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NATIONAL ASSOCIATION FOR STATE COMMUNITY SERVICES PROGRAMS

WAP Monitors' Training

Agenda

- OMB Basics
- Fiscal Monitoring
- Red Flags
- Audit Essentials



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OMB Basics

Subpart D – Post Federal Award Requirements



- ***..302 Financial management***

- States must follow state law
- Financial management system must provide:
 - Identification, in its accounts, of all Federal awards received and expended (CFDA title & number, etc.)
 - Accurate, current and complete disclosure of financial results for each award
 - Source and application of funds
 - Effective control over all funds, property and other assets (safeguarding of assets)
 - Comparison of expenditures with budget
 - Written procedures on payments
 - Written procedures for determining allowability of costs

Subpart D–Post Federal Award Requirement Performance and Financial Monitoring and Reporting



- ***_.328 Monitoring and reporting program performance***
 - Non–Federal entity must monitor its activities to assure compliance with requirements
 - Monitoring must cover each program, function or activity
 - Performance reports must be submitted
 - Must include performance vs. objective

Subpart D—Post Federal Award Requirement

Subrecipient Monitoring and Management



- ***_.330 Subrecipient and contractor determinations***
 - Pass-through entity determines status
 - Substance of relationship more important than the form of the agreement
 - **Subrecipients:**
 - Characteristics:
 - Determines who is eligible to receive Federal assistance
 - Has its performance measured in relation to the Federal program
 - Has responsibility for adherence to Federal requirements
 - Uses Federal funds to carry out a program for a public purpose, as opposed to providing goods or services

Subpart D—Post Federal Award Requirement Subrecipient Monitoring and Management



- ***_.330 Subrecipient and contractor determinations,*** Continued
 - **Contractors:**
 - Characteristics:
 - Provides goods or services within normal business operations
 - Provides similar goods or services to many different purchasers
 - Normally operates in a competitive environment
 - Provides goods or services that are ancillary to the operation of the Federal program
 - Is NOT subject to compliance requirements

Subpart D–Post Federal Award Requirement Subrecipient Monitoring and Management



- ***_.331 Requirements for pass-through entities***
 - All pass-through entities shall:
 - Ensure subawards include:
 - Federal award information, including CFDA number
 - All clauses required by Federal statute, regulation, etc.
 - Each administrative, national policy and program-specific requirement
 - Any additional Federal requirements
 - A recognized indirect cost rate
 - Access to records
 - Closeout terms

Subpart D–Post Federal Award Requirement Subrecipient Monitoring and Management



- ***_.331 Requirements for pass-through entities,*** Continued
 - All pass-through entities shall:
 - Evaluate each subrecipient’s risk of noncompliance with Federal statutes, regulations and terms and conditions of the subaward, which includes consideration of:
 - Subrecipient’s prior experience with same or similar subawards
 - Results of previous audits
 - New personnel or new or changed systems
 - Federal agency monitoring

Subpart D–Post Federal Award Requirement Subrecipient Monitoring and Management



- ***_.331 Requirements for pass-through entities,*** Continued
 - All pass-through entities shall:
 - Monitor the activities as necessary to ensure Federal awards are used for authorized purpose, in compliance with laws, regulations and provisions of subawards
 - Analyze financial and programmatic reports of subs
 - Follow-up and ensure subs take timely and appropriate action on all deficiencies from audits and on-site reviews
 - Issue a management decision for audit findings

Subpart D–Post Federal Award Requirement Subrecipient Monitoring and Management



- ***_.331 Requirements for pass-through entities,*** Continued
 - All pass-through entities shall:
 - Depending upon pass-through entity’s assessment of risk posed by the subrecipient, the following monitoring tools may be used to ensure proper accountability and compliance with program requirements and achievement of performance goals”
 - Performing on-site reviews of operations
 - Providing training and technical assistance
 - Arranging for agreed-upon-procedures engagements
 - Ensure every sub is audited
 - Consider whether adjustments are needed on pass through books

Subpart D – Post Award Requirements

- Internal Controls
 - Establish and maintain effective internal control over Federal awards
 - In compliance with:
 - “Standards for Internal Control in the Federal Government” (Comptroller General of the United States)
 - “Internal Control Integrated Framework” (COSO)
 - Comply with Federal statutes, regulations and the terms and conditions of the awards
 - Evaluate and monitor compliance
 - Take prompt action when instances of noncompliance are identified in audit findings

COSO Framework



- Key Concepts:
 - Internal control is process
 - Internal control is impacted by people, not just policies and manuals
 - Internal control provides reasonable assurance, not absolute
- Definition
 - A process, effected by an entity's board of directors, management and other staff, designed to provided reasonable assurance regarding achievement of objectives:
 - Effectiveness and efficiency of operations
 - Reliability of financial reporting
 - Compliance with applicable laws and regulations
 - Safeguarding of assets

Subpart D – Post Award Requirements

- Internal Control Framework
 - **Control Environment** – Organization’s culture that influences ethical behavior.
 - **Risk Assessment** – Process of identifying risks that threaten achievement of goals.
 - **Control Activities** – Processes and procedures to support compliance and mitigate risk.
 - **Information and Communication** – Providing right information to the right people at the right time.
 - **Monitoring** – Process to verify that the controls are working as intended.

Green Book

- Same 5 Components
- Adds 17 principles



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Fiscal Monitoring

**Why do we
monitor....?**



NASCSP

...because...



**We want our
programs, and
therefore our
agencies to be**

Top 10 Risks for Non-profits

- ▶ 1. Loss of Government funding
- ▶ 2. Reduction in Foundation funding
- ▶ 3. Lack of succession
- ▶ 4. Workplace injury
- ▶ 5. Fraud
- ▶ 6. Data security
- ▶ 7. IT downtime
- ▶ 8. Unrelated business activities
- ▶ 9. Disgruntled former employee
- ▶ 10. Natural disaster

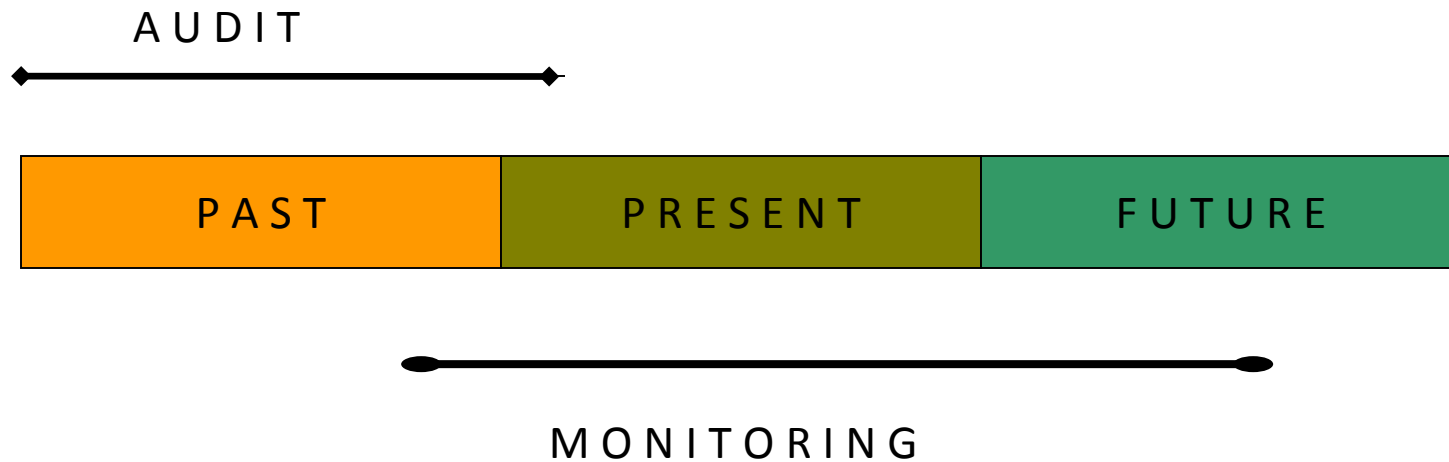
Monitoring Continuum



Monitoring Continuum



Monitoring Continuum





WHAT SHOULD WE BE TESTING IN OUR MONITORING?

TRANSACTIONS **OR**
SYSTEMS

Success is

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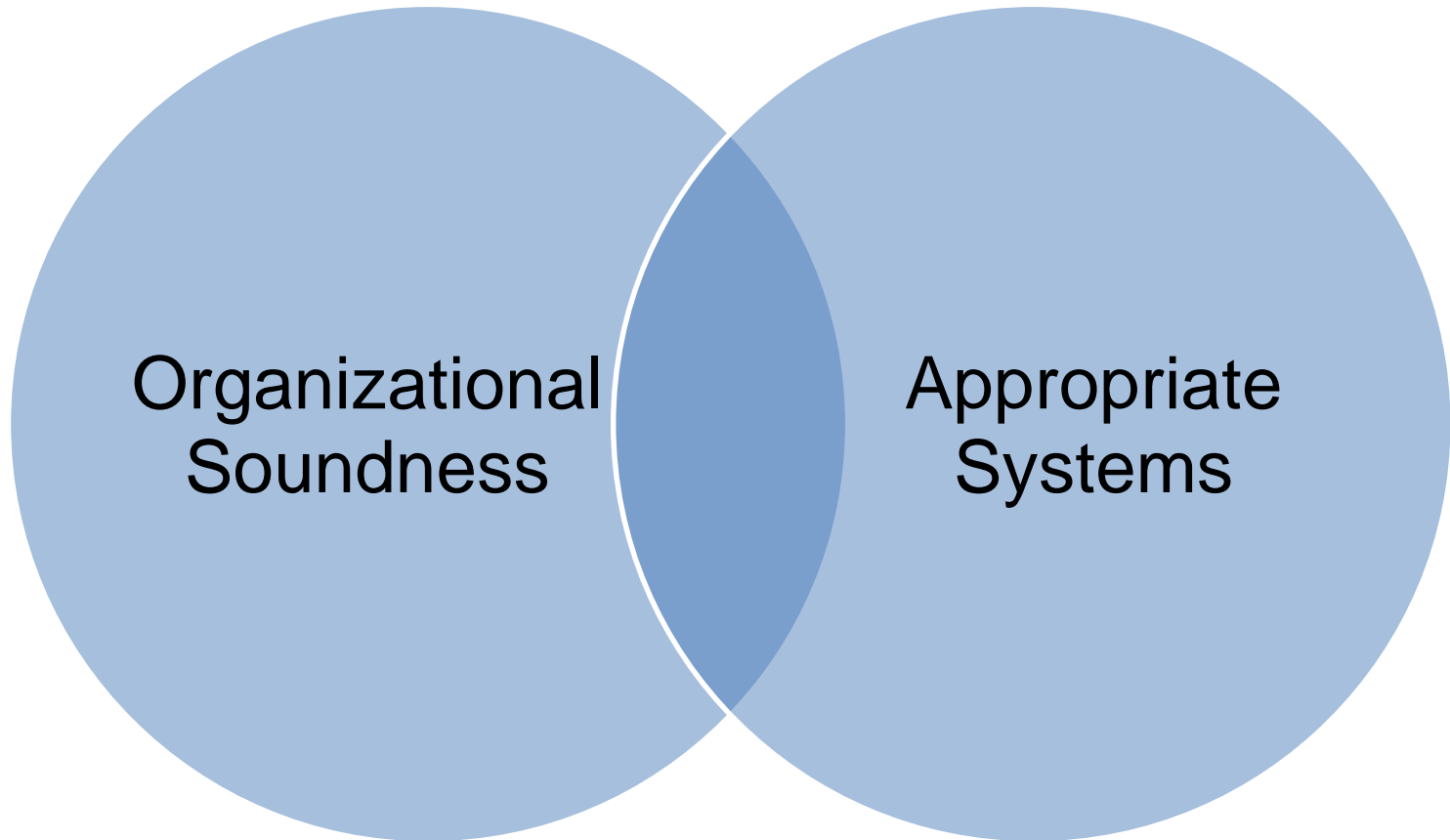
Organizational
Soundness

Organizational Soundness



- What are we looking for:
 - Entity must exist
 - Foundation must be strong
 - Legal minimum requirements
 - Appropriate governance
- Assessment tools:
 - Organizational documents
 - Annual documents
 - Board meeting records
 - Board trainings
 - Does the Board take its fiduciary duty seriously?
 - Review financials

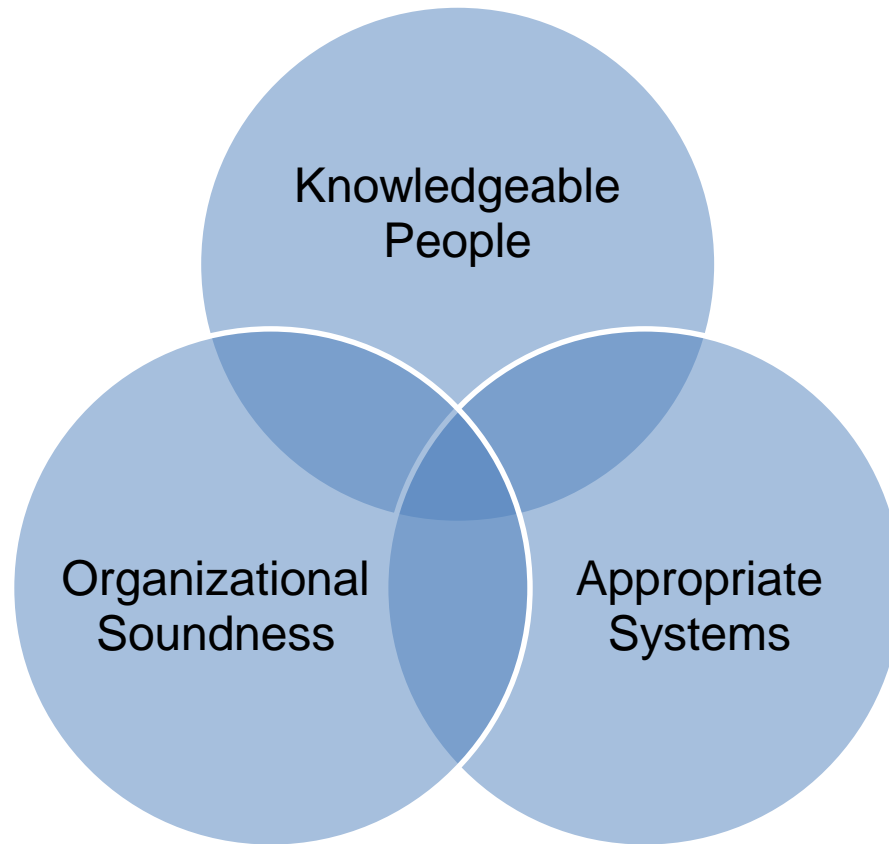
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Appropriate Systems

- What are we looking for:
 - Financial systems are in place that can support programs
 - Data systems provide accurate information
 - Compliance system is functioning as intended
- Assessment tools:
 - Annual audit is ‘clean’
 - Reports coming out of system are correct
 - Someone is responsible for compliance

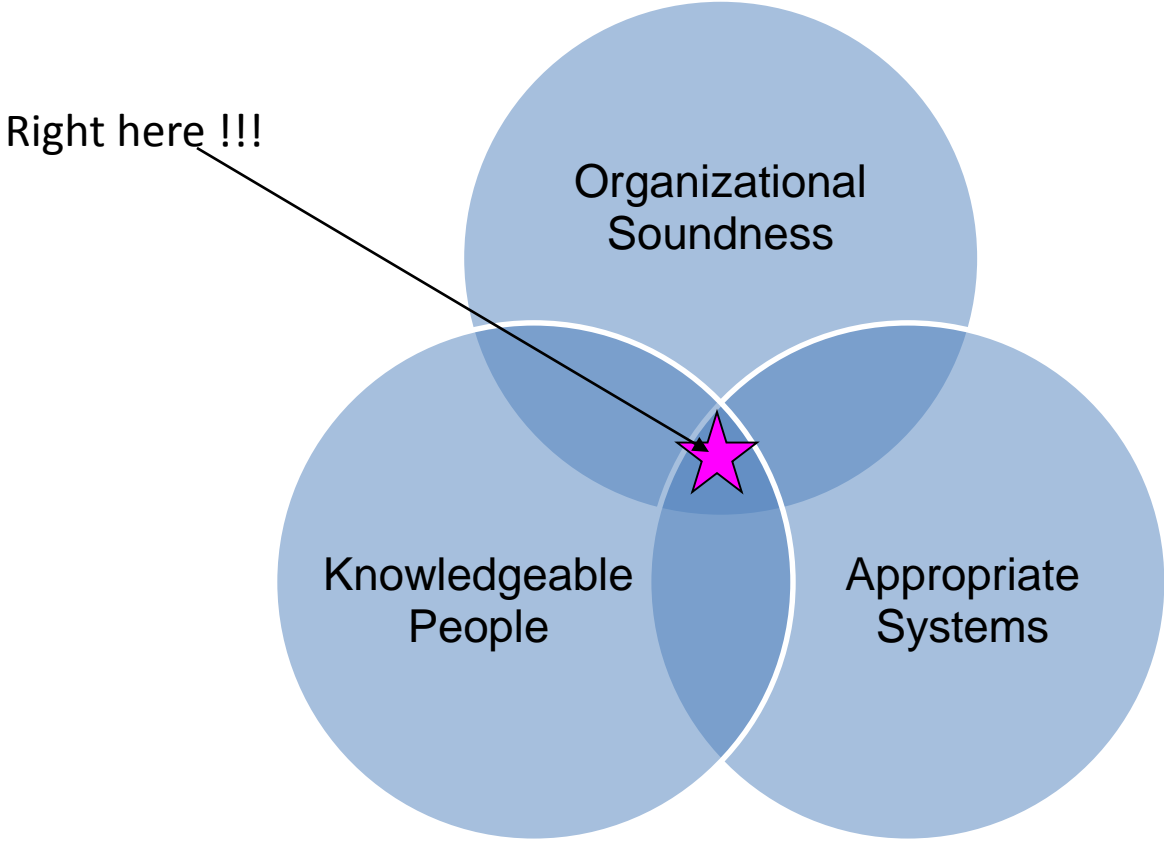
Success is



Knowledgeable People

- What are we looking for:
 - People with the technical capabilities
 - People with the proper motivation
- Assessment tools:
 - Is the hiring process rigorous
 - Do people have the knowledge
 - Is there a professional development plan in place
 - Are there performance evaluations

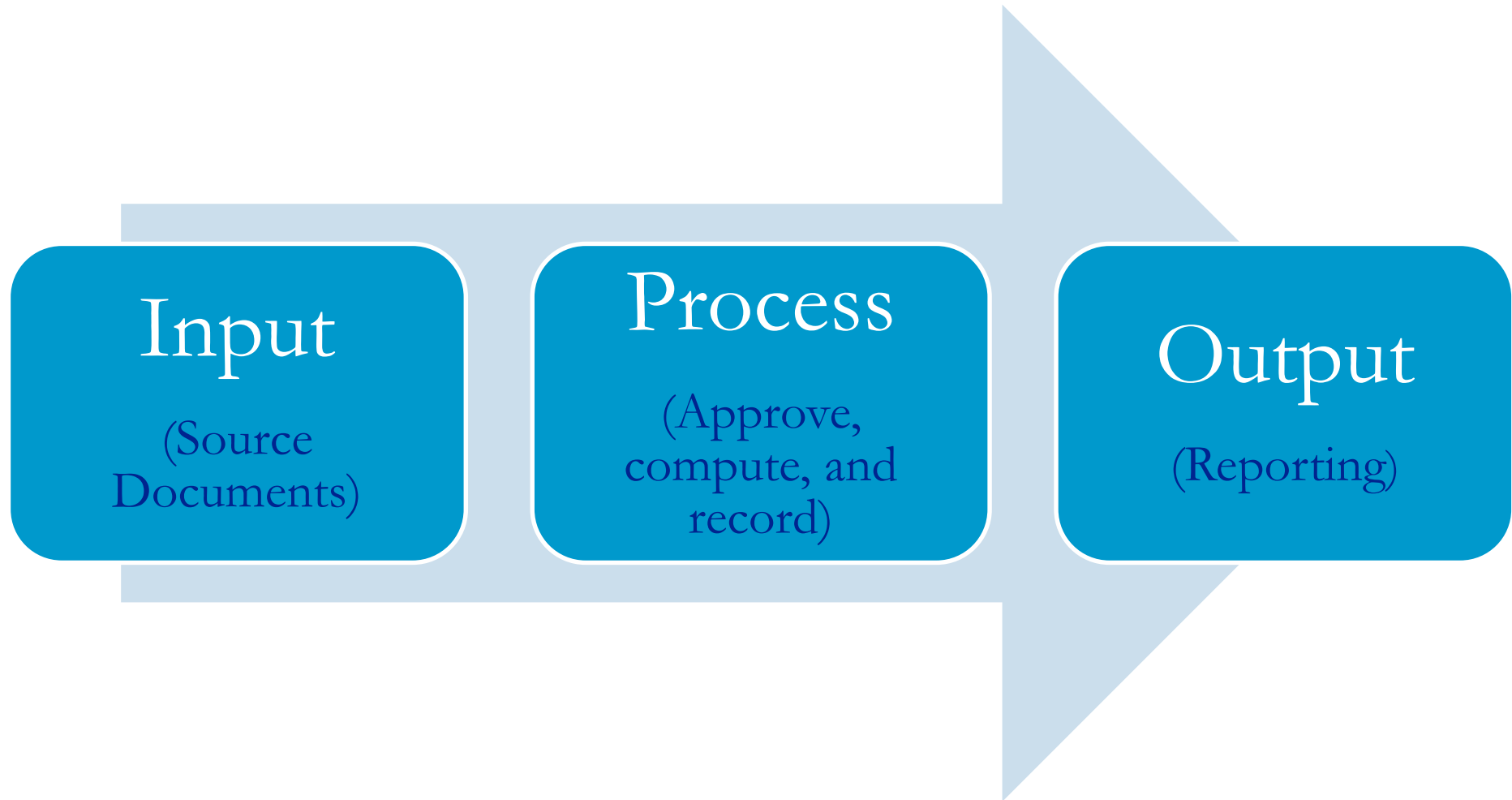
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Systems Testing Design

- Identify process objectives
- Review process with process owner
- Flowchart process
- Determine risks
- Identify controls in place
- Identify design gaps (deficiencies)
- Gather evidence
- Conclude if system is working as designed

SYSTEM: Flow of information



Flow of Information

- 1. Initiating and authorizing transactions:
 - How and by whom
 - Source documents
- 2. Recording and processing transactions
- 3. How is incorrect processing resolved:
 - How are errors identified
 - How are they corrected
- 4. Reconciling and reporting financial information

System Basics

- A. Policies and procedures
- B. Segregation of duties
 - Authorizing transactions
 - Recording transactions
 - Maintaining physical custody of assets
- C. Documentation
- D. Independent checks
 - Audits
 - Spot checks
- E. Monthly budget vs. actual

Desired Outcomes

A sound financial reporting system includes methods and records that:

1. Identify and record all valid transactions (completeness).
2. Provide, on a timely basis, sufficient detailed information about transactions.
3. Allow for the recording of transactions at their proper monetary value.
4. Record transactions in the proper accounting period.
5. Properly disclose transactions in the financial statements.

Practical Considerations

- **JOURNAL ENTRIES**
 - How originated?
 - Documentation required
 - Reviewed and approved
- **FICTITIOUS**
 - Vendors
 - Employees

WATCH



Must Haves

- **Appropriate systems**
 - Written financial policies and procedures
 - Proper segregation of duties
 - Timely reconciliations
 - Journal entry control
- **Qualified and competent people**
 - Written personnel policies and procedures
 - Staff development and appraisals
- **Sound governance**
 - Timely review of budget vs. actuals
- **Audit**

Common System Deficiencies

- 1. Lack of Segregation of Duties
 - Especially in smaller organizations
- 2. Lack of or outdated policies and procedures
 - Review every 3 years
- 3. Untimely information
- 4. Undocumented procedures
- 5. Lack of controls over specific exposures:
 - Ghost employees/Fictitious vendors/Journal entries
- 6. Inadequate Board or Management oversight

Common Findings

- Inadequate account reconciliations
- Unsupported adjusting journal entries
- Inadequate supervision of staff
- Staff lacking appropriate accounting skills
- Inadequate sense of ethical environment
- Lack of risk assessment
- Out of date financial policies and procedures
- Lack of financial monitoring
- Untimely financial processing

Common Findings

- Lack of segregation of duties
- Inadequate approval processes
- Undocumented cost allocation process
- Inadequate support documentation
- Reimbursement requests not reconciled to general ledger

Systems Testing Approach

Systems Concern

- Competent people
- Journal entry process

Possible Test

- Job descriptions
- Annual reviews
- Professional Development
- Documentation required
- Approvals

Systems Testing Approach

Systems Concern

- Board oversight

Possible Test

- Approving budget
- Approving ED activity
- Reviewing monthly budget vs actuals
- Financial expertise
- Training & development
- Conflict of interest

Systems Testing Approach

Systems Concern

- Policies and procedures
- Information technology

Possible Test

- Fiscal policies
- Personnel policies
- Board policies
- Reviewed & updated
- Security reviewed
- Disaster recovery

Dumb Criminals

- Three people went to a bank to cash checks they had recently stolen. This was a problem as the victim worked at the bank and her co-workers noticed the name on the checks.
- A counterfeiter tried passing off a billion dollar bill. The problem is there no such thing as a billion dollar bill.
- Two 17 olds set seventeen fires in Montgomery County, Maryland. They took pictures of the acts and displayed them on the internet.

Case Study - A

You are monitoring the Weatherization program of XYZ Community Action. XYZ completely outsources all production of weatherized units (it has no staff that do construction work). You have noticed from your desk review that the cost per unit for XYZ is exactly twice what it is for the three neighboring CAPS. The Weatherization director tells you this is not possible.

Case Study - A

You have the Finance Director assemble the following sub-contractor summary:

Able, Inc. \$ 84,500 for 42 units

Baker Company \$ 150,726 for 71 units

Charlie Corp. \$ 327,441 for 23 units

Currently, all invoices come into the finance office and are paid directly from there.

Do you have any concerns? What are your next steps? Any controls you might suggest going forward?

Case Study - B

You have been asked to monitor ABC CAP. In the review of payroll transactions, you notice that there are two employees who make more than the Executive Director.

In the current system, payroll is prepared by the accounting clerk. She also is a “people person” so she is the defacto Human Resource Department – conducting interviews and hiring new employees.

Does this cause you any concern? What additional records might you want to review? What enhancements to internal controls would you recommend?

Case Study - C

You are in River City to do the monitoring visit for the CAP. You have interviewed the program staff and are impressed with the knowledge and dedication of the program people. Next, you turn your attention to the fiscal office. When you arrive, 2 of the 3 fiscal staff are on vacation. About one-half of the items you asked to review are in a pile waiting for you in a small conference room.

Case Study - C

You try tracing a transaction from January through the general ledger and get confused because it is in, out, in twice, backed out three times and then posted backwards. When you ask for clarification, you are told only the finance director knows how to use that stupid *'generous leader'* program. You finally call the Board Treasurer for help and he says that the Board has not looked at that month yet (it's October now).

Do you have any concerns? What 'red flags' are you seeing? Do you have any suggestions for improvements? If so, what are they?



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Financial Red Flags

Red Flags

- *How do organizations get into trouble?*
- Make bad decisions
- Depend on an undiversified revenue stream
- Fail to operate effectively and efficiently
- Make short-term decisions – not long-term
- Have a ‘bloated’ administrative structure

Potential questions to answer

- Is the organization able to meet its short-term obligations?
- Can the entity afford to pay off its long-term debt commitments?
- Is the organization using its resources efficiently?
- Does the entity have the right financing mix?
- What is the firm's ability to withstand setbacks?
- Is this organization one that we want to fund?

Before we start...

- Financial analysis is a science **and** an art
 - There is no one right way to conduct it
- Don't analyze the numbers in a vacuum
 - Numbers provide a 'trigger' for further questions
- You must know the environment (i.e. business, local economy, ...)

Disclaimers

- Using the past to predict the future



- *Rules of thumb*
- Trends and benchmarking

Red Flags

- Operating results:
 - 1. Increase (Decrease) in Net Assets for the Year
 - Goal – Breakeven or positive
 - Mitigating – One time or planned result
 - 2. Actual vs. Budget
 - Goal – actual within 2 – 3% of budget
 - Mitigating – Emergency unplanned event or one time revenue
 - 3. Administrative expenses as a percent of total
 - Goal – 10% or less
 - Mitigating – possessing a funding source that funds

Red Flags

- Cash Flow Management
 - 4. Cash flow from operations
 - Goal – Positive cash flow from operations
 - Mitigating – Strong plan in place
 - 5. Grants receivable as a percent of annual grant revenue
 - Goal – 30 days or less
 - Mitigating – Strong capital in place to allow
 - 6. Payables as a percent of expenses
 - Goal – 30 days or less
 - Mitigating – contracts in place that allow slow pay

Red Flags

- Cash Flow Management (continued)
 - 7. Available cash on hand
 - Goal – at least 15 days
 - Mitigating – a well managed cash flow system
 - 8. Current ratio
 - Goal – at least 1.25
 - Mitigating – Very timely funding sources

Red Flags

- Future oriented measures
 - 9. Unrestricted net assets as a percent of revenue
 - Goal – 5 – 10%
 - Mitigating – Strong planning systems in place
 - 10. Revenue dependency
 - Goal – Largest revenue source is less than 25% of total revenue
 - Mitigating – Strong program operations with little chance of funding disruption; program has strong political support

Red Flags

- Future Oriented Measures (continued)
 - 11. Long-term debt to net assets
 - Goal – 25% or less
 - Mitigating – Direct relationship between long-term assets and long-term debt is 1 to 1
 - 12. Debt service costs as a percent of expenditures
 - Goal – 5% or less
 - Mitigating – Long-term funding commitment is in place related to principal and interest

Red Flags

- Future Oriented Measures (continued)
 - 13. Future commitments (obligations) to revenue
 - Goal - ??????????
 - Mitigating – Multi-year funding contracts in place
 - 14. Net book value of fixed assets
 - Goal – at least 50%
 - Mitigating – Good maintenance and safety program is in place



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Audit Essentials

What is an Audit?

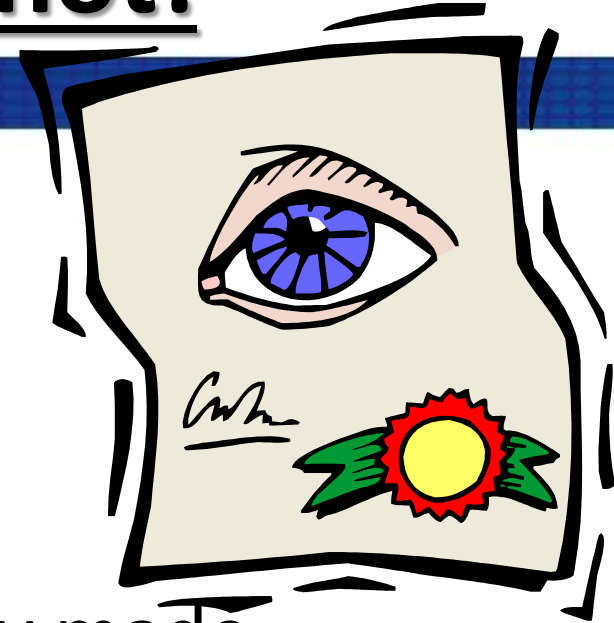


- An audit is the professional **opinion**
- of a **Certified Public Accountant**
- that the financial statements are **fairly presented**
- in accordance with **Generally Accepted Accounting Principles (GAAP)**



What an Audit is not!

- Not a guarantee
- Not an insurance policy
- Not a statement that the agency made *good* decisions
- Not that the agency is in good financial condition



Types of Auditor's Opinions

- Unqualified (“Clean”)
 - Without Modification
- Qualified
 - Deviation from GAAP
 - Limitation of scope
- Adverse
- Disclaimer



Twin Cities Community Action Programs

Schedule of Findings and Questioned Costs

A. Summary of Auditor's Results

1. The auditor's report expresses an unqualified opinion on the financial statements of Twin Cities Community Action Programs.
2. No reportable conditions relating to the audit of the financial statements are reported in the Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters.
3. No instances of noncompliance material to the financial statements of Twin Cities Community Action Programs were disclosed during the audit.
4. No reportable conditions were disclosed during the audit of the major federal award program as reported in the Independent Auditor's Report on Compliance With Requirements Applicable to the Major Program and Internal Control Over Compliance.
5. The auditor's report on compliance for the major federal award program for Twin Cities Community Action Programs expresses an unqualified opinion.
6. There were no audit findings relative to the major federal award program for Twin Cities Community Action Programs.
7. The programs tested as major programs were the U.S. Department of Health and Human Services, Low Income Home Energy Assistance, CFDA #93.568 and Head Start CFDA #93.600.
8. The threshold for distinguishing Types A and B programs was \$300,000.
9. Twin Cities Community Action Programs was determined to be a low-risk auditee.

B. Findings – Financial Statements Audit

None

C. Findings and Questioned Costs – Major Federal Award Programs Audit

Finding: None

Questioned Costs: None

Subpart F – Audit Requirements

- Required for non-Federal entities that expend \$750,000 or more in Federal awards in a year
- The auditee shall:
 - Prepare appropriate financial statements
 - Procure or otherwise arrange for the audit
 - Follow up and take corrective action on audit findings
- Audit Reporting
 - Opinion on financial statements
 - Report on internal control over financial reporting and on compliance with laws, regs and provisions of awards
 - Report on compliance and internal control over compliance applicable to each major program
 - Schedule of findings and questioned costs
 - Summary of audit results

Subpart F – Audit Requirements

- Major Program – Compliance Elements
 - A. Activities Allowed/Unallowed
 - B. Allowable Costs/Cost Principles (combined)
 - C. Cash Management
 - D. Davis–Bacon
 - E. Eligibility
 - F. Equipment and Real Property Management
 - G. Matching, Level of Effort and Earmarking
 - H. Period of Availability of Federal Funds
 - I. Procurement and Suspension and Debarment
 - J. Program Income
 - K. Real Property Acquisition and Relocation Assistance
 - L. Reporting
 - M. Subrecipient Monitoring
 - N. Special Tests and Provisions

Financial Analysis Process

- **EXAMPLE COMMUNITY ACTION**
- *Step 1* – Acquire financial statements
 - 3 to 7 years, if possible
- *Step 2* – Quick Scan
 - Look for large changes
 - Look for key numbers
- *Step 3* – Review the financial statement footnotes