposed changes to the 2024 audit rule. As a small firm, we have several issues we would like to raise with the proposed change in the rotation rule from eight (8) years to six (6) years.

- Independence – We can only surmise this change has to do with the appearance of independence of auditors. However, we know of no studies or rulings by oversight boards which would indicate eight years raises independence concerns, as opposed to six years. The Audit Rule over the past 12 years has been ten years, six years, and eight years for audit rotation requirements. Of those, eight years appears to hit the sweet spot for knowledge of a client and performing efficient audits while not being of serious concern for independence. Is there any real issue of independence with conscientious firms at eight years, or is this just a change because we need to change something?
- Planning – We would estimate many firms and clients who are in years six, seven, and eight of audits have already begun the scheduling and planning process, at least if they attempt to have efficient and on-time audits. Our firm already has scheduled dates for prelim and final on-site visits with all our state audits. The clients have booked those dates for us to be on-site. Part of this process is to schedule travel in the most efficient manner with entities in the same area of the state, and this includes entities we would be completing years seven and eight for rotation purposes. Throwing that out in April does not seem wise as some auditor selections are supposed to be made by May 1st to avoid an audit finding.
- Revenue Flow – While some may say this should not be an issue for discussion in such a change, in reality it is. Many firms try to balance out their audits so that there is a logical and systematic alignment with audits and which years they would fall off on the rotation rule so as to not create huge drop-offs. In this case, a firm would not only be losing their audits that completed year eight in the prior year but also years six and seven. As such, instead of losing 1/8 of audits and their revenue, a firm now is losing 3/8 of their audits and revenue. For a small firm, that can be devastating. It is a hit to a larger firm as well, but if both lose those anticipated revenues and are unable to replace them in the current year, adjusting is much harder on the small firm. Large firms normally have a pretty consistent turnover in personnel year-to-year, so they can choose to not fill positions that come open. A small firm like ours that has had no turnover in the past six years and only one position turnover in twelve years has no flexibility with staffing.
- Overloading Schedule – Even if a one-year grace period is allowed for this change, a firm would really have to consider trying to load up on any audits in the current year to offset a three-year drop-

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www.manningacs.com

off in audits in 2025 to survive the revenue drop. This would tend to create the potential for rushed audits and/or late audits, neither of which would be in the best interest of the client or the state.

- Agreed-upon Procedures (AUP) – While this change would cause significant issues with all the agencies being audited, we believe it would be even worse for those entities required to get AUPs. There are already a limited number of firms that find it worthwhile to perform AUPs, which provides limited options for these entities. Many of these entities have volunteers who are responsible for getting their auditor selection process done. Additionally, the Department of Finance Authority – Local Government Division (DFA-LGD) has just required a significant change in the budgeting and reporting process for these small entities which has frustrated their volunteers and has caused some to quit as treasurers. This is not a good time to put additional stress on entities which the State Auditor's Office has struggled to keep current with their audits and AUPs.

We hope that the Office of the State Auditor consider the issues we have raised with the proposed change of the audit rotation rule from eight years to six years.

We thank you for this opportunity to comment on these proposed changes.

Manning Accounting and Consulting Services, LLC

Manning Accounting and Consulting Services, LLC

Exhibit 14

May 15, 2024

Joseph M. Maestas, P.E., State Auditor
State of New Mexico, Office of the State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, New Mexico 87507

Re: Public Comment on 2024's Notice of Changes to the State Audit Rule

We have reviewed the proposed changes to the 2024 audit rule. As a small firm, we have several issues we would like to raise with the proposed change in the rotation rule from eight (8) years to six (6) years. We sent a previous response dated March 11, 2024 of which we still believe are relevant and have not been addressed.

After the Office of the State Auditor (OSA) received many responses regarding this change, all of which appeared to be opposed to the change, the OSA cancelled the hearing and stated that "the auditor rotation rule will not change this year, and any succeeding changes to the audit rule will contain transition information to ensure entities have sufficient time to make any changes." The OSA then released a new proposal for this rotation rule change on April 23, 2024, with no real significant changes to the rule previously proposed. We will provide additional responses to this proposed change, which we do oppose.

The supposed "transition rule" is not a legitimate transition. We specialize in school district audits with a secondary concentration in audits/AUPs related to domestic water/ditch associations. School districts have to make their selections by May 1 of each year. The OSA came out with a proposed rule change one week prior to when districts had to make their selections. The bidding process was over by that time. Therefore, no auditor could make adjustments to their audit load or now go out and try to get additional audits because the OSA is going to arbitrarily reject audits that were already in the revenue stream projections for 2025 and 2026.

The proposed transition rule spoke of "four-year cycles." There are no four-year audit proposals. While the rule allows for eight years, all of the OSA language and information reported to the OSA is still based upon three-year cycles, which is what school districts still bid. By waiting until entities already had to be in the completion phase of their selection process for the current year, the OSA also prevented them from doing a new two- to four-year proposal (since it appears the OSA would have been fine with a four-year proposal) which would have allowed them to maintain the audit firms they had and wanted to maintain until the end of the current eight-year cycle. Many entities would have done this had this proposed rule change been proposed in early March instead of late April. As such, the OSA did not allow a true transition for those in three-year cycles, the normal cycle for audits.

This change, if enacted, could be devastating for our firm, and potentially other firms in our situation. Under the eight-year rotation rule, we anticipated losing 4.9% of our current school district revenue in 2025, 7.2% in 2026, and 26.8% in 2027, which is when each of those districts would hit eight years. We would now lose 38.8% of this revenue next year. There is also an additional 28.5% of revenue that is back out to bid in the three-year cycle next year, meaning we could lose over two-thirds of our primary governmental revenue in one year. We moved from a managed transition to a cliff.

No sane business owner is going to put themself in this type of a situation voluntarily. What would the OSA look at doing if the legislature indicated they were considering cutting your funding by two-thirds?

As the owner of a small firm, it appears that governing agencies we are subject to – AICPA, GASB, and now the OSA – are doing everything in their powers to see that small accounting firms are pushed out of the governmental accounting area. The State has experienced a significant consolidation of firms in the past ten years. We believe this is just going to help accelerate this consolidation.

Let's look at what that consolidation looks like between 2014 and 2023.

2014 State Audit Information					
Classification	# of Firms	Audits Performed	% of Audits	$ Value of Audits	% of $ Value
KPMG	1	2	0.4%	$1,237,630	6.4%
21+ Audits	6	186	38.8%	$11,312,338	58.1%
11-20 Audits	7	92	19.2%	$2,179,450	11.2%
6-10 Audits	17	130	27.1%	$3,182,564	16.3%
1-5 Audits	30	69	14.4%	$1,569,489	8.1%
Totals	61	479	100.0%	$19,481,471	100.0%

2023 State Audit Information					
Classification	# of Firms	Audits Performed	% of Audits	$ Value of Audits	% of $ Value
KPMG	1	1	0.2%	$1,204,645	5.0%
REDW, LLC	1	2	0.4%	$539,303	2.2%
21+ Audits	12	346	71.0%	$19,251,200	79.1%
11-20 Audits	3	49	10.1%	$1,167,313	4.8%
6-10 Audits	6	49	10.1%	$1,027,820	4.2%
1-5 Audits	12	40	8.2%	$1,144,875	4.7%
Totals	35	487	100.0%	$24,335,156	100.0%

In 2014, there were 72 approved audit firms of which 61 did audits. In 2023, there were 54 approved audit firms of which only 35 did audits. The number of audits and the value of those audits has increased significantly in those nine years at the top.

Small firms are being pushed out. In 2014, 47 firms did 10 or fewer audits which accounted for 41.5% of the audits and 24.4% of the value of those audits. In 2023, only 18 firms did 10 or fewer audits which accounted for 18.3% of the audits and only 8.9% of the value of those audits. At the same time, firms doing 21 plus audits, or a few specialized large audits, went from 7 firms performing 39.2% of the audits and 64.5% of the value of the audits to 14 firms doing 71.6% of the audits and 86.3% of the value of those audits.

In 2014, the audit rotation rule was 12 years for audits of $60,000 or less (421 audits) and 6 years for audits over $60,000 (58 audits). In 2023, the rotation rule was eight years, and now you are proposing going down to six years with an abrupt change in how audits would be grandfathered for the previous eight-year cycle. While you may not agree, we do believe this will lead to additional consolidation.

Our firm must now seriously consider transitioning a large portion of our time to non-profit audits. We do a few audits in this area but have declined many opportunities to do other non-profit audits as we prefer where we have concentrated our time with school district audits. Our five-member on-site audit team has hundreds of combined school district audits under our belts, not something most audit teams can claim. However, we're not sure that really matters now.

We have heard no good explanation as to why the OSA believes that a six-year rotation rule is needed over the current eight-year rotation (twelve years was probably too long and six years is probably too short for a mandate). It can't really be justified on independence issues because that isn't an issue at eight years. Even the Sarbanes-Oxley rotation rules only require audit partners to rotate at seven years, not firms, for companies subject to the Securities and Exchange Commission.

A short rotation rule history: In 2014, the rule was the aforementioned twelve-year or six-year cycle depending on value. In 2016, this changed to a straight six-year cycle with a transition which gave until 2018 to complete. In 2021, the rotation rule was changed to the current eight-year rule. Now, in 2024 the OSA is proposing going back to the six-year rule. Four different rotation rules in an eight-year period does not instill confidence in the decision process at the OSA.

Being blunt, this seems to be one of three things; 1) it's political; we change personnel in the OSA and they must put their stamp on the Audit Rule; 2) making abrupt changes, especially downward in the rotation rule, seems to lead to further consolidation so the OSA has to deal with fewer firms; 3) or it's as simple as "because we can".

We hope that the Office of the State Auditor consider the issues we have raised with the proposed change of the audit rotation rule from eight years to six years.

We thank you for this opportunity to comment on these proposed changes.

Manning Accounting and Consulting Services, LLC

Manning Accounting and Consulting Services, LLC

Exhibit 15

From: Michael Vigil Sr.
To: Christopher Hall
Subject: Proposed Audit Rule comments
Date: Friday, March 8, 2024 12:51:23 PM

Good morning Mr. Hall,

I would first like to introduce myself to you. I was a NM licensed CPA until September 2023 when I retired and chose not to renew my license. However, I spent most of my professional career working with public school districts and charter schools. I was the CFO of the Albuquerque Public School District from 1992 to 2006. I formed a financial management firm afterwards to serve small school districts and public charters. My son continues this business.

I wanted to comment on an item the audit rule proposes to change. The 8 year rotation came about because many of the audited entities have difficulty finding firms willing to conduct the audit. Shortening the rotation may seem appropriate but only if you are able to find a new firm. Firms also take the first couple of years building their permanent files and knowledge of the audited entity so that they can adequately identify and address audit issues. Independence issues are addressed through many accountancy regulations and guidelines and should not impact an audit. Rotating the auditor on a shorter timeline will only reduce the efficiency of the audit process.

I would like to specifically like to address the rotation for larger entities. Because of the complexity and scope of a large entity audit, there are few firms that can or will audit these entities. Examples of these entities include the NM Public Education Department and Albuquerque Public Schools. Currently, the firm auditing APS uses many out of state auditors to do much of the work out of state. This is brought up to demonstrate that the large entities have the choice of using one of the few larger firms or a consortium of firms that may bid together. We have experienced the consortium approach with the NM PED audit in the past and that experience was not good. Differences in the various firms audit processes confused the audit. Working with the different component units under the audit allowed me to see the different audit approaches used and the problems caused. If the Office of the State Auditor wishes to reduce the audit rotation time, I request that large entities be identified and allowed to maintain the 8 year rotation.

As a former CFO, I appreciated the audit to identify areas of internal control weakness and areas in need of improvement. However, because of changes to the State Auditor rule auditor rule, we receive findings that, in my opinion, should not be on the audit report. Realize that school district's issue bonds and other financings and their audited financials are read by the bond investors. These minimal findings should not be included with audited financials. I would suggest the state audit rule require a management report of other issues that would include these findings. The findings I am referring to include many of the "Other Matter" findings. We have seen findings issued for under calculating a travel per diem by $1.60; one auditor cited a deposit not made within 24 hours missing the deadline by 2 hours; procurement issues when entities searched for 3 or more quotes but because of supply chain issues only received 2 (the auditor would not accept a not available as a quote).

As I stated above, I am retired but feel it is important to bring real value to the audit process. I believe the above will add value to the audits under your jurisdiction.

Thank you for your consideration. I can be reached at this email or on my cell phone at 505-263-4269.

Michael J Vigil
michael@vigilgroup.net
505-263-4269

Exhibit 16

The Education Trust Board of New Mexico

THE HONORABLE MICHELLE LUJAN GRISHAM
GOVERNOR OF NEW MEXICO

STEPHANIE RODRIGUEZ
CABINET SECRETARY
NEW MEXICO HIGHER EDUCATION DEPARTMENT

BOARD MEMBERS
GARY L. GORDON, CHAIR
ROBERT J. DESIDERIO, VICE CHAIR
LAWTON DAVIS
MONT GREEN
CHAMIZA PACHECO DE ALAS

EXECUTIVE DIRECTOR
NATALIE CORDOVA

March 13, 2024

The Honorable Joseph M. Maestas, P.E., CFE, New Mexico State Auditor
The New Mexico Office of the State Auditor
2540 Camino Edward Ortiz, Suite A,
Santa Fe, NM 87507

Re: Request for Public Comment on 2024's Notice of Changes to the State Audit Rule

During our review of the Notice of Changes to the State Audit Rule, we noted that the State Auditor's Office is proposing the following amendment in Section 2.2.2.8(F)(3) to amend and shorten the auditor rotation rule from eight (8) to six (6) years. We appreciate this opportunity to provide input on this proposed change.

Having a "rotation rule" contradicts and interrupts the natural selection process by agencies. This proposed limitation eliminates otherwise eligible firms that may be able to provide the audit services, at times specialized in certain audit and financial areas. By imposing such a rule, and in the current proposed rule a more restrictive time period, it works against the intent of the best firm being selected to provide audit services.

As you are likely aware, the firms approved to perform audits under this rule are limited in availability and, at times, limited in specialized areas of expertise. The Education Trust Board (ETB) oversees more than $2 Billion in fiduciary assets/investments. The annual audit of ETB requires specific audit expertise. Only one firm responded for the prior audit RFP. If the one firm that responded is eliminated by no other criteria than this rule – we fear there will not be a qualified firm available to perform such services.

Additionally, though eight (8) years is also an arbitrary unnecessary limit – it at least allows for alignment with the state's 4-year Request For Proposal (RFP) period. The proposed six (6) year limit creates additional administrative effort on the agency, oversight agencies and approved audit firms, without any benefit in return.

Existing professional audit standards guide auditors and firms regarding independence. The proposed rule provides no benefit, and rather, wastes time, effort and precious resources of agency personnel. Further, the audit rule already includes safeguards that allows the Office of the State Auditor (OSA) to review and oversee its approved audit firms. Should there be a specific concern of the years of audit in which a firm is engaged with a specific client, the OSA maintains authority and control to review such concerns outside of the arbitrary rotation rule.

I respectfully request your full consideration that the current length of rotation rule (8 years) not be modified as proposed. Further evaluation of the benefit of a rotation rule should be considered.

Sincerely,

Natalie Cordova

Executive Director and CFO, NM Education Trust Board

State of New Mexico
STATE INVESTMENT COUNCIL
41 Plaza La Prensa
Santa Fe, New Mexico 87507
Phone: (505) 476-9500
Fax: (505) 424-2510

Exhibit 17

March 6, 2024

Joseph M. Maestas, P.E., State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, New Mexico 87507

Re: Request for Public Comment on 2024's Notice of Changes to the State Auditor Rule

Dear State Auditor Maestas:

I have reviewed the changes to the State Audit Rule proposing the following amendment; "amend and shortens the auditor rotation rule from eight (8) to six (6) years." As the CFO of the New Mexico State Investment Council for the past twelve years, I would like to share the following comments which I hope will be helpful.

During the last RFP process for external audit services in early 2021, the proposal requirements were lengthened from 3 years to 4 years based upon the auditor rotation requirements being changed from six (6) to eight (8) years. Now we are potentially going back to the original six (6) years without any recognition that we have received a proposal in 2021 for a 7th year, which is for fiscal year 2024.

My biggest concern is that during and subsequent to the pandemic there appears to be challenges within state government and the accounting profession, in general, to maintain adequate staffing for accounting positions. The fact that our beautiful state is so large and spread out doesn't help. Going back to the six (6) year rotation requirement is potentially going to add more uncertainty to an already difficult situation which will likely increase risk and potentially cause delays while costing more. This is especially true during the earlier years of a new auditor relationship.

I would also raise the question of whether there is any evidence that reducing the rotation requirement, as recommended, reduces risk? Being in the accounting profession for over 40 years, I am not aware of such a study. In fact, most studies prove that the opposite is true.

Your consideration of my comments is greatly appreciated.

Respectfully submitted,

Brent H. Shipp, CPA, CFA, CAIA
Chief Financial Officer

Exhibit 18

From: JB Mauldin
To: Christopher Hall
Subject: Seventh Judicial District Attorney Office"s Viewpoint Regarding OSA"s 2024 Proposed Auditor Rotation Rule Change
Date: Thursday, March 7, 2024 9:26:39 AM

Good Morning Mr. Hall,

We would like to provide our viewpoint regarding changing the auditor rotation rule from eight years to six years.

We are a small agency that is located outside of any metropolitan area. This presents a serious challenge in obtaining audit firms that are willing and able to perform our annual audit. When we have solicited firms in the past we have received very little response from approved audit firms. Also, audit firms that have done our agency's audit previously are no longer on the list so our list of possible interested firms is even less than it once was.

In addition to the challenges of obtaining an audit firm to begin with, rotating to a new firm more often will also lead to more expensive audits as each new auditor will have a higher workload in the first and second years to familiarize themselves with each agency's operations. This could also lead to lower quality audits due to lack of resources and meeting deadlines.

We believe that higher quality audits are performed as the audit firm understands each agency's operations and this can only happen after numerous audit years have been completed.

So in summary, we are opposed to shortening the auditor rotation rule and believe it will adversely affect our agency. We appreciate your time and consideration on this matter.

Sincerely,

J.B. Mauldin
Chief Financial Officer
Seventh Judicial District Attorney's Office
PO Box 1099
Socorro, NM 87801
Ph. (575)835-0052

Exhibit 19

From: rp@swascpa.com
To: Christopher Hall
Subject: Audit Rotation Rule
Date: Wednesday, March 6, 2024 9:17:29 AM

Christopher,

I comment I would like to make is if the OSA is going to change the audit rotation rule form six years to eight years this places an additional pull on resources from our firms and as you know our industry is currently being stress tested. I also understand why your office would like to make this change. I would suggest if the OSA makes this change they do it next year and announce now that the change will be coming in fiscal year 2024 so we have time to regear our resources.

At the end of the day whatever your office decides we will do our very best to make it work.

Sincerely

Robert Peixotto, CPA Managing Member
Southwest Accounting Solutions, LLC
Phone: 505-610-4455
6000 Uptown Blvd Suite 490
Albuquerque, New Mexico 87110

TKM Auditors Advisors CPAs

Exhibit 20

March 5, 2024

Joseph M. Maestas, P.E., CFE
New Mexico State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, New Mexico 87507

RE: Request for Public Comment – 2024 Proposed New Mexico State Audit Rule

Dear State Auditor Maestas,

I hope this letter finds you well. My name is Daniel O. Trujillo, CPA, CFE, CGFM, CGMA, and I am writing to you in my capacity as Managing Partner of TKM, LLC (Formerly Kubiak Melton & Associates, LLC), a New Mexico CPA firm based in Albuquerque. Our firm has closely reviewed the proposed 2024 Audit Rule and would like to formally submit our public comment.

Upon our review of the proposed 2024 Audit Rule 2.2.2 NMAC, we identified a proposed change to 2.2.2.8(3) NMAC – *Auditor Rotation Rule* that will put undue burden on New Mexico state agencies, local public bodies, other New Mexico governments, and IPAs that fall under your purview. Specifically, changing mandatory auditor rotation from eight (8) years down to six (6) years. While we understand the intention behind this proposal—to ensure freshness in perspective—there are several challenges and implications that we believe warrant careful consideration. We are concerned that this change might inadvertently affect both the governmental entities we serve and the auditing profession in several ways:

1. **Learning Curve and Efficiency:** The initial years of an auditor's engagement with an entity involve a steep learning curve as the auditor acquires an in-depth understanding of the entity's operations, systems, and processes. Reducing the rotation period could mean that just as an auditor becomes fully efficient and deeply familiar with the entity, it would soon be time to rotate, potentially impacting the quality of audits due to a shortened period of peak efficiency.

2. **Cost Implications for New Mexico Governments:** Changing auditors more frequently could lead to increased costs for entities, particularly smaller ones, due to the initial higher investment needed when a new auditor takes over to understand the operations and its specific challenges. These costs may not be just financial but also in terms of time and resources devoted to onboarding new auditors.

3. **Audit Quality and Continuity:** A shorter rotation period could impact the continuity and quality of audits. Long-term relationships, underpinned by a deep understanding of the government's operations and its nuances, can enhance the quality of the audit through insights gained over time. Frequent changes might disrupt this continuity, potentially affecting audit quality.

4. **Market Concentration Concerns:** A shorter rotation period could unintentionally exacerbate market concentration issues in the New Mexico audit profession, as entities might gravitate towards larger audit firms perceived to be more capable of managing frequent transitions, potentially disadvantaging smaller audit firms.

www.tkm.cpa (505) 822 5100 (505) 822 5106

6747 Academy Road NE, STE A, Albuquerque, NM 87109

5. **Increase in Late Audits:** As the challenges discussed above amass, we believe that this change to the Audit Rule will create an unintended whirlwind of late audits. With late audits – taxpayers, legislators, funders, and stakeholders will lose faith in various New Mexico government's transparency and accountability.

6. **Undue Burden of More Frequent Procurement:** New Mexico procurement laws allow multi-term contracts up to four (4) years (*New Mexico Statutes 13-1-150. Multi-term contracts; specified period*). Under the current eight (8) year rotation rule, governments can do two-four years contracts with their auditors, which commonly occurs. If the rotation is changed to six (6) years, the entity will have to do more frequent procurements which can be demanding for smaller government entities with less resources. It also would require the IPAs to bid on contracts more frequently which only one can win- as we know they are not compensated for the time and effort put in to that endeavor, only if they are awarded the contract.

Instead of decreasing the mandatory audit rotation timeframe, we would suggest exploring additional mechanisms to enhance audit quality and integrity, such as increased oversight, professional development, and best practice sharing, which could complement the rotation policy without necessitating a shorter rotation period.

In conclusion, we would strongly advise against the change to move the audit rotation from eight (8) years to six (6) years. From our experience when Former Auditor Keller moved the audit rotation to six (6) years, we experienced many unintended consequences it caused as outlined in this letter. Let us learn from what hasn't worked for previous State Auditors and commit to the eight (8) rotation which has produced the best results for New Mexico government's accountability and transparency.

Thank you for considering our perspective on this important issue. We look forward to the opportunity to discuss this further.

Very truly yours,

Daniel O. Trujillo

Daniel O. Trujillo, CPA, CFE, CGFM, CGMA

Managing Partner

Exhibit 21

TAXATION & REVENUE
NEW MEXICO

STATE OF NEW MEXICO
Taxation and Revenue Department

Michelle Lujan Grisham
Governor

Stephanie Schardin Clarke
Cabinet Secretary

Tax Information & Policy Office

Office of the Secretary
1100 S. St. Francis Dr.
Santa Fe, NM 87505
Phone: (505) 827-0341
Fax: (505) 827-0331

April 29, 2024

Christopher Hall
Office of the State Auditor
Christopher.Hall@osa.nm.gov

Dear Mr. Hall:

The Taxation and Revenue Department wanted to provide a brief written comment in response to your Notice of Proposed Rulemaking and Public Hearing. One of the amendments to Regulation 2.2.2.8 NMAC, subsection H paragraph (2), strikes "CRS", but retains mention of the combined reporting system number. Effective July 1, 2021, the Department deployed a redesign which retired the combined reporting system. The number issued to businesses from that point forward is known as the New Mexico business tax identification number (NMBTIN). We wanted to make sure you had this information prior to finalizing the amendments.

Sincerely,

Alicia Romero

Alicia Romero
Tax Information and Policy Office Manager
Alicia.Romero@tax.nm.gov

Exhibit 22

CliftonLarsonAllen LLP
6501 Americas Parkway Northeast, Suite 500
Albuquerque, NM 87110

phone 505-842-8290 **fax** 505-842-1568
claconnect.com

March 12, 2024

Joseph M. Maestas, P.E., CFE
New Mexico State Auditor
2540 Camino Edward Ortiz, Suite A
Santa Fe, New Mexico 87507

Via email: christopher.hall@osa.nm.gov

We appreciate the opportunity to submit these comments. Below are our proposed amendments and requests for clarification regarding the draft Audit Rule.

2.2.2.7 Definitions

1. We noticed that various acronyms removed from the definitions that are still in use throughout the rule. There should be additional consideration to add some acronyms or whether the remainder of the rule should be reviewed to omit references to acronyms no longer defined.

2.2.2.8 F (3)/2.2.28 G (1) (b) Audit Rule Rotation

CLA opposes the proposed changes to the Auditor Rotation Rule under 2.2.2.8 F (3)/2.2.28 G (1) (b) from 8 years to 6 years. We respectfully request that this proposed change be reconsidered. CLA believes that this change would have negative implications, primarily including an increased risk of untimely audits and increased audit fees for entities. Some examples of the factors that would have negative implications include the following:

- There are numerous entities in which their FY23 audit was their 6th or 7th consecutive year with their auditor and may have already been in process of planning on using their existing auditor for the next 1-2 years to complete the 8 year period. This change would trigger an immediate rotation.

- A proposed rule change issued in February 2024, with a possible April 2024 finalization, will cause a significant compression of the procurement process in FY24. This will add an additional administrative burden to numerous entities, in which many are already facing staffing shortages. In addition, this will put more entities at risk of untimely audits due to the untimely and/or unplanned procurement process.

- The ability to remain consistent with IPA helps with the knowledge transfer and audit efficiencies. Lack of continuity of personnel at a government does not allow for efficiencies. More frequent auditor rotations will increase audit costs. Additional time and effort are needed for a first-year audit engagement due to the learning curve. Efficiencies are built with learned knowledge, over time.

- The change in the rotation rule will increase the frequency of the issuance of RFPs, which will impact both the entities and the IPAs. For the entities, the procurement process is an involved process that requires more resources of that entity, that is unnecessary when the current procurement allows a 4-year period on professional services. For the IPAs, responding to an RFP is a time-consuming process in which we prepare numerous proposals in the March-April timeframe. The increase in RFPs because of change in the rotation rule will place an additional burden on IPAs, which will be one of the factors to consider when evaluating which RFPs we respond to. This could contribute to a lack of competitiveness and increased costs for the entities.

- The RFP process delays the timing of a fully executed contract, which does not allow the performance of interim/preliminary work until after the end of the fiscal year. The ability to perform interim/preliminary, prior to July 1, is essential for timely submissions of audit reports. More frequently issued RFPs will result in more audits being started in July or later, increasing the risk of an untimely audit.

- In addition, as drafted, it is not clear as to what services are referenced under this rule/section.

CLA has evaluated and discussed this proposed change with internal and external stakeholders and has not identified any positive outcomes or benefits with this change. Instead, CLA believes that this change would create an environment that is less attractive to IPAs and would increase the administrative burden on state and local government entities in the state.

Therefore, CLA respectively requests that the Office of the State Auditor defer any modification to the auditor rotation rule at this time and consider connecting with various stakeholders to evaluate the implications of a proposed change.

2.2.2.10 J. (21) The New Mexico opioid allocation agreement

1. Please elaborate the compliance expectations. There is more than one agreement that includes an allocation to NM.

CliftonLarsonAllen LLP

Matt Bone, CPA, CGFM, CGMA
Managing Principal – New Mexico

Laura Beltran-Schmitz, CPA, CFE, CGFM, CICA
Principal

Exhibit 23

From: Peery-Galon, Renada, ERB
To: Christopher Hall
Subject: RE: [EXTERNAL] RE: 2024 State Audit Rule Changes
Date: Thursday, February 15, 2024 11:33:27 AM
Attachments: image002.png
2.2.2 NMAC Requirements for Contracting and Conducting Audits of Agencies.pdf

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Good morning Christopher,

The proposed change is to 2.2.2.10. Y. GASB 68, accounting and financial reporting for pensions (1) (f).

With markups:

(f) PERA and ERB shall each prepare an employer guide that illustrates **the use of their respective schedule of employer allocations report to create journal entries generally required by GASBS 68.**~~the correct use of their respective schedule of employer allocations report by their participant employers. The guides shall explicitly distinguish between the plan-level reporting and any employer-specific items.~~ The calculations ~~and record-keeping necessary~~ at the employer level (for adjusting journal entries, amortization of deferred amounts, etc.) shall be described and illustrated. The employer guides shall be made available to the participant employers by June 30 of the subsequent fiscal **year**. Stand-alone state agency financial statements that exclude the proportionate share of the collective net pension liability of the state of New Mexico shall include note disclosure referring the reader to the statewide comprehensive annual financial report for the state's net pension liability and other pension-related information.

Without markups:

(f) PERA and ERB shall each prepare an employer guide that illustrates the use of their respective schedule of employer allocations report to create journal entries generally required by GASBS 68. The calculations at the employer level (for adjusting journal entries, amortization of deferred amounts, etc.) shall be described and illustrated. The employer guides shall be made available to the participant employers by June 30 of the subsequent fiscal year. Stand-alone state agency financial statements that exclude the proportionate share of the collective net pension liability of the state of New Mexico shall include note disclosure referring the reader to the statewide comprehensive annual financial report for the state's net pension liability and other pension-related information.

This part of State Audit Rule was put in place at the implementation of GASB 68 in 2015. We are now 9 audit years into GASB 68, and the employer guide is mainly utilized for creating journal entries required by GASB 68. I worked with PERA on the proposed changes, and I know that they also want to request these changes to State Audit Rule. Should I let Lynette Kennard, PERA CFO, know to submit the proposed State Audit Rule changes to you?

Thank you for your assistance!

New Mexico
Department *of* Finance
and Administration

407 Galisteo St,
Santa Fe, NM 87501
(505) 827-4985

Cabinet Secretary Wayne Propst
Deputy Cabinet Secretary Renee Ward
Acting State Controller Mark Melhoff

Governor Michelle Lujan Grisham

Exhibit 24

To: Joseph Maestas, *State Auditor*
New Mexico Office of the State Auditor
Joseph.Maestas@osa.nm.gov

From: Mark Melhoff, *Acting Controller*, Financial Control Division
New Mexico Department of Finance and Administration

Date: March 7, 2024

RE: PUBLIC COMMENT REGARDING 2024 PROPOSED CHANGES TO THE NEW MEXICO STATE AUDIT RULE

This memorandum shall serve as public comment by the Financial Control Division ("FCD") of the Department of Finance and Administration ("DFA") regarding proposed changes to the 2024 Audit Rules under the New Mexico Administrative Code ("NMAC"). The FCD's public comments are as follows.

The FCD strongly opposes proposed changes to the Auditor Rotation Rule under NMAC 2.2.2.8.F.3

The FCD opposes proposed changes to the NMAC 2.2.2.8.F.3, which change the auditor rotation period from eight years to six years. The proposed rule change is concerning for the following reasons:

1. **Inconsistencies.** A six-year cycle will cause inconsistencies between the audit contracting process and the state procurement code. Under NMSA (1978) § 13-1-150, service contracts are limited to four years, including all extensions and renewals. When compared to an eight-year cycle, a six-year cycle would require an additional request for proposal, resulting in increased administrative costs and a burden for all state entities.

2. **Unclear Implementation Date.** In the year of implementation, state agencies hitting the six-year maximum would be required to issue a new request for proposal ("RFP"). If the audit rule becomes effective in April without some type of future implementation date, state agencies may not have adequate time to complete an RFP by July 1st. This would lead to delays in agency audits as well as delays for the state's ACFR.

3. **Potential Audit Issues.** In recent years, the state has seen a steady decline in the number of firms that can perform agency audits. Decreasing the rotation period could have a potential impact on the number of available firms willing to engage in state agency audits.

The FCD proposes changes to the report due dates under NMAC 2.2.2.9.A.1.C

Under NMAC 2.2.2.9.A.1.C, the due date for the DFA agency audit is November 1st. The FCD proposes changing the date for DFA-341 to November 15th for the following reasons. First, the DFA houses the Board of Finance severance tax bond ("STB") Capital Outlay program, which provides funds for all legislatively approved STB capital outlay projects statewide. Many due dates for state agencies have been, or are being, pushed back. Further push back results in challenges for the DFA because the DFA must complete the DFA's audit by November 1st while also depending on state agencies to timely perform reconciliation and close out of prior year activity. If due dates continue to be extended, then the DFA recommends increasing the time for only the DFA.

The State Controller's Office of the DFA proposes additional notice requirements to the Report Due Dates under NMAC 2.2.2.9.A.5.

The State Controller's Office ("Controller") of the DFA proposes the DFA be added as an agency required to receive notice of when circumstances exist that will make an agency's audit report late. The reason for the proposed change is the DFA is responsible for completing the state's annual comprehensive financial report ("ACFR"). The ACFR is highly dependent on the timely submission of audits by state agencies. However, when a state agency, state entity, or component of the state, submits a late audit, the time required to properly compile the ACFRs is increased. As such, the Controller respectfully requests the DFA, like the state auditor, receive notice of when circumstances exist that will make an agency's audit report late, provided the state entity falls under the purview of the DFA and reports within the ACFR.

The FCD proposes the DFA be added as an agency responsible for engaging in a SOC-2 compliance audit.

Regulations at NMAC 2.2.2.10.S.2 direct the Department of Information Technology ("DoIT") to engage in an SOC-2 compliance audit of the state's Enterprise Resource Planning (ERP) system also known as SHARE on an annual basis. However, under statute at NMSA (1978) § 6-5-2.1 (F), the FCD of the DFA must "prescribe, develop*, operate and maintain* a uniform statewide accounting system network[.]" (Emphasis added). As such, the DFA strongly believes the DFA should be added as an agency responsible for engaging in an SOC-2 compliance audit. This means, the DFA and DOIT will jointly engage in an SOC-2 compliance audit of the SHARE system.

For questions, email the FCD's Acting Controller, Mark Melhoff at marks.melhoff@dfa.nm.gov.

JOSEPH M. MAESTAS, PE, CFE
STATE AUDITOR

RICKY A. BEJARANO, CPA, CGMA
DEPUTY STATE AUDITOR

State of New Mexico
Office of the State Auditor

Exhibit 25

File name: 2024 Audit Rule Hearing- Public Comments Transcribed
Video Length: 51:35
Video date: 5/29/2024

<u>2024 Public Hearing and Commentary on Rule Changes</u>

17:54 OSA: That is the summary of previously submitted comments. Now we are going to get in the meat of today's action, which is the actual public comments. So if I had a gavel I would hit it but since I don't, I will metaphorically gavel this hearing open. And now it's your turn – so if there is anyone here in the room that would like to make a public comment, please raise your hand and we'll run the mic to you. And again, if you're here or online, this is being recorded in lieu of a transcription so please state your name, the agency or firm or your affiliation and you got three minutes to talk.

18:52 Oscar Rodriguez, Chief Financial Officer for the New Mexico Finance Authority: Good morning, can you hear me? Good morning, everyone, Auditor. I'm here to provide my input, I would have done it also online. [OSA: Who are you, Sir?]. My name is Oscar Rodriguez, I am the Chief Financial Officer for the New Mexico Finance Authority. I've been there almost eight years. Prior to that I was the finance director for the city of Santa Fe. Before that I was the town manager in Taos – so I have a lot of experience with the rotation of Auditors. And I can tell you it's certainly convenient to not have to do an RFP go through the whole process to select a new auditor, etc. But I should think a lot of my colleagues here would agree that there is a lot of things in our business that well they are convenient are probably not safe to do. Or at least not the right thing to do. I would say that the rotation that is proposed for six years, in my opinion, is right on the mark. I was at NMFA when change went from six years to seven years. I thought that was just a little odd, having experience with financial control elsewhere in the state. I was also concerned about the auditors becoming too familiar, too comfortable if you will with the systems that they are auditing. Was also concerned with the public view of a system, a set of books that had been audited by the same people for eight years. I think that at some point it rightfully draws attention to are they really finding everything that needs to be found out. And also, I think it helps us establish clearer expectations about rotations. It's going to happen and sometimes the idea that we are going to turn in a good audit. In order to continue the contract, etc – at least that conversation helps us avoid that. I very much support the change in rotation to six years. Mr. Maestas, I came here really to just talk about that, it's a significant thing for me. But when I heard you introduce the idea of a more enduring audit rule – I want to applaud that as well. My god, shouldn't we have an audit rule that everyone can put away and when you need it call on it. As oppose to go online, search which is the most current version, etc and making sure you're making the right interpretations. I applaud that as well. So real clearly, speaking for myself, based on 15/16 years of financial management in NM. I support very much the rotation being brought back to six. I was comfortable with that, Of course I enjoyed not having to do the extra RFP for the eight years. But I am very comfortable with the six years.

22:28 OSA: Anyone else here at the society?

22:37 Brent Shipt, Chief financial officer with the state investment council: Hello, my name is Brent Shipt. I am the Chief financial officer with the state investment council. I know Oscar very well, worked with him on an ongoing basis because of the relationship our entities have together. I did want to take the contrary position that he took. I am very much opposed to going out to eight years based upon research that I have done. I am not aware of any study that would indicate shorting that requirement from eight to six has really any true benefit. You mentioned a few minutes ago just that the pressure the accounting industry is under. This auditor rotation requirement change potentially has negative ramifications and I would just challenge everyone. Go out there and look what really supports this change. I would also raise the question neighboring states, Texas, Colorado, Arizona – what do they do? I think they are closer to ten years. So, I think eight is a pretty good compromise. Six is without a doubt in my mind going in the wrong direction. Just so you know my background, I've been a CPA in NM going on 40 years. If I haven't been auditing, I've been audited by CPA firms. I've kept my license active all these years. Very acquainted with auditors in this room, Moss Adams, CLA, I think they do fine jobs and I am just very much opposed to this change at this point.

24:48 OSA: Seeing no other comments.

25:00 Laura Beltran Schmitz with Clifton Larson Allen CLA: You give me a mic and that could be a little dangerous. Thank you for your time and coming here today. My name is Laura Beltran Schmitz, I'm with Clifton Larson Allen CLA, also pleased to be hearing the state society. Proud member of the board as well and working here with the staff. I appreciate the time, comments, and opening remarks, Auditor regarding the rotation specifically and the concerns over the familiarity bias and that is a great point. It's important for us to also acknowledge we, as IPAs take into consideration are required to document all threats to independence. In addition to familiarity bias, there are additional threats that we are to document and address as part of our internal quality review system. So, this is something we keep in mind when we are performing our audit procedures and going through quality review process. We appreciate that acknowledging exemptions that could be made if there are potentially smaller governments that are unable to get a auditor to submit for their audit. We do know even this year, with the rule still being eight years. There were at least two that we're aware of that had to undergo an exemption from your office and it was appreciated. And they are actually in the metropolitan area. So, I think this is a larger issue than potentially those in rural communities. To the point of familiarity bias, an entity can terminate the relationship with an IPA at any point in the contract. So just because you bid for four years, it doesn't mean you automatically have that contract for four years because we do have to renew our contracts through your office every year. So, if there is that concern, the entity can choose to terminate that relationship or I believe the State auditors office has the opportunity to reject those contracts, if there is that concern that the familiarity bias is approached or even exceeded without thorough documentation of a quality review process. So, thank you for your time.

27:20 OSA: I want to take a second to ask for any other speakers in the room but then also I just got a message that the office is receiving calls that the zoom link isn't working. Perhaps people may have the wrong zoom link. Obviously, some people are on zoom so it must be working for some people. Hope is there any way you can reach out, or Ben can you and hope reach out to Andrea and try to clarify this and see if there is some way to fix this? Thank you. With that, I'm sorry for the interruption. Are there any other people here at this society that would like to. Great, Ill get you the mic.

28:33 Daniel Trujillo, managing partner of TKM IPA: Good morning, State Auditor, your team. We appreciate you all taking time to schedule and reschedule it. I just had a quick comment. My name is Daniel Trujillo, managing partner of TKM IPA. I've been an IPA for seventeen years and the one thing that kind of stuck out to me going through the changes that Mr. Hall was going through is that there was an overwhelming amount of comments against the eight year down to the six year rotation rule from reputable big agencies, small agencies everything in between, IPAs. Although I see where your experience might be due to the familiarity threat might be real and Im sure in some instances it is. I would just encourage to heed those comments, the fact that so many agencies large and small, IPAs who are making them, I think there is probably something there that we should really look at and make sure were really considering before making a change to go down to the six years. I appreciate your time and that's one thing that stuck out during the comments. Thanks.

30:02 OSA: Ms. Zamora.

30:09 Natalie Zamora with the Education Trust Board of New Mexico: Hello. I'm Natalie Zamora with the Education Trust Board of New Mexico. Ms. Cordova our executive director wanted me to say this on her behalf. She noted one of the concerns is that this is an industry norm and doesn't appear to be a need for rotation rule as audit standards already sufficiently address independence. And that's all.

30:35 OSA: Thank you. Anybody else here? Ok. Hope do you want to see if anyone wants to make a comment online? And hopefully we'll get some more people joining us here in a minute. That are online. I would make that announcement right now. Anybody that hears this is already on the zoom call but it's being put on our website. Where again is it going to be? So basically, we posted the zoom link on the front page of our website. So, if there is anyone out there who is on the zoom call who is getting calls from people who aren't able to access it please advise them that our IT director is posting the link on our home page. Basically, where it says 2024 Audit Rulemaking. [NMSCPA: It is the same link for everybody so it should be working. I would recommend trying to shut down and start back up and try and join it again.]

32:16 NMSCPA: Byron Manning – you have your hand raised you may go ahead and state your comment. You will have three minutes. Thank you. Byron, you can go ahead and start with your comment. He may have raised his hand on accident. Ok, Byron, we will come back to you. I'm going to go ahead with the next person. Audrey Jaramillo, you may unmute yourself and state your comment for three minutes. Thank you.

33:16 Audrey Jaramillo, managing partner of JAG: Ok, thank you. Auditor Maestas and those of you, you can hear me, correct? [NMSCPA: Yes.] Ok, perfect. I'm Audrey Jaramillo, managing partner of JAG, Jaramillo Accounting Group and other affiliations and experiences I've had is in governance as an elected official for my local school board for eight years and then on my local town council and commission for six years approximately. I see this from all different angles, but I definitely wanted to state that we are against auditor rotation. We see that the procurement should really line up with the four and four years of professional services. We see the generational shift that everyone sees with turnover and problems happening and sometimes the Auditor is the only consistent variable in the equation. IPAs are really struggling with unqualified clients. For instance, I don't think you'd have your administrative assistant engineer the building you're in. We are seeing it all the time with people that are definitely unqualified in business and finance positions. So that's making it very difficult, and you add rotation into that and I think it's a storm. I think of it also in a doctor analogy, I mean you appreciate your doctor that you get to know maybe a family doctor, they know you, they can best diagnose you, they know your symptoms they know your history. You can always get another opinion if that's necessary. But I think it's even offensive that a doctor would deny his training and professional training in ethics to not give someone news they don't want to hear. Would we say just because an engineer, attorney, or doctor served a client for six years that they wouldn't do a good job that they would tell the client or not tell the client something they need to hear. For most of us, we can't even imagine that. So, it could just be and Auditor I want to be sorry that you had some experiences locally but I do think it could be adjust in other ways and still trust local control. But some alternatives I wanted to offer the 89 schools districts and all the charters have audit committees. These audit committees make recommendations to the boards of who the auditor should be. So that's already a check and balance on the governance if an auditor does need to change. We even have community members on those audit committees. So that could be implemented on a broader basis. I think most of us think it would be a compromise to change the onsite manager have that type of retirement or even change the partner on in charge of the engagement. That would be a good compromise, so to speak. But if there is an unethical auditor or someone who is actually just not following independence standards and having a familiarity bias. Which I'm not even sure what that exactly looks like in this situation that you had. I hope you share it with us so we could help like problem solve. But I think it needs to be addressed with that IPA in the desk reviews that OSA does on the IPA or with the governmental entity itself with governance and alerting governance that you're concerned about a bias or hearing something in a 12-6-6 letter or hearing something on the hotline about fraud or that an auditor isn't reporting something. But most of all of us, we are professionals we hold to our standards. [NMSCPA: Andrea. Andrea. I apologize, I hate to cut you off but your three minutes is up.] Oh, ok. Thank you.

37:29 NMSCPA: If anyone else online would like to make a comment – please raise your hand so I may call on you. Byron, I see that your hand is raised. You may go ahead and unmute, and you have three minutes to say your comment. Byron if you are unable to speak, you can go ahead and put your comment in the chat. Anyone online who would like to make a comment, please raise your hand so that I may call on you. Byron we will check on you again. I'm going to call on Chip Lowe. You may unmute and state your comment. You have three minutes. Thank you.

38:38 Chip Lowe, finance director of Lee county: Yes, thank you. Can you hear me? [NMSCPA: Yes] My name is Chip Lowe, I am the finance director down here in Lee county. Mr. Maestas, I'm not going to discuss, I made my comments about the auditor rotation, and I respect your position on that. I just wanted to say that you said earlier that you were planning on going around the state and doing training on the Audit rule. And I would just like to invite you down to Lee county, we'd be more than happy to host you and hopefully give you a good stay. That's all the comment I got. Thank you.

39:22 NMSCPA: Thank you. Byron, I went ahead and asked on zoom for you to unmute. Please let me know if that works. If it does not work, I recommend jumping off really quickly and jumping right back on.

39:38 Byron Manning from Manning accounting and consulting services: Ok, can you hear me now? [NMSCPA: Yes, we can hear you. Byron you have three minutes to state your comment. Starting now.] Ok. First of all, I was just checking after you had. Again, it's Byron Manning from Manning accounting and consulting services, one of the small firms. After you had rereleased the Audit rule, I had sent in additional comments on it, I didn't see that they were ever posted. So, I just wanted to make sure that you did receive those. [OSA: I believe we read those out earlier.] Well, the ones that are posted were the ones we posted originally back in March when you first did it and then when you made the changes to it, we sent another one commenting on it and that we never saw posted in comment section. So just checking to see if you got it – we kind of gave you statistics on the drops of small firms in ten years. [OSA: copy that Mr. Manning, I will find it and reach out to you if we did not receive it. I'll find out why it hasn't been posted. So, thank you.] Ok, because I sent it to the one who had sent me the email saying that I didn't need to send it again if I didn't want to. So, I responded to his email and attached the comments to it when we did it. We have pointed out, do oppose it. We do feel that as the years have been reduced and this will be the fourth change in eight years the audit rotation rule that the small firms have kind of got squeezed out with it. At the very least coming out as late as it did how you can maintain your seven or eight was too late for many entities to do. That if you do stay at six after all the comments against it. We do believe that you should revise that entities that were in year six or seven in the current year could maintain through their eight. Had this been released in February they would have been able to do that. But releasing at the end of April, many of those entities no longer had that option. As that process was completed, so that would be our only comment. If you're going to stay with the six but you change your grandfathering in to allow those entities who in the current year would be on six or seven could maintain the same auditor to the end of eight to allow for a more smooth transition. Thank you.

42:34 OSA: Thank you Mr. Manning and I apologize I did receive them, and I didn't realized I did receive them but I am having them posted on the website right now.

42:45 NMSCPA: Thank you, I am going to go ahead and move on to the next person. Natalie Cordova, you may go ahead and state your comment for three minutes. Starting now.

42:56 Natalie Cordova, Education Trust Board of New Mexico: Thank you. Good morning, State Auditor and Audit team. I appreciate this opportunity; I was fortunate enough to log in just in time to hear Natalie Zamora iterate some comments. I appreciate that. One more thought and Audrey beat me to it in mentioning it. I do believe the auditors office already has sufficient regulation or control already written in its authority. Given the ability to perform a review and otherwise ultimately decide an agency and IPA are not able to work together. So, I suppose maybe redirect back to that rule, and emphasize I don't believe a rotation rule number one is necessary should it be found to be such, I do highly recommend keeping with the eight years as it is very helpful with the RFP process. It is an enormous undertaking for entities to resources and effort to properly adhere to the RFP process as well as firms responding if there even is a response for that agency. So, I appreciate this opportunity, just wanted to reiterate I believe there are already sufficient rules within the audit rule and that this one is not necessary. Thank you.

44:31 NMSCPA: Thank you. Are there any other online comments? Please raise your hand and I will call on you. Again, any comments online, please raise your hand and I will call on you.

45:00 OSA: Thanks Hope. Why don't we give it a couple more minutes. I don't know if that was an echo from me or if somebody else just tried to say something. [unknown: one second here, you're on.] [NMSCPA: I don't see any more hands raised on zoom to make any comments.] Copy that. I will also say, I will also note that the rulemaking is supposed to close tomorrow. The record for the rulemaking is supposed to close tomorrow. I will double check the register publication dates. There is not a huge huge rush to get this published since this doesn't really affect this current auditor or audit rotation or audit cycle, I should say. So, I will propose holding a comment period open for an extra week to allow anyone who could not join the zoom link today, well send out a notice to that effect through the society and through our lists so that anyone who was unable to join the meeting today because of technical difficulties they will have the opportunity to provide written comment. With that, unless there are any other comments, I will close this hearing and put it back over to Auditor Maestas for some closing remarks.

Exhibit 26

Concise Explanatory Statement For Rulemaking Adoption:

Findings required for rulemaking adoption:

Findings MUST include:
- Reasons for adopting rule, including any findings otherwise required by law of the agency, and a summary of any independent analysis done by the agency;
- Reasons for any change between the published proposed rule and the final rule; and
- Reasons for not accepting substantive arguments made through public comment.

Reasons for adopting rule:
This is the annual update to 2.2.2 NMAC, promulgated pursuant to 12-6-12 NMSA 1978, to clarify audit procedures, change contract submittal dates, change due dates for some agency audits and for the state's comprehensive audit report, correct references, correct grammatical and formatting errors, and provide additional guidance to auditors.

Reasons for changes between the published proposed rule and final rule:

Non-substantive, non-material grammatical and formatting changes;

Accepting substantive arguments and persuasive public comments opposing proposed rule amendments; and

Accepting substantive arguments and persuasive public comments requesting a change that was not proposed in the original rule but did not implicate due process rights of any agency or entity other than the agencies requesting the change.

Reasons for not accepting substantive arguments made through public comments:

Did not accept substantive arguments from a commenter that would have resulted in rule changes affecting third parties that would not have been a logical outgrowth of the proposed rule and therefore would have violated others' due process rights.

Issuing authority (If delegated, authority letter must be on file with ALD):
Name:
Joseph M. Maestas

Check if authority has been delegated ☐

Title:
New Mexico State Auditor

Signature: (BLACK ink only OR Digital Signature)
DocuSigned by:
Joseph M. Maestas
9E987C895EC34B4...

Date signed:
7/8/2024

NOTICE OF MINOR, NONSUBSTANTIVE CORRECTION

The Office of the State Auditor gives Notice of a Minor, Nonsubstantive Correction to 2.2.2 NMAC.

Pursuant to the authority granted under State Rules Act, Subsection D of Section 14-4-3 NMSA 1978, please note that the following minor, non-substantive corrections to spelling, grammar and format have been made to all electronic copies of the above rule, as follows:

Section 8: In Subsection G, paragraph (1), subparagraph (b), there was an errata amendment to change "…eight years…" to "…six years…" that was left from the initial proposed rule that was not changed, after the rule hearing, due to a clerical error. The existing language "…eight years…" was corrected in all electronic versions of the above rule.

A copy of this Notification will be filed with the official version of the above rule.