



New Federal Audit Regulations: Avoiding Compliance Pitfalls

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What is a Single Audit?

- Congress enacted the Single Audit Act in 1984 to govern the financial requirements and reporting of expenditures of Federal grants by non-Federal governments, Indian tribes, universities, or non-profit organizations. The Act has been revised and reissued several times, most recently in 2011, to be effective as of December 26, 2014.
- OMB Circular A-133 Compliance Supplement is issued periodically.

New Regulations

- The new regulations apply to audits of fiscal years beginning on or after Dec 26, 2014, in other words, fiscal years beginning January 1, 2015. Compliance during year 2015 will be audited by the auditor.
- Single Audit threshold is increased from \$500,000 to be \$750,000. Accordingly, some entities who had Single Audits at the \$500,000 level will now be exempt.
- Major Program determination changes – Type A/B threshold increases from \$300,000 to \$750,000.

New Regulations (Cont.)

- Criteria for being a low-risk auditee –
 - a) For each of the two preceding audit periods, prior Auditor's reports do not indicate a going concern, and
 - b) Auditor's opinion on financial statements and on schedule of expenditures of federal awards were not modified.
- The threshold for questioned costs increases from \$10,000 to \$25,000.
- Summary Schedule of Prior Year findings requires additional information about reasons prior year finding not fully corrected.
- Sub-recipients not required to submit Single Audit reports to pass-through entities – audit will available on SAC (Single Audit Clearinghouse)

Examples of control deficiencies:

- a. Insufficient control consciousness within the organization and the control environment. Control deficiencies in other components of internal control could lead the auditor to conclude that weaknesses exist in the control environment.
- b. Ineffective oversight by those charged with governance of the entity's financial reporting, performance reporting, or internal control, or an ineffective overall governance structure.
- c. Control systems that did not prevent, or detect and correct material misstatements so that it was necessary to restate previously issued financial statements or operational results. Control systems that did not prevent or detect material misstatements in performance or operational results.

Examples of control deficiencies

(Cont.):

- d. Control systems that did not prevent, or detect and correct material misstatements identified by the auditor. Misstatements involving estimation and judgment for which the auditor identifies potential material adjustments.
- e. An ineffective internal audit function or risk assessment function at an entity for which such functions are important to the monitoring or risk assessment component of internal control, such as for a large or complex entity.
- f. Identification of fraud of any magnitude on the part of senior management
- g. Failure by management or governance to assess the effect of a significant deficiency previously communicated to them and correct if needs to be corrected.

Examples of control deficiencies (Cont.):

- h. Inadequate controls for the safeguarding of assets.
- i. Evidence of intentional override of internal control by those in authority to the detriment of the overall objectives of the system.
- j. Deficiencies in the design or operation of internal control that could fail to prevent, or detect and correct, fraud, noncompliance with provisions of laws, regulations, contracts or grant agreements, or abuse having a material effect on the financial statements or the audit objective.

Examples of control deficiencies (Cont.):

- k. Inadequate design of information systems general, application, and user controls that prevent the information system from providing complete and accurate information consistent with financial, compliance, or performance reporting objectives or other current needs.
- l. Failure of an application control caused by a deficiency in the design or operation of an information systems general control.
- m. Employees or management who lack the qualifications and training to fulfill their assigned functions

Common Single Audit Findings

- Activities/Costs allowed or unallowed
 - Payroll using budgeted time allocation vs. actual time
 - Segregation of duties
- Cash Management
 - Request reimbursement before incurring the costs
- Davis Bacon Act
 - Failure to obtain certified payrolls
- Eligibility
 - Not documenting or following up on instances of ineligibility
- Equipment and Real Property Mgmt
 - Not separately maintaining Federal Equipment

Common Single Audit Findings (Cont.)

- Matching, level of effort and earmarking
 - Failure to meet the requirements
- Period of Availability
 - Failure to understand terms (pre-award costs)
- Procurement, Suspension and Debarment
 - Failure to check suspension/debarment (or document that it was done)

Common Single Audit Findings (Cont.)

- Reporting
 - Underlying support does not exist or does not agree with report
- Subrecipient monitoring
 - Not performing monitoring of subrecipients
 - Not maintaining evidence of monitoring performed
- Special Tests and provisions
 - Not understanding the requirements of the grant agreement

Significant Deficiencies and Material Weaknesses

- A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.
- A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.
- A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Compliance Requirements

A: Allowable Activities

Identify types of activities which are either specifically allowed or prohibited by the laws, regulations, and the provisions of contract or grant agreements pertaining to the program.

B: Allowable Costs

Direct costs are those that can be identified specifically with a particular final cost objective, i.e., award, project or other activity of the organization.

Indirect costs are those costs that have been incurred for common or joint objectives and cannot be readily identified with a particular final cost objective. Stated differently, indirect costs are those costs remaining after direct costs have been determined and assigned directly. (i.e. General and Administrative, depreciation)

C: Cash Management

When entities are funded on a reimbursement basis, program costs must be paid for by entity funds before reimbursement is requested from the Federal Government. If funds are advanced, recipients must follow procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement.

Compliance Requirements (Cont.)

D: Davis Bacon Act

Laborers and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by Federal funds must be paid wages not less than those established for locality of project (prevailing wage rates) by the DOL

E: Eligibility

The specific requirements for eligibility are unique to each Federal program and are found in the laws, regulations, and the provisions of contract or grant agreements pertaining to the program.

F: Equipment and Real Property Management

Title to equipment acquired by a non-Federal entity with Federal awards vests with the entity. Equipment means tangible nonexpendable property, including exempt property, charged directly to the award having a useful life of more than one year and an acquisition cost of \$5,000 or more per unit. However, lower limits may be established. The non-Federal entity may not dispose of or encumber the title to real property without prior consent of the awarding agency.

Compliance Requirements (Cont.)

G: Matching, level of effort, earmarking

The specific requirements for matching, level of effort, and earmarking are unique to each Federal program and are found in the laws, regulations, and the provisions of contract or grant agreements pertaining to the program.

Matching or cost sharing includes requirements to provide contributions (usually non-Federal) of a specified amount or percentage to match Federal awards. Matching may be in the form of allowable costs incurred or in-kind contributions (including third-party).

Level of effort includes requirements for (a) a specified level of service to be provided for a period, (b) a specified level of expenditures for specified activities to be maintained, and (c) Federal funds to supplement and not supplant non-Federal funding of services.

Earmarking includes requirements that specify the minimum and/or maximum amount or percentage of the program's funding that must/may be used for specified activities, including funds provided to subrecipients. Earmarking may also be specified in relation to the types of participants covered.

Compliance Requirements (Cont.)

H: Period of Availability of Federal Funds

Federal awards may specify a time period during which the non-Federal entity may use the Federal funds. Where a funding period is specified, a non-Federal entity may charge to the award only costs resulting from obligations incurred during the funding period and any pre- award costs authorized by the Federal awarding agency.

I: Procurement, Suspension and Debarment

Non-Federal entities are prohibited from contracting with or making sub-awards under covered transactions to entities or principals that are suspended or debarred.

J: Program Income

Program income is gross income received that is directly generated by the federally funded project during the grant period.

Program income may be used in one of three methods: deducted from outlays, added to the project budget, or used to meet matching requirements.

Compliance Requirements (Cont.)

K: Real Property Acquisition and Relocation Assistance

The Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970, as amended, (URA) provides for uniform and equitable treatment of persons displaced by federally assisted programs from their homes, businesses, or farms. Property acquired must be appraised by qualified independent appraisers. All appraisals must be examined by a review appraiser to ensure acceptability.

L: Reporting

Financial Reporting, Performance Reporting, Special Reporting

Recipients should use the standard financial reporting forms or such other forms as may be authorized by OMB (approval is indicated by an OMB paperwork control number on the form). Each recipient must report program outlays and program income on a cash or accrual basis, as prescribed by the Federal awarding agency.

Compliance Requirements (Cont.)

M: Subrecipient Monitoring

Monitoring the subrecipient's use of Federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements, and that performance goals are achieved.

N: Special Tests and Provisions

For both programs included and not included in the Supplement, the auditor shall identify any additional program compliance requirements not based in law or regulation.

Types of Compliance Requirements

CFDA	A.	B.	C.	D.	E.	F.	G.	H.	I.	J.	K.	L.	M.	N.**
	Activities Allowed or Unallowed	Allowable Costs/Cost Principles	Cash Management	Davis-Bacon Act	Eligibility	Equipment and Real Property Management	Matching, Level of Effort, Earmarking	Period of Availability of Federal Funds	Procurement and Suspension and Debarment	Program Income	Real Property Acquisition and Relocation Assistance	Reporting	Subrecipient Monitoring	Special Tests and Provisions
93 – Department of Health and Human Services (HHS)														
93.044														
93.045														
93.053	Y	Y	Y		Y		Y	Y		Y		Y	Y	Y
93.090	Y	Y	Y			Y	Y	Y				Y	Y	
93.095														
93.096	Y	Y	Y	Y		Y	Y	Y	Y			Y	Y	
93.153	Y	Y	Y			Y	Y	Y	Y	Y		Y		
93.210	Y	Y	Y		Y			Y		Y				
93.217	Y	Y	Y				Y	Y		Y		Y	Y	
93.224														
93.527	Y	Y	Y			Y		Y	Y	Y		Y		Y
93.268	Y	Y	Y					Y		Y		Y		Y
93.505	Y	Y	Y		Y	Y	Y	Y	Y	Y		Y	Y	
93.508	Y	Y	Y		Y	Y		Y	Y	Y		Y	Y	
93.525	Y	Y	Y		Y			Y	Y			Y	Y	
93.556	Y	Y	Y				Y	Y				Y	Y	
93.558	Y	Y	Y		Y	Y	Y	Y	Y			Y	Y	Y
93.714														
93.563	Y	Y	Y			Y	Y	Y				Y	Y	
93.566	Y	Y	Y		Y			Y				Y		
93.568	Y	Y	Y		Y		Y	Y				Y	Y	
93.569	Y	Y	Y		Y		Y	Y				Y	Y	Y
93.575														
93.596	Y	Y	Y		Y	Y	Y	Y				Y	Y	Y
93.600	Y	Y	Y	Y	Y	Y	Y	Y		Y		Y	Y	
93.645	Y	Y	Y				Y	Y				Y		
93.658	Y	Y	Y		Y	Y	Y	Y				Y	Y	Y
93.659	Y	Y	Y		Y	Y	Y	Y				Y	Y	
93.667	Y	Y	Y				Y	Y				Y	Y	
93.718	Y	Y	Y		Y		Y	Y	Y	Y		Y		Y
93.719	Y	Y	Y				Y	Y				Y	Y	Y
93.767	Y	Y	Y		Y		Y	Y				Y	Y	
93.775														
93.777	Y	Y	Y		Y		Y	Y	Y			Y	Y	Y
93.778														
93.889	Y	Y	Y			Y	Y	Y	Y			Y	Y	
93.914	Y	Y	Y		Y		Y	Y	Y	Y		Y	Y	
93.917	Y	Y	Y		Y	Y	Y	Y	Y	Y		Y	Y	
93.918	Y	Y	Y			Y	Y	Y	Y	Y		Y		
93.958	Y	Y	Y				Y	Y	Y			Y	Y	Y
93.959	Y	Y	Y				Y	Y	Y			Y	Y	Y
93.991	Y	Y	Y				Y	Y				Y	Y	
93.994	Y	Y	Y				Y	Y		Y		Y	Y	

Auditor's Testing Program

COMPLIANCE TEST WORKSHEET—FEDERAL AWARD PROGRAMS

Entity: [Client Name]

Financial Statement Date: June 30, 2014

Federal Program(s): []

Audit Program Step Circular		Voucher, check, or other number					
A-87 (2 CFR Pt 225)	A-122 (2 CFR Pt 230)						
A.6.	A.6.	<p>For selected transactions, determine that each charge was: Consistent with allowable activities and properly classified and accumulated into the activity total. Supported by appropriate documentation, such as:</p> <ol style="list-style-type: none"> 1) Approved purchase orders. 2) Receiving reports. 3) Vendor invoices. 4) Canceled checks. 5) [] <p>Correctly charged as to account, amount, and period. Authorized or not prohibited under state or local laws or regulations (only applies to Circular A-87).</p> <p>Approved by the federal awarding agency, when required.</p> <p>In accordance with the allowability of costs provisions of the applicable cost principles and any limitations in the program agreement, program regulations, or program statutes.</p> <ol style="list-style-type: none"> 1) Necessary and reasonable for the proper administration of the program. 2) Allocable to a particular cost objective (e.g., a specific function, program, project, department, or the like) if the goods or services involved are charged or assigned to such cost objective in accordance with relative benefits received. <p>d. Applied uniformly to federal and non-federal activities.</p> <p>e. Given consistent accounting treatment within and between accounting periods.</p> <p>f. Calculated in conformity with CASB Standards, generally accepted accounting principles or another comprehensive basis of accounting, when required under the applicable OMB cost principles or CASB Standards.</p> <p>g. Not included as a cost or used to meet cost sharing requirements of other federally-supported activities of the current or a prior period.</p> <p>h. Net of all applicable credits, e.g., volume or cash discounts, insurance recoveries, refunds, rebates, rental income, trade-ins, adjustments for checks not cashed, and scrap sales.</p> <p>i. Not included as a direct cost of a federal program if the same or similar costs were allocated as an indirect cost to the same program (or not included as an indirect cost of a federal program if the same or similar costs were allocated as a direct cost to the same program).</p> <p>j. For actual costs. (The charges are for actual costs rather than estimated based on budgeted or projected amounts.)</p>					
B.41.a.	B.39.a.						
B.41.b.	N/A						
c.	B.39.b.						
d.	c.						
e.	d.						
f.	e.						
g.	f.						
h.	g.						
i.	h.						
j.	i.						
k.	j.						

Auditor's Testing Program (Cont.)

I.	k.	For fringe benefit allocations, charges, or rates, such allocations, charges, or rates are based on the benefits received by different classes of employees within the organization.				
D.4.	D.4.	Davis-Bacon Act—When applicable				
E.4.d.	E.4.d.	Eligibility—When applicable				
H.6	H.6	For an obligation or obligations incurred during the period of availability.				
I.7.a.	I.7.a.	Supported by a contract file, when required, that documented the significant history of the procurement, including the rationale for the method of procurement, selection of contract type, basis for contractor selection, and the basis of contract price.				
b.	b.	The result of procurement procedures providing full and open competition.				
c.	c.	Supported by documentation of justifiable rationale to limit competition in those cases where competition was limited.				
d.	d.	Supported by contract files and a cost or price analysis supporting the procurement action.				
e.	e.	Approved by the awarding federal agency, when required. [Procurements exceeding \$100,000 may require prior approval when (1) awarded by noncompetitive negotiation, (2) awarded when only a single bid or offer was received, (3) awarded to other than the apparent low bidder, or (4) when specifying a "brand name" product.]				
f.	f.	In compliance with other procurement requirements specific to an award.				
I.8.	I.8.	When applicable, determine that state's laws and procedures were followed and that the policies and procedures used were the same as for state funds. (Applies only to state and federal awards sub-granted by the state to a local government or Indian tribal government.)				
I.10.	I.10.	Determine that, before entering into a covered transaction, the entity followed its procedures for verifying that an entity and any of its principals is not debarred, suspended, or otherwise excluded.				
K.5.	K.5.	Real Property Acquisition—When applicable				
K.6.	K.6.	Replacement Housing Payments—When applicable				
K.7.	K.7.	Rental and Down Payment Assistance Payments—When applicable,				
K.8.	K.8.	Business Relocation Payments—When applicable				

Schedule of Expenditures of Federal Awards (SEFA)

Not For Profit Entity

Schedule of Expenditures of Federal Awards

For the Year Ended June 30, 2014

Federal Grantor/ Pass-through Grantor/ Program or Cluster Title	Federal CFDA Number	Agency or Pass-Thru Number	Federal Expenditures
U.S. DEPT OF HEALTH & HUMAN SERVICES/ PASS-THOUGH - COUNTY OF SAN DIEGO			
Community Service Block Grant	93.569	County of San Diego	\$ 500,000
Teen Pregnancy Prevention Program	93.297	San Diego Youth Services	140,000
Community-Based Child Abuse Prevention Grants	93.590	City of Oceanside	20,000
Promoting Safe and Stable Families	93.556	County of San Diego	250,000
Total U.S. Dept of Health and Human Services			\$ 910,000
U.S. DEPT OF HOUSING & URBAN DEVELOPMENT			
Supportive Housing Program	14.235	Community Housing Works	\$ 60,000
Community Development Block Grant	14.218	City of La Mesa	40,000
Community Development Block Grant	14.218	County of San Diego	150,000
Community Development Block Grant	14.218	City of Oceanside	30,000
Community Development Block Grant	14.218	City of Escondido	25,000
Total U.S. Dept of Housing & Urban Development			\$ 305,000
U.S. DEPT OF EDUCATION			
Education for Homeless Children and Youth	84.196A	City of Cardiff	\$ 95,000
Total U.S. Dept of Education			\$ 95,000
U.S. DEPT OF TREASURY			
Volenteer Income Tax Assistance	21.009	Internal Revenue Service	\$ 20,000
Total U.S. Dept of Treasury			\$ 20,000
CORP FOR NATIONAL & COMMUNITY SVCS			
Social Innovation Fund	94.019	LISC San Diego	\$ 70,000
Total Corp for National & Community Services			\$ 70,000
Total Federal Awards			\$ 1,400,000

Note A - Basis of Presentation: This schedule is prepared on the accrual basis of accounting.

OMB Circulars

- To manage federal compliance requirements, organizations must adhere to the following compliance requirements:
 - 1) OMB Circular A-102 – Common Rule
 - 2) OMB Circular A-110 – Administrative Requirements
 - 3) OMB Circular A-122 – Cost Principles
- Note: OMB Circular A-133 is a “how to” on auditing federal grants

Indirect Cost Rate Agreements

	Direct Federal Program Services	Direct Non-Federal Program Services	(Indirect Cost Pool) Management and General	Fund Raising	Total
Salaries and wages	\$ 200,000	\$ 100,000	75,000	\$ 25,000	\$ 400,000
Payroll taxes	44,000	20,000	12,000	4,000	80,000
Employee benefits	20,000	10,000	7,500	2,500	40,000
Total personnel costs	<u>264,000</u>	<u>130,000</u>	<u>94,500</u>	<u>31,500</u>	<u>520,000</u>
Auto expense	16,550	3,000	3,450	-	23,000
Food and supplies to homes	100,000		-	-	100,000
Fund raising - Direct expenses			-	55,000	55,000
Insurance	22,000	3,500	14,250	-	39,750
Interest	38,200	1,500	-	-	39,700
Office	5,000	3,000	1,500	500	10,000
Outside services	70,000	67,500	73,800	9,500	220,800
Program - Direct expenses	84,750	17,000	-	-	101,750
Repair and maintenance	11,000	7,000	2,000	-	20,000
Telephone	10,000	6,000	3,000	1,000	20,000
Utilities	28,500	11,500	7,500	2,500	50,000
Total expenses	\$ <u>650,000</u>	\$ <u>250,000</u>	<u>200,000</u>	<u>100,000</u>	\$ <u>1,200,000</u>

Indirect Cost Rate Agreements

What does this mean?

Assumptions:

The NFP has a 20% negotiated indirect cost rate agreement for its federal program

The NFP's non-Federal program allows a 10% indirect rate to be billed.

	Direct Federal Program Services	Direct Non-Federal Program Services	(Indirect Cost Pool) Management and General	Fund Raising	Total
Total direct costs are	\$ 650,000	\$ 250,000	\$ -	\$ 100,000	\$ 1,000,000
Total allocated overhead at 20%	<u>130,000</u>	<u>50,000</u>	<u>(200,000)</u>	<u>20,000</u>	<u>-</u>
Total allocated costs with 20%	780,000	300,000	(200,000)	120,000	1,000,000
Total billable costs would be	<u>780,000</u>	<u>275,000</u>	<u>(155,000)</u>	<u>100,000</u>	<u>1,000,000</u>
Unbillable costs	\$ <u>-</u>	\$ <u>25,000</u>	\$ <u>-</u>	\$ <u>20,000</u>	\$ <u>45,000</u>

Remember these were approved at 20% 10% 0%

A-122 Exercise

Identify 10 unallowable costs noted in A-122

- 1)
- 2)
- 3)
- 4)
- 5)
- 6)
- 7)
- 8)
- 9)
- 10)

A-122 Exercise

Compensation for Personal Services

- Includes all compensation paid currently or accrued by the organization during the period of the award. Compensation costs are allowable when:
 - 1)
 - 2)
 - 3)

A-122 Exercise

Compensation for Personal Services

- Fringe Benefits – Usually allowable and must be _____.
- Costs include Annual leave, sick leave, holiday, social security, pension, etc.
- Employer Contributions are allowable when paid in accordance with established written policies.

A-122 Exercise

Compensation for Personal Services

- Support for Salaries and Wages
- Timesheets/Time Distribution Reports, etc. must:
 - 1)
 - 2)
 - 3)
 - 4)

A-122 Exercise

Depreciation/Use Allowances

- It is based on acquisition cost or fair market values at time of donation.
- If you elect the use allowance approach must exclude:
 - 1) Cost of land
 - 2) Any portion donated by Fed. Gov.
 - 3) Any matching portion
- Maximum use allowance
- Buildings and improvements - _____% of acquisition cost
- Equipment - _____% of acquisition cost.

A-122 Exercise

Depreciation/Use Allowances

- Adequate Records must be maintained under either method.
- Physical inventories must be taken at least once every two years.
- Equipment and Capital Expenditures are Unallowable as indirect costs.
- Prior approval from the awarding agency must be obtained to directly charge it.

A-122 Exercise

Fines and Penalties –

- Unallowable when it is for costs of failures to comply with federal, state or local laws.
- Allowable when it is incurred as a result of compliance with specific provision of an award or instructions in writing from the awarding agency.

A-122 Exercise

Fundraising Costs

- Are these costs beneficial or detrimental under A-122?
- Which one and why?

A-122 Quiz

If a specific item of cost is not mentioned in Attachment B, the implication is that the cost is unallowable.

- True or False
- See opening paragraph

A-122 Quiz

Costs of advertising and public relations designed solely to promote the organization are unallowable.

- True or False
- See 1.f.(4)

A-122 Quiz

“Mixed drinks” containing alcohol are allowable.

- True or False
- 3. Alcoholic Beverages

A-122 Quiz

Audit costs charged included in the indirect pool are not allowable.

- True or False
- 4.b



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