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# Proposed Changes to Federal Grant Policies and Single Audits

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# Agenda

- Background
- Audit Requirements
- Cost Principles
- Administrative Requirements
- Next Steps

# Background

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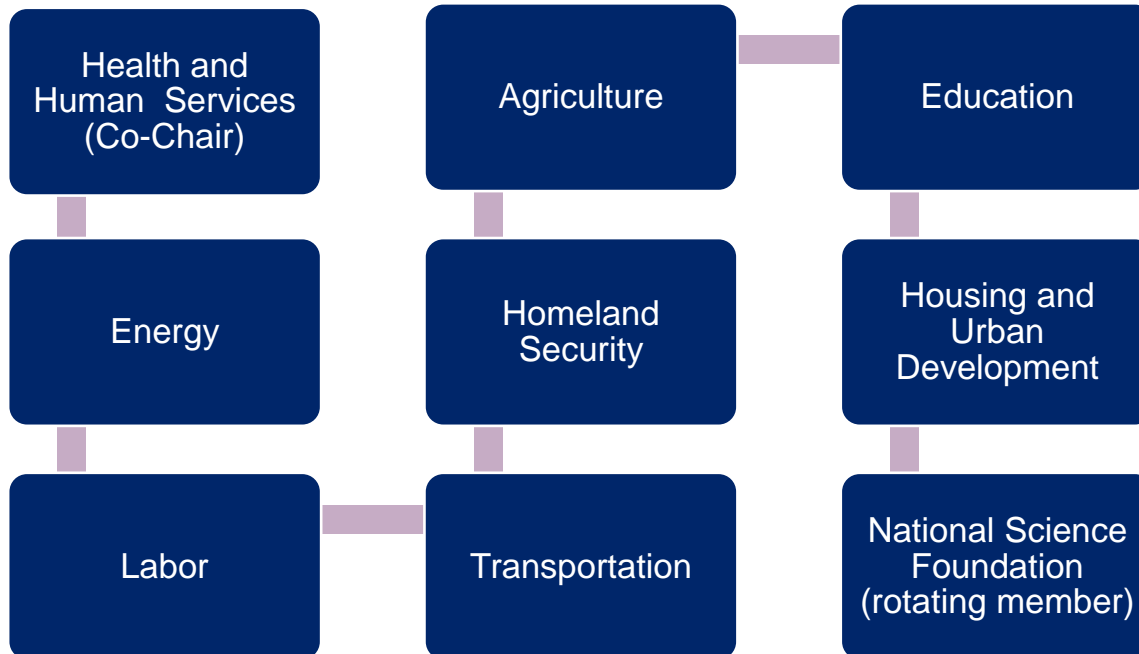
- National Single Audit Sampling Project (June 2007)
  - Conducted by the United States Department of Education
  - 208 Single Audits were in-depth reviewed for compliance with federal compliance and reporting requirements, receiving ratings as follows:
    - 115 were rated “acceptable” and could be relied upon
    - 30 were rated “limited reliability” due to significant deficiencies
    - 63 were rated “unacceptable” and could not be relied upon
  - The 93 deficient audits were not confined to either a sector (i.e., governments vs. non-profits) or auditor (i.e., national firm vs. local)

# Background

- President directed Office of Management and Budget (OMB) to work with Executive Branch agencies, state, local, and tribal governments, and other key stakeholders (working groups) to evaluate potential reforms to Federal grants policies:
  - November 23, 2009 – Executive Order 13520 on *Reducing Improper Payments and Eliminating Waste in Federal Programs*
  - February 28, 2011 – Presidential Memorandum on *Administrative Flexibility, Lower Costs, and Better Results for State, Local, and Tribal Governments*
- Executive Order 13563, *Improving Regulation*, issued on January 18, 2011, states each federal agency must “tailor its regulations to impose least burden on society, consistent with obtaining regulatory objective, among other things, and to the extent practicable, the costs of cumulative regulations.”
- President reinforced commitment to reform in Executive Order 13579, *Regulation and Independent Regulatory Agencies*, issued on July 11, 2011

# Background (continued)

- OMB issued Memorandum 12-01 on October 27, 2011, creating Council on Financial Assistance Reform (COFAR):
  - Charged with creating a more streamlined and accountable structure to coordinate financial assistance
  - COFAR is cochaired by the Office of Federal Financial Management at OMB and includes the eight largest grant making agencies as well as one rotating member .



# Background (continued)

- Since COFAR's first meeting in November 2011, COFAR and other stakeholders have developed a series of potential reforms to streamline and improve financial management and policy for federal government funds.
- OMB issued Advance Notice on potential reforms on February 24, 2012 (<http://www.whitehouse.gov/sites/default/files/omb/financial/fr-notice-grant-reform-2012.pdf>).

The reforms proposed are intended to improve the performance of federal grants and cooperative agreements ,while targeting waste, fraud, and abuse to ensure accountability in the use of funds

# Audit Requirements



# Single Audit Dollar Threshold

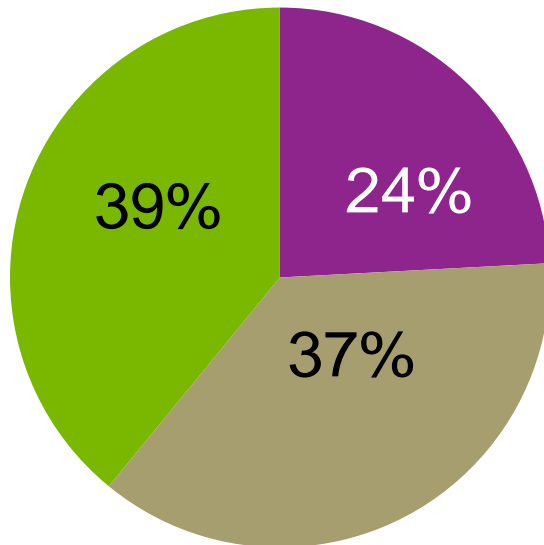
- Increase audit threshold from \$500K to \$1M
- Establish focused (reduced) version of single audit for entities with expenditures between \$1M and \$3M:
  - Test only two compliance requirements for a major program
    - Allowable costs always tested
    - Second requirement selected by federal agencies
    - Target risk of improper payments, waste, fraud, and abuse
- Require “full” single audit for entities with expenditures more than \$3M:
  - Streamlined compliance requirements

OMB's aim is to concentrate audit resolution or oversight resources on higher dollar and high risk awards.

# Impact of Tiered Approach

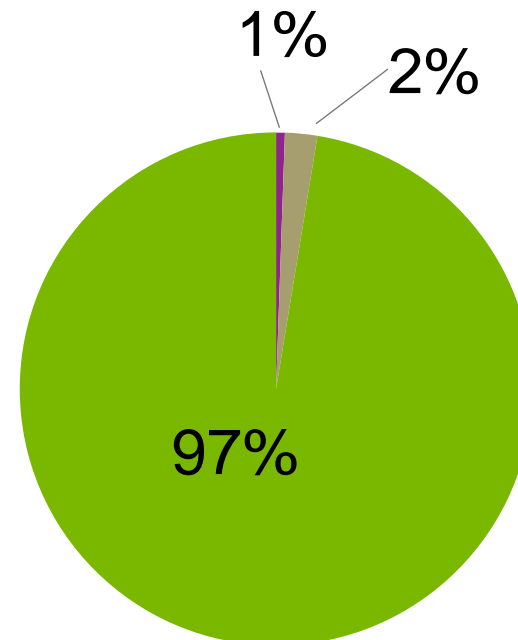
## Number of Single Audits

- \$500K - \$1 M: 10,724
- \$1M - \$3 M: 16,320
- \$3 M +: 17,376



## Total Dollars Covered

- \$500K - \$1M: \$7.8B
- \$1M - 3M: \$28.9B
- \$3M +: \$1,384.3B



# Single Audits by Agency

Single Audits by Agency	As Cognizant	As Oversight		
		> \$3 million	\$1 – 3 million	< \$1 million
Agriculture	14	777	1,196	776
HUD	270	4,211	4,881	2,848
Labor	13	345	239	134
Transportation	70	653	537	391
NSF	9	35	38	37
Energy	2	139	148	68
Education	480	4,791	4,401	2,894
HHS	240	3,114	2,721	1,880
Homeland Security	8	236	323	303

# “Streamlining” Compliance Requirements for Full Single Audits

- Focus on “stewardship” of Federal funds:
  - Emphasize elements that address improper payments, waste, fraud, and abuse
  - Streamline (reduce) other elements to reduce audit burden
  - Compliance requirements no longer considered “universal.”
- Target subset of compliance requirements for increased testing, larger samples, and/or lower levels of materiality:
  - Allowable or unallowable activities and costs
  - Eligibility
  - Period of availability
  - Procurement, suspension, and debarment
  - Reporting
  - Selection of subrecipients and subrecipient monitoring
  - Special tests and provisions.



# “Streamlining” Compliance Requirements for Full Single Audits (continued)

- Reduce testing of other requirements by making them optional, smaller samples, and/or higher levels of materiality:
  - Cash management
  - Davis-Bacon Act
  - Equipment and real property management
  - Matching, level of effort, and earmarking
  - Program income
  - Real property and relocation assistance.

OMB believes that refocusing the Compliance Supplement to reduce the number of compliance requirements would reduce the audit burden on recipients and provide agencies with more risk-based audits.

# “Streamlining” Compliance Requirements for Full Single Audits (continued)

Compliance Requirements	Now	As Proposed	
		> \$3 million	\$1 – 3 million
Activities Allowed or Unallowed	✓	↑	If selected by agency
Allowable Costs/Cost Principles	✓	↑	★ <b>Mandatory</b>
Cash Management	✓	↓	If selected by agency
Davis – Bacon Act	✓	↓	If selected by agency
Eligibility	✓	↑	If selected by agency
Equipment	✓	↓	If selected by agency
Matching, Level of Effort, Earmarking	✓	↓	If selected by agency
Period of Availability of Federal Funds	✓	↑	If selected by agency
Procurement, Suspension, Debarment	✓	↑	If selected by agency
Program Income	✓	↓	If selected by agency
Real Property	✓	↓	If selected by agency
Reporting	✓	↑	If selected by agency
Subrecipient Monitoring	✓	↑	If selected by agency
Special Tests and Provisions	✓	↑	If selected by agency

**Legend**  
 Increased focus  
 Decreased focus

# Strengthening Audit Follow-up by Federal Awarding Agencies

- Require agencies to designate “senior accountable agency official” to oversee audit resolution process
- Require agencies to implement audit-risk metrics:
  - Timeliness of report submissions
  - Number of audits with other than unqualified opinions on major programs
  - Number of repeat findings.
- Encourage agencies to engage in “cooperative audit resolution” and to take proactive approach to resolving audit recipient weaknesses and deficiencies.
- Digitize single audit reports into searchable database to facilitate audit follow-up.

OMB believes that strengthening audit resolution policies should result in agencies taking a more proactive (collaborative) approach towards follow-up and in a decrease in audit findings and program risk over time.

# Cross-agency Coordination

- Reinforce requirement that federal awarding agencies are to coordinate additional audits of a recipient entity with the Federal oversight or cognizant agency
- Require federal agencies to conduct audit follow-up of subawards (second tier) for audit findings regarding financial or internal control systems not specific to program delivery when recipient receives a majority of its awards through direct grants:
  - Eliminates initial follow-up responsibility of pass-through entity
  - Subrecipients not required to “negotiate” with both Federal agency and pass-through entity for the same issue
  - Once resolved, pass-through entity responsible for audit follow-up monitoring of general findings to ensure compliance of audit resolution.

OMB believes that these changes will allow pass-through entities to focus on programmatic requirements.



# Cost Principles

# OMB Cost Principles – Consolidation

- Consolidate cost principles into single document with limited variations:
  - OMB Circular A-21 – Educational Institutions
  - OMB Circular A-87 – Governments
  - OMB Circular A-122 – Nonprofit Organizations
  - Health and Human Services at 45 CFR Part 74 Appendix E – Hospitals.

These reforms above are aimed at providing uniformity in documentation requirements across different types of entities.

# Cost Principles – Indirect Cost Rate

- Option 1: Establish mandatory flat rate that is discounted from the recipient's already negotiated rate
- Option 2: Five recipients option of flat rate or negotiating a rate
  - Recipients with a previously negotiated rate may have the additional option of accepting a discounted rate from their already negotiated rate.
  - Discounted rates could be maintained for up to a four-year period with minimal documentation, or raised through negotiation with full documentation.

OMB believes Option 1 could significantly reduce burden associated with indirect cost rate calculation and negotiation, as well as reduce overall indirect costs.

# Cost Principles – Indirect Cost Rate (continued)

- Under both options, OMB would work with cognizant federal agencies and the HHS Division of Cost Allocation to develop a list of flat rates and discount factors by entity type
- Establishing either a mandatory or optional flat indirect cost rate could reduce administrative burdens on recipients associated with documenting, justifying, negotiating, and maintaining support for a negotiated rate

# Cost Principles – Explore Alternatives for Time and Effort Reporting

- Reform would involve working with the federal grant and Inspector General communities to identify risks associated with justifications for salaries and wages and to identify possible alternative mechanisms for addressing those risks beyond current time-and-effort reporting requirements
- Include consideration of the ideas described in existing pilots or development of new pilots to document the allowability and allocability of salaries and wages charged to federal awards as direct costs
- Three pilots currently under consideration:
  - Demonstration Partnership
  - Department of Labor’s Workforce Innovation Fund
  - Department of Education’s Request for Ideas.

OMB believes pilot programs could result in substantial reductions of the current administrative burden associated with time and effort reporting while enhancing compliance and stewardship.

# Cost Principles – General

- Include cost of computing devices not otherwise subject to inventory controls as allowable direct cost supplies
- Clarify that threshold of \$5,000 is the allowable maximum residual inventory of unused supplies that may be retained for use on another Federal award at no cost, as long as cost was properly allocable to original agreement at time of purchase.
- Specify gains and/or losses related to debt arrangements on capital assets due to speculative financing arrangements (such as hedges, derivatives, etc.) are unallowable
- Eliminate requirement that printed “help-wanted” advertising comply with particular specifications.

# Cost Principles – General

- Allow for excess or idle capacity in consolidated data centers, telecommunications, and public safety facilities
- Clarify budgeting for contingency funds associated with federal award for construction or upgrade of large facility or instrument, or for IT systems:
  - Is an acceptable and necessary practice
  - The method by which contingency funds are managed and monitored is at discretion of the Federal funding agency.

# Cost Principles – General (continued)

- Revise OMB guidelines to allow costs for expenses associated with effort to collect improper payment recoveries or related activities, if specifically approved or directed by the awarding agency
- For nonprofit organizations:
  - Provide example of the Certificate of Indirect Costs
  - Provide example of indirect cost proposal documentation requirements.



# Administrative Requirements

# Administrative Requirements

- Consolidate administrative requirements in OMB Circulars A-102 and A-110 into a consolidated and uniform set of administrative requirements for all grant recipients
- Require agency consideration of the merit of each proposal and the financial risk associated with each applicant prior to making award:
  - Indicators of risk include past financial, internal control, and programmatic performance
  - Outcome of review should affect award decisions, and risk assessment may also affect terms and conditions
  - This reform would not apply to formula grants.

OMB believes this would formalize a best practice already conducted by many agencies.

# Administrative Requirements (continued)

- Require agencies to provide a 90-day advance forecast of funding opportunities in an updated Catalog of Federal Financial Assistance (CFFA):
  - This reform is aimed at providing applicants with additional time and information with which to prepare financial assistance applications
  - CFFA replaces CFDA and includes domestic and international funding priorities.
- Provide a standard format for announcements of funding opportunities, including:
  - Eligibility or qualification information
  - Clear description of all criteria used in agency review of applications
  - Disclosure of all terms and conditions that may be attached to the award.
- Reiterate that information collections are limited to standardized data elements approved by OMB as required under the Paperwork Reduction Act of 1995



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# AICPA Clarity Project

# What is the Clarity Project?

- Release of the Statements of Auditing Standards No. 122 – 125
- AICPA issued an Audit Risk Alert specifically on the Clarified Auditing Standards organized in 4 parts:
  - Substantive changes
  - Clarifying changes
  - Formatting changes
  - Standards not yet issued in project
- Applicable for audits with years ending after December 15, 2012

# Comprised of Several SAS's

- The Auditing Standards Board has issued the following Statements on Auditing Standards marking the largest milestone to date of its Clarity Project:
  - SAS No. 122, *Statements on Auditing Standards: Clarification and Recodification*
  - SAS No. 123, *Omnibus Statement on Auditing Standards–2011*
  - SAS No. 124, *Financial Statements Prepared in Accordance With a Financial Reporting Framework Generally Accepted in Another Country*

# SAS No. 122

- This statement contains the *Preface to Codification of Statements on Auditing Standards, Principles Underlying an Audit Conducted in Accordance With Generally Accepted Auditing Standards*, and 39 clarified SASs. This statement recodifies and supersedes all outstanding SASs through No. 121 except:
  - SAS No. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*, as amended;
  - SAS No. 65, *The Auditor's Consideration of the Internal Audit Function in an Audit of Financial Statements*;
  - SAS No. 87, *Restricting the Use of an Auditor's Report*; and the following clarified SASs that were issued to address practice issues timely and are already effective:
    - SAS No. 117, *Compliance Audits* (issued December 2009);
    - SAS No. 118, *Other Information in Documents Containing Audited Financial Statements* (issued February 2010);
    - SAS No. 119, *Supplementary Information in Relation to the Financial Statements as a Whole* (issued February 2010); and
    - SAS No. 120, *Required Supplementary Information* (issued February 2010).

# SAS No. 123

- This statement contains amendments to:
  - SAS Nos. 117–118
  - SAS No. 122, AU–C sections:
    - *200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance With Generally Accepted Auditing Standards*
    - *230, Audit Documentation*
    - *260, The Auditor’s Communication With Those Charged With Governance*
    - *705, Modifications to the Opinion in the Independent Auditor’s Report*
    - *915, Reports on Application of Requirements of an Applicable Financial Reporting Framework*
  - These amendments conform SAS Nos. 117–118 to SAS No. 122 and address other changes necessitated by the Clarity Project.



# SAS No. 124

- SAS No. 124 supersedes the requirements and guidance in SAS No. 51, *Reporting on Financial Statements Prepared for Use in Another Country*, and redrafts that statement to apply the ASB's established clarity drafting conventions.
- This statement requires the auditor, in instances where a report that is to be used in the United States was prepared in accordance with a financial reporting framework generally accepted in another country, to include an emphasis-of-matter paragraph to highlight the foreign financial reporting framework, but permits the auditor to express an unqualified opinion.