



# State of North Carolina

## Department of State Treasurer

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### Memorandum #1039

August 11, 2005

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, 2005

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, 2005. 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 Yellow Book CPE Requirements**

The Governmental Accounting Office (GAO) has issued a technical amendment to the 2003 revised *Governmental Auditing Standards* (GAGAS), commonly referred to as the Yellow Book, that revises paragraph 3.45 and the related footnote of the Continuing Professional Education (CPE) requirements contained in the Competence standard. This Guidance on GAGAS CPE replaces the 1991 document *Interpretation of Continuing Education and Training Requirements*. Auditors affected by this amendment are those only involved in fieldwork and who charge less than 20 percent of their time annually to audit and attestation engagements conducted under GAGAS. These auditors are required to take 24 hours of training in each 2-year period in subjects and topics directly related to governmental auditing, the government environment, or the specific or unique environment in which the audited entity operates. Auditors that are involved with planning, directing, and reporting in addition to fieldwork still have to comply with the remainder of the 80-hour CPE requirements.

This technical amendment, issued in April 2005, has been incorporated into the concurrent release of *Governmental Auditing Standards: Guidance on GAGAS Requirements for Continuing Professional Education* from the GAO. This document provides guidance to auditors and audit organizations in implementing the CPE requirements prescribed in the 2003 revision of GAGAS.

A few of the other major changes found in this amendment include:

- Audit organizations are allowed greater flexibility in granting exceptions to the CPE requirements for such reasons as extended family leave, military leave, and disasters. Workloads, budget, or travel constraints are not allowed as exceptions.
- In determining CPE hours needed for auditors who become subject to yellow book after the beginning of an audit organization's 2-year CPE period, a pro rated approach based on 6 month intervals is to be used. Each 6-month period is considered a quarter and an audit organization should define a prorated number of hours based on the number of full 6-month intervals remaining in the CPE period.
- The new requirements expand and update the lists of subjects and topics that could satisfy the 24-hour and 80-hours CPE requirement under GAGAS.
- It also includes a paragraph on taxation and examples of qualified tax training CPE under GAGAS. CPE related to tax services provided by the auditor that are not related to the subject matter of audits under GAGAS who not qualify. Individual and Corporate Income tax return training is an example of CPE that does not qualify. However, if certain taxation or other topics relate to an objective or the subject matter of an audit, training could qualify under GAGAS. Auditors who audit tax revenues of a governmental entity would be able to claim GAGAS CPE hours related in taxation.

Both the technical amendment and the *Governmental Auditing Standards: Guidance on GAGAS Requirements for Continuing Professional Education* are effective for CPE measurement periods beginning on or after June 30, 2005. A copy of the entire document may be found at GAO's web-site: <http://www.gao.gov/govaud/ybk01.htm>. The LGC has issued memo #1040 that gives a detailed summary of the changes in the new *Guidance on GAGAS Requirements*.

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

OMB Circular A-133 2005 Compliance Supplements (CS): For 2005, there will not be a complete reissuance of Office of Management and Budget's 2005 Compliance Supplement. OMB only intends to issue new or significantly changed programs in Parts 4 and 5, those parts of the CS that relate to the Part 4 and 5 changes, and updated appendices. There will be no substantive changes to Part 3 and no new cluster of programs for this year's CS. For programs with minor changes, the changes will be listed in Appendix V and can serve as the basis for the auditor to make "pen and ink" changes to the 2004 CS. Therefore, for 2005, the auditor will need to use both the 2004 and 2005 CS for planning and review purposes.

Seven new federal programs will be included in the new 2005 CS. They will include:

- US Dept. of Education - U.S. Dept. of Education - Mathematics and Science partnerships (84.366);
- U.S. Dept. of Health and Human Services – National Bioterrorism and Hospital Preparedness Program (93.889);

- US Dept. of Homeland Security –State Homeland Security Grant Program (97.004), Urban Areas Security Initiative (97.008), Homeland Security Grant Program (97.067)

Eleven programs/clusters with significant changes including:

- U.S. Dept. of Agriculture - WIC (10.557);
- U.S. Dept. of Education - Crosscutting (84.000), Migrant Education State-Grant Programs (84.011), Special Education Cluster (84.027/84.173);
- U.S. Dept. of Health and Human Services – TANF (93.558), Child Support Enforcement (93.563), Foster Care (93.658).

Data Universal Numbering System (DUNS): Beginning with fiscal periods ending in 2005, OMB requires the reporting DUNS number(s) on all Data Collection Forms (Form SF-SAC) submissions reporting expenditures of direct Federal awards. DUNS is a unique 9-digit number provided by Dun and Bradstreet. If no direct federal award expenditures are reported, DUNS is requested, but not required. To obtain a DUNS #, call 866-705-5711 (free call) or <http://eupdate.dnd.com/requestoptions/government/ccrreg/>.

### **Mental Health Cost Finding 2004-2005**

The N.C. Department of Health and Human Services (DHHS) Controller's Office, in conjunction with the Division of Medical Assistance and Division of Mental Health, Developmental Disabilities, Substance Abuse Services, will not require a cost finding report from the Local Management Entities (LMEs)/ Area Programs for the reporting year 2004 – 2005. For years ending June 30 ,2005, the data necessary for verifying the program cost and System Management cost will be obtained by DHHS staff during on-site reviews as part of the annual monitoring process scheduled for this fall as well as audit procedures required as part of the annual audit through the use of the Crosscutting Supplement. For year end's beginning in 2006, DHHS will require the submission of cost data, in which the content and format have yet to be developed. This cost data will come only from LMEs and Area programs who still provide direct services that are material in nature.

### **Appropriations for Buses**

Amount appropriated for schools by NC Department of Public Instruction as part of the school buses financing arrangements are considered grants to schools boards. The annual amounts appropriated by DPI must be reported on the Schedule of Expenditures of Federal and State Awards and treated similar to Textbooks. If any LEA receives an appropriation over the State threshold (\$300,000), it may be audited as major if it is determined to be high risk. To verify that the funds were appropriated and for other compliance questions contact DPI Transportation Services, at 919-807-3571. Due to limited auditing procedures, no compliance supplement was prepared.

### **Office of State Auditor's Designated Programs for 2005**

Having determined the programs that are major to the State, the N. C. Office of State Auditor (OSA) identifies major programs by certain counties and area public health authorities in order to satisfy federal requirements on testing eligibility. 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 2005 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, 2005, the programs that are determined major by the State are as follows:

<u>Program</u>	<u>CFDA</u>
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

If any of the programs listed above are audited as major, a turnaround document and CPA Representation letter must be completed and submitted to the LGC along with the audit reporting package.

### **Changes to Single Audit Thresholds**

A 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.

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.

Determining Major State Programs: 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.

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.

### **Management Letters and Yellow Book Findings**

GAGAS requires that the following matters, unless clearly inconsequential, be reported in a management letter and the management letter be referenced in the yellow book report:

- internal control deficiencies that are not reportable conditions,
- immaterial violations of provisions of contracts or grant agreements,
- immaterial abuse.

### **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. Auditors of 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, federal programs that include 50% of the federal grant dollars should be audited.

### **Significant Accounting Policies Note to the SEFSA**

OMB Circular A-133 requires that the SEFSA include a note that describes significant accounting policies used in preparing the SEFSA. Guidance from the AICPA in *Government Auditing Standards and Circular A-133 Audits - AICPA Audit and Accounting Guide* recommends that this include the following, at a minimum:

- Basis of Accounting (no prescribed method by Circular A-133, modified accrual most common)
- Presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* and the **State Single Audit Implementation Act**.
- Therefore some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements

If a SEFSA is included in a yellow book only audit (no single audit), then the statement “presented in accordance with the requirements OMB Circular A-133” should be removed.

### **Presentation of Federal Cluster of Programs on the Schedule of Expenditures of Federal and State Financial Awards**

The State of North Carolina’s cognizant agency, the U. S. Department of Health and Human Services, and the AICPA has recommended that when reporting the Cluster of Programs on the

SEFSAs, the programs clustered by federal agencies be separated from the additional programs added to the cluster by State agencies. A footnote to the SEFSA identifying the State Cluster should be included. Programs that have been clustered by federal agencies cannot be “unclustered” by State agencies; however, State agencies may add additional federal programs and/or State programs. A Federal Cluster of Programs can be found in Part 5 of the federal CS (sect. A of the State CS). A State Cluster of Programs can be found in Sect. B of 2005 State CS (“CFDA#” followed by “CL”).

For example, the State cluster Subsidized Childcare Cluster, which includes the federal cluster Child Care and Development Fund Cluster (93.596, 93.575) and State funding, should be presented on the SEFSA as follows:

<u>Grantor/Pass-through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass Through Grantor's Number</u>	<u>Fed(Direct &amp; Pass-through) Expenditures</u>	<u>State Expenditures</u>
<u>US Dept of Health and Human Services</u>				
<u>Administration for Children and Families</u>				
Passed-through the N.C. Dept. of Health and Human Services				
Subsidized Child Care (Note 4)				
<u>Child Care Development Fund Cluster</u>				
Division of Social Services				
Child Care Development Fund-Administration	93.596	XXXXX	203,500	--
Division of Child Development				
Child Care Development Block Grant	93.575	XXXXX	1,050,251	--
Child Care Development Fund--Mandatory	93.596	XXXXX	828,038	--
Child Care Development Fund—Match	93.596	XXXXX	311,928	43,469
Total Child Care Fund Cluster			2,393,717	43,469
Social Services Block Grant	93.667	XXXXX	99,235	--
TANF	93.558	XXXXX	154,284	--
Smart Start		XXXXX	--	651,482
State Appropriations		XXXXX	--	541,671
Total Subsidized Child Care (Note 4)			2,647,236	1,236,622

Notes to the Schedule of Expenditures of Federal and State Financial Awards:

- The following are clustered by the NC Department of Health and Human Services and are treated separately for state audit requirement purposes: Subsidized Child Care, Foster Care and Adoption, Mental Health Services, Developmental Disability Waiting List Services, Substance Abuse Services, and Infants and Toddlers with Disabilities.

The federal programs that have been added by the State as part of the State Cluster Subsidized Child Care cluster, TANF (93.558) and Social Service Block Grant (93.667), are separated from the federal cluster Child Care Development Fund Cluster. Also a footnote or note that identifies these State Cluster of programs is referenced in the cluster and included in the Notes to the Schedule of Expenditures of Federal and State Financial Awards.

**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

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need this information to adequately make a management decision. The LGC will reject single audit reports that have compliance findings and either no questioned cost 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.

### **Yellow Book Audits and References to OMB Circular A-133**

Audits performed under GAGAS and not requiring a Single Audit should not reference OMB Circular A-133 requirements as this may be misleading to the users of the audit report. The reference “required by OMB...” should not appear in Auditor’s Independence Report and the basis of presentation note in the Schedule of Expenditures of Federal and State Awards (SEFSA). Audits performed under GAGAS do not require a summary of auditor’s results and schedule of prior year audit finding.

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.nctreasurer.com>, 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@nctreasurer.com](mailto:james.burke@nctreasurer.com).