



RICHARD H. MOORE
TREASURER

North Carolina Department of State Treasurer

*State and Local Government Finance Division
and the Local Government Commission*

JANICE BURKE
DEPUTY TREASURER

Memorandum #1024

August 13, 2004

To: Finance Officers of Counties, Municipalities, Boards of Education, Public Authorities, and Certified Public Accountants

From: T. Vance Holloman, Director
Fiscal Management Section

Subject: Single Audit and Yellow Book Issues for the Fiscal Year Ending June 30, 2004

The following is a discussion of issues concerning local governments and public authorities that are required to have federal or State single audits or audits conducted under Governmental Auditing Standards for year ending June 30, 2004. A more inclusive discussion of federal and State single audit issues can be found in Section 35-E of the *Audit Manual for Governmental Auditors in North Carolina*.

Changes to Single Audit Thresholds

The U. S. Office of Management and Budget (OMB) has revised OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," to increase the threshold for a federal single audit from \$300,000 to \$500,000 per year (*Federal Register*, Vol. 68, Notice 38401, June 27, 2003). This change is in effect for fiscal years ending after December 31, 2003. Therefore, any unit of government or public authority in North Carolina must have a federal single audit performed under OMB Circular A-133 if total federal award expenditures were \$500,000 or more per fiscal year. A copy of OMB Circular-A revised to show changes published in the *Federal Register June 27, 2003*, can be obtained at the OMB web site: <http://www.whitehouse.gov/omb/circulars/index.html>. For audits years 1997-2003, the audit threshold is \$300,000 or more per year.

After conferring with local government officials, State officials and auditors, it was decided that the thresholds for a State Single audit would mirror the federal requirements. Beginning for audits with fiscal year ending June 30, 2004, local governments and public authorities that expend \$500,000 or more in state financial assistance must have a single audit performed in accordance with the State Single Audit Implementation Act and OMB Circular No. A-133.

As in prior years, units that get more than \$100,000 in combined federal and State financial assistance are required to have an audit performed in accordance with Yellow Book Standards.

Changes to Determining Major State Programs

As discussed in Memorandum # 993, revisions to the 2003 Compliance Supplements to OMB Circular A-133 made it necessary for the Office of State Auditor to designate certain programs of certain local governments to be audited as a major program by their local auditors. At that time, units and their local auditors asked our staff to consider changing the criteria for determining major State programs. The LGC conferred with local government officials, State officials, and local auditors, and a change was made. A State program is defined as a program with State expenditures, which includes State benefit payments. Beginning with the fiscal year ending June 30, 2004, a State program is determined to be a major program by the following process:

1. For federal programs with a \$300,000 or more State match financial assistance or State supplement, the program must be audited as major unless it was audited as major in at least one of the two most recent audit periods.
2. A single State financial assistance program with expenditures of \$300,000 or more must be audited as major if it is determined to be high risk using the criteria for federal program risk found in Section 525 of OMB Circular No. A-133 (or refer to Section 35-E of the *Audit Manual for Governmental Auditors in North Carolina*). A program may be considered low risk if it was audited as major in at least one of the two most recent audit periods and the auditor feels that prior year audit findings, if any, do not preclude the program from being low risk.
3. Percentage of coverage rule for State programs: The auditor shall audit a sufficient number of State programs as major programs, such that, in the aggregate, they encompass at least 50 percent of total state awards expended. **There is no low risk auditee determination for State awards.**

Federal and State expenditures should not be combined when determining major programs. However, if a program is determined to be either a major federal program or a major State program, the whole program should be tested as a major program.

Additional State Requirement to Audit Certain Federal Programs as Major Effective for Years Ending on or after June 30, 2004

The N. C. Office of State Auditor (OSA) identifies programs to be audited as major by certain counties and area public health authorities in order to satisfy federal requirements on testing eligibility for programs determined to be major by the State of North Carolina. These programs are in addition to using the risk-based criteria for federal programs and the threshold amounts for State programs. The Local Government Commission notified the counties and public health authorities and their auditors in April 2004 of the additional programs. If a county or public health authority was selected as having additional programs to be audited as major, the entire program should be tested.

For year ending June 30, 2004, the programs that are major by the State are as follows:

Program	CFDA
Medical Assistance Program (Medicaid)	93.778
Temporary Assistance for Needy Families (TANF)	93.558
Low-Income Home Energy Assistance (LIHEAP)	93.568
State Children's Insurance Program (CHIP)	93.767
Foster Care - Title IV-E	93.658
Special Supplemental Nutrition Program for Women, Infants, and Children (WIC)	10.557

So if a local government auditor audits any of the programs listed above as major, a turnaround document and CPA Representation letter must be completed. The LGC will not approve invoices for audit reports that do not have the required turnaround document and CPA representation letter enclosed with the audit-reporting package. Both the turnaround document and CPA rep letter should be submitted to this office with the audit report. The turnaround document would be used by the Office of State Auditor (OSA) as part of their audit documentation to satisfy the federal eligibility compliance requirement. Copies of both the turnaround document and representation letter may be obtained at our Single Audit Resources website. The OSA needs both documents in order to determine major State programs for the upcoming year-end. Please refer to common reporting problems beginning on page 7.

The above requirement is a result of the changes to the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplements for audits of States, Local Governments, and Non-Profit Organizations beginning for years ending June 30, 2003. The State Auditor is responsible for meeting the internal control and compliance audit objectives for eligibility (refer to LGC memo #993, April 23, 2003). Since the new eligibility requirements are to be tested by the local government auditors, there is a change in determining major programs.

**Amendment to Governmental Auditing Standards (Yellow Book) Paragraph 46
*Interpretation of Continuing Education and Training Requirements (April 1991)***

The U. S. General Accounting Office (GAO) has issued an internet notice that rescinds portions of par. 46 of the *Interpretation of Continuing Education and Training Requirements* (April 1991) and issued revised guidance. Effective immediately, GAO has deleted inclusion of taxation in the listing of subjects and topics that would always satisfy the 80-hour requirement. In addition, GAO has also rescinded the following section of par. 46: "...instruction in subjects and topics that meet the CPE requirements of licensing bodies (such as state boards of accountancy) or professional organizations (such as the American Institute of Certified Public Accountants (AICPA) or the Institute of Internal Auditors) would also satisfy the 80-hour CPE requirement."

Our office has been asked whether certain tax courses would relate to an objective of an audit conducted under Yellow Book and therefore be allowed. In our opinion, courses that cover the proper reporting taxes on W2s or 1099s may be allowed. According to GAO, tax courses would count if they directly enhance an auditor's professional proficiency to perform audits. If an auditor performed an audit under government auditing standards and taxation were a component of the audit or engagement, then the course would qualify as CPE under the 2003 Yellow Book. It should be emphasized that professional judgment should be used in determining whether a

specific tax course qualifies under GAGAS. For more information refer to LGC memo #1021, June 11, 2004 or <http://www.gao.gov/govaud/ybk01.htm>.

Clarification of Yellow Book Independence Standards

GAO has indicated to us that there is a way in which an auditor who audits the primary government under the revised GAO independence standards could perform bookkeeping services for a discretely presented component of that primary government without impairing the independence. If the primary government's auditor states in the auditor's report that they did not audit the component and relied solely upon the work of the component unit's auditor in issuing their opinion on the financial statements of the primary government, the independence of the primary government's auditor would not be impaired.

Component units, especially ABC Boards, usually do not have the same type of audit performed. The component unit's audit may have been performed in accordance with generally accepted auditing standards (GAAS) only, while the primary government may have a Yellow Book or Single Audit. If this is the case, the independent auditor's report and the compliance reports for the primary government should disclose that the component unit's audit was performed in accordance with GAAS only. Examples of this will be included in the Audit Manual for Governmental Auditors in North Carolina. Please refer to LGC memo #1021, June 11, 2004.

Eligibility Testing for Medical Assistance Program (Medicaid)

The changes in the federal requirements for testing eligibility referred to above will result in the Office of State Auditor relying on the work of local government auditors in testing eligibility (please refer to LGC memorandum # 993). Some of the auditors have questioned the procedures to be performed due to the statements made at CPE courses covering testing eligibility of the Division of Medical Assistance programs. Auditors should follow the guidance in the State Compliance Supplement, such as verifying information in the statewide information systems, and Federal Compliance Supplements.

Other U. S. Office of Management and Budget (OMB) Issues

Besides the issuance of the revised Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," the OMB made the following announcements:

- Beginning with fiscal periods ending in 2005, OMB requires the reporting **Data Universal Numbering System (DUNS)** number(s) on all Data Collection Forms (Form SF-SAC) submissions reporting expenditures of direct Federal awards. If no direct federal awards expenditures are reported, DUNS is requested, but not required. DUNS is a unique 9-digit number provided by Dun and Bradstreet (D&B).
- Grant applicants applying for grants on or after October 1, 2003 must provide a DUNS number. OMB has recommended that organizations should verify that they have a DUNS number or take the steps needed to obtain one as soon as possible if there is a possibility that they will be applying for the Federal grants or cooperative agreement. Organizations can receive a DUNS number at no cost by calling the dedicated toll free DUNS number request line at 1-866-705-5711.

- In addition to raising the threshold for single audits, the revised OMB Circular A-133 changes the **threshold for cognizant agency** for audit from \$25 million to \$50 million and makes related technical changes.
- For audit periods ending in 2004, 2005, 2006, non-Federal entities that require having a Federal Single Audit must complete the **revised Data Collection Form SF-SAC for 5-2004**. Audits submitted for years prior to 2004 must use one of the previous versions of the form (8-97 or 3-20-2001). Data Collection forms may be obtained from the Federal Audit Clearinghouse web-site at: <http://harvester.census.gov/sac/>. A link is located at the Single Audit Resources in the Department of State Treasurer's Single Audit website.

Management Letters and Yellow Book Findings

Audits performed under Generally Accepted Governmental Auditing Standards (GAGAS) should communicate all reportable conditions and compliance findings material to the financial statement amounts in the auditor's Yellow Book report (Report on Compliance and Internal Controls over Financial Reporting). Occasionally, for audits performed only under GAGAS (no Single Audit), the finding is cited only in the management letter and referenced in the yellow book report. It is preferred that the finding be referenced in the yellow book report and noted in a separate schedule included in the audit. The finding could be noted in the yellow book report itself, but all the applicable elements must be included.

Unlike audits not subject to GAGAS, the finding cannot be cited solely in the auditor's letter to management and referenced in the report. If the finding is considered too immaterial for inclusion as a finding in the report and mentioned in the management letter, then the letter must be referenced in the yellow book report.

Financial Assistance from Federal Emergency Management Administration

Effective March 1, 2003, FEMA became part of the Department of Homeland Security (DHS). Grants under this program continue to be funded under FEMA requirements and should be audited using FEMA's requirements until those requirements are superseded by DHS requirements and made part of subsequent awards. Since recipient's funding periods may not coincide with this change in the CFDA number, recipients should include the CFDA number shown on their notices of award (whether 83.548 and/or 97.039) in completing the Schedule of Expenditures of Federal Awards (SEFA). When awards from both CFDA 97.039 and CFDA 83.548 are present, they should be combined when determining Type A programs. If the program was a major program under the legacy CFDA number in either of the previous two years, the provision in the risk-based approach for prior audits is considered to have been met. On the SEFA, both the DHS CFDA number and the legacy agency's corresponding CFDA number should be presented separately.

Criteria for Federal Low-Risk Auditees-State Single Audits

Single audits that were performed based solely on funding from State of North Carolina do not meet the percentage of coverage rule requirements of OMB Circular A-133 §__530 since no federal awards were audited as major programs. Charter Schools need to be careful since federal funding for charter schools is increasing and many had single audits performed the previous two years due to the State Public School Fund expenditures. So if a governmental unit such as a municipality or charter school expends federal grants and did not issue a federal single audit report in the previous two years, they should audit federal programs that include 50% of the federal grant dollars.

FYE 2004 Confirmation Reports from DHHS

The N. C. Department of Health and Human Services (DHHS) Controller's Office is again preparing to make all reports that supply auditors with an independent confirmation of the financial assistance provided to units of government available on the Controller's website at the following URL: <http://www.dhhs.state.nc.us/control/>. Since these reports may be accessed and printed from this website, DHHS will not routinely mail hardcopies to users. For SFY 2003, DHHS continued to receive confirmation requests from many CPAs and their local government clients even though the confirmation reports were available on our website. We encourage you to obtain these reports online and save the cost of generating and mailing confirmation letters. The DHHS Controller's Office target date for the reports to be available on the website is August 31, 2004. **The LGC has prepared Excel spreadsheets that will provide assistance in preparing the Schedule of Expenditures of Federal and State Awards for Subsidized Childcare, Mental Health, Developmental Disabilities, and Substance Abuse Service Programs, and Public Health Programs.** Included are instructions, a spreadsheet for data entry, and a spreadsheet that displays the proper presentation. Modifications may be necessary by the user for a particular unit of government. The DHHS Controller's Office generates various confirmation reports and related Keys to Account Codes (when required), all of which may be accessed at the website.

Hurricane Relief Funds

The Department of Commerce is no longer distributing money for Hurricane Relief. Crime Control and Public Safety is now handling those funds through their existing programs.

Questioned Costs

Occasionally, the auditor will list a compliance finding and cite the questioned costs as "none" or "undeterminable." Although it is understandable that questioned costs cannot be determined in certain findings of noncompliance, an explanation as to why is necessary. Funding agencies need this information to adequately make a management decision. The LGC will reject single audit reports that have compliance findings and either no questioned costs amount is provided or there is no explanation as to why the finding had no questioned costs. OMB Circular A-133 §__510(a)(3) states that "Known questioned costs that are greater than \$10,000 for a type of compliance requirement for a major program..." shall be reported as a finding.

Most Common Single Audit Deficiencies for Fiscal Year Ended June 30, 2003

Cluster of Programs

- 1) Program name listed should be consistent with name of program on grant schedule to avoid confusion on what programs have been audited.
- 2) ID of Major Program should have all relevant CFDA numbers and refer to the program name as cluster (i.e. Food Stamp Cluster 10.551, 10.561; Nutrition Cluster 10.553, 10.555, 10.556, and 10.559).
- 3) If a cluster has both federal funding and state appropriations (i.e. Subsidized child care) and is separated on the grant schedule, be sure it is clear that all funding was audited under the ID of major programs

Financial Opinion

- 1) The auditor's report did not reference the accompanying Schedule of Expenditures of Federal and State Awards as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Yellow Book Report

- 1) Management letter referenced immaterial compliance findings, but the management letter was not referenced in the compliance section of the report.
- 2) Reference to general-purpose financial statements when basic financial statements were issued.

Section II Financial Statement Awards Findings

- 1) Yellow Book compliance findings do not have all the required elements

Section III Federal Awards and Section IV State Awards Findings and Questioned Costs

- 1) Questioned costs were not given and there was no explanation as to why the finding resulted in no questioned costs.

Corrective Action Plan

- 1) Corrective Action Plan was not included for Yellow Book findings.
- 2) Corrective Action Plan did not contain the name(s) of the contact person(s) responsible for corrective action and the anticipated completion date. (Refer to Section 315(c) of OMB 133 and page 2 of this memo).

Identification of Federal (or State) Programs

- 1) Program(s) that are listed as (a) major program(s) in the Summary of Auditor's Results, Schedule of Findings and Questioned Costs should have the same program name as presented on the Schedule of Expenditures of Federal and State Awards.
- 2) Cluster(s) of Programs should be presented by cluster name and corresponding CFDA's for the programs listed. If the cluster is not presented properly on the Schedule of Expenditures of Federal and State Awards, all programs associated with the cluster should be listed within the ID of Federal (or State) Programs.

Schedule of Expenditures of Federal and State Awards

- 1) The name of granting agency or pass through agency is not correct. (Refer to 2004 Compliance Supplements or Carolina County's Schedule of Expenditures of Federal and State Awards in the *Audit Manual For Governmental Auditors in NC*.)
- 2) Total amounts provided to subrecipients (OMB A-133 § ____ .310 (b) (5)) only require the program name, CFDA# (if applicable) and the amount passed-through. The subrecipient's name is not required.
- 3) Basis of Accounting: If schedule is presented for a yellow book audit only then it is misleading to state that the schedule is presented in the accordance with the requirements of OMB Circular A-133.

Data Collection Forms

- 1) Copy of a signed data collection form was not received.

Office of State Auditor's CPA Representation Letter

- 1) Copy of CPA Representation Letter was not received.
- 2) CPA Representation Letter was not signed

Office of State Auditor's Turnaround Document

- 1) Copy of Turnaround Document was not received.
- 2) Turnaround Document was not signed
- 3) All seven pages were not submitted
- 4) The document was not completed in its entirety. All items 1 through 5 should be completed.

Previous single audit memos along with other yellow book and single audit resources can be obtained from the N. C. Department of State Treasurer's Web page at: <http://www.treasurer.state.nc.us>, by scrolling down to single audit issues in "select a topic" box. If you have any questions relating to these issues, contact Jim Burke at (919) 807-2389 or james.burke@treasurer.state.nc.us.