

SAO STATE OF GEORGIA

Internal Controls

A-133 & Sub-recipient Monitoring Guidance

2009

STATEWIDE COMPLIANCE DIVISION

A-133 & Sub-recipient Monitoring Guidance

PURPOSE AND OVERVIEW

State Agencies who receive Federal awards are required to design internal controls which help to ensure compliance with Federal laws, and regulations as per the A-102 Common Rule and OMB Circular A-110 (2 CFR part 215). This guidance, along with the accompanying tools, is intended to assist your agency in complying with these requirements by outlining a framework for effective internal controls. This guidance may not necessarily reflect how your agency chooses to implement effective internal controls, but is intended to serve as a tool to assist in evaluating their effectiveness. Your agency is expected to determine the most appropriate and cost effective internal controls applicable to your environment which serve to provide reasonable assurance for compliance with Federal program requirements.

A sound system of internal controls should meet the following objectives:

- Verify that transactions are recorded in a manner which allows your agency to prepare accurate reliable financial statements, and which,
- Comply with applicable laws and regulations as well as any other provisions of the grant award agreement, and which,
- Help safeguard against loss.

COMPLIANCE REQUIREMENTS

OMB Circular A-133 Identifies 14 types of Compliance Requirements. Recipients of Federal awards should establish internal control objectives specific to each area as it applies to their particular grant award as identified in OMB A-133 Part 2, Matrix of Compliance Requirements. A brief description of the 14 types of compliance requirements are listed below.

Activities Allowed or Un-allowed (A)

Each Federal award is funded for a specific purpose, and funds provided under each program should only be used for activities which benefit the intended purpose of the award.

Allowable Costs/Cost Principles (B)

This compliance requirement covers the cost accounting policies, expenses and expenditures, and actual use of Federal funds associated with the administration of a Federal assistance program. In other words, it provides the basis and principles for which recipients must adhere to when expending the assistance they have received.

The OMB has issued a Cost Principle Circular for each of the recipient categories below:

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- OMB Circular A 87, “Cost Principles for State, Local, and Indian Tribal Governments”
- OMB Circular A-21, “Cost Principles for Educational Institutions”
- OMB Circular A-122, “Cost Principles for Non-Profit Organizations”

The three circulars list various types of cost or expense item (such as travel expense, maintenance expense, payroll salaries, lobbying costs, purchase of materials, payment of utility bills, etc.), and establishes whether each is either allowable or unallowable.

Cash Management (C)

This section covers the actual management, or handling, of funds pertaining to a Federal program, specifically on how Federal assistance is distributed to recipients and how recipients manage the funds until disbursement. The actual transfer of funds, commonly referred to as “draw-downs”, is usually done electronically by requesting the funds to the Federal agency via website or a network. The funds are automatically transferred from the US Department of Treasury to the recipient’s bank account. Federal assistance for program operations is provided to recipients usually by one of two methods, also called “funding techniques”: by either advances of funds or by reimbursement of funds.

- Advances of funds – Advances are Federal funds provided to a recipient before the program activity is performed.
- Reimbursement of funds – This funding technique requires the recipient to pay program expenditures with their own funds, and then request a reimbursement for those expenses from the Federal government or pass-through entity.

Davis-Bacon Act (D)

As part of the US Department of Labor’s (DOL) government wide implementation of the Davis-Bacon Act, Federal regulations require that all laborers and mechanics employed by a contractor or subcontractor to work on construction contracts in excess of \$2,000 which are financed by Federal assistance funds must be paid wages not less than those established by the DOL for the geographic location of the project, also known as the prevailing wage rate. The clause should also include a requirement for the contractor to submit to the recipient a weekly copy of certified payrolls.

Eligibility (E)

The main objective of this compliance requirement is that only eligible individuals or organizations participate in Federal assistance programs. To comply with this objective recipients must assure that proper eligibility determinations are made for the specific program in accordance with the program’s purpose, and also obtain evidence of such compliance.

Equipment and Real Property Management (F)

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Equipment is defined as tangible property acquired using Federal assistance funds, having a useful life of more than one year, and an acquisition cost of \$5,000 or more per unit. Recipients must use the equipment for Federal program for which it was acquired, and must maintain proper records of this equipment as well as implement an appropriate internal control system to safeguard and maintain the equipment. If sold, a proportion is returned to the Federal government equal to the proportion of Federal funds used to obtain the equipment. Real Property acquired by recipients using Federal awards must be used for the originally authorized purpose or other federally sponsored projects or programs as authorized. If the property is sold, a share is provided to the Federal government equal to the proportion of Federal funds used to acquire the item.

Matching, Level of Effort, Earmarking (G)

Certain Federal awards may require recipients to provide a level of contributions to a Federal program, to maintain specific levels of performance or achievement, or to restrict the amount of Federal funds used for a specific purpose.

Matching, also referred to as “cost sharing”, is a requirement for the recipient to provide contributions or donations (usually non-Federal) of a specified amount or percentage to supplement Federal assistance received.

Level of effort defines particular goals or objectives the recipient must achieve with the assistance received, and includes requirements for a specified level of service to be provided.

Earmarking is a requirement that specifies a limit amount or percentage of the program’s assistance that must (minimum) or may be used (maximum) for specified activities, i.e., administrative expenses.

Period of Availability of Federal Funds (H)

This compliance requirement identifies that individual Federal grants are awarded for a specified time period, generally one year. Federal regulations prohibit the use of funds from a grant award outside its specified timeframe unless authorized by a Federal agency.

Procurement and Suspension and Debarment (I)

Procurement of goods and services from a vendor must be obtained in compliance with laws and regulations, allowing for open competition and a fair selection process. Certain non-Federal entities may have been prohibited from receiving Federal assistance, through suspension or debarment, due to previous non-compliance. When purchasing a good or service, the recipient must verify that the vendor or owners/upper management have not been suspended, debarred or otherwise excluded by the Federal government.

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Program Income (J)

Occasionally program income may be received on a federally funded program, through rent, fees, sales of program goods or services, etc. This income may be added to the program budget, or be used to replace a portion of existing funding, or in some cases may be used to satisfy program matching requirements.

Real Property Acquisition and Relocation Assistance (K)

Under the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (URA), any person displaced by a Federal programs from their home, businesses, or farm, is entitled to just compensation and assistance in relocation. Additionally, the property should be appraised by an independent appraiser and reviewed and certified to have met an accepted fair value.

Reporting (L)

All recipients of Federal awards must submit reports to the Federal government to track program activity, both financial and performance related. Some of these reports may vary by award or by recipient and may have varying deadlines, while other standardized reports have been established which apply to all recipients.

Sub-recipient Monitoring (M)

Any recipient of a Federal award, who passes some or all of that assistance to another recipient, or sub-recipient, is responsible to monitor the award activities of that sub-recipient. Sub-recipient monitoring may consist of review of sub-recipient single audit findings and corrective action plans, site visits, review of agreed upon sub-recipient reports, as well as additional communication and training.

Special Tests and Provisions (N)

Certain programs have specific and unique compliance requirements established by laws, regulations, and the provisions of contract or grant agreements pertaining to the program which do not fit into any of the requirements listed above. This sections covers those unique those requirements. The auditor must review the program's contract and grant agreements and referenced laws and regulations to identify the unique compliance requirements and develop audit objectives and audit procedures under this section.

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COSO INTERNAL CONTROL COMPONENTS

The characteristics of internal control can be represented using the five components of the COSO (Committee of Sponsoring Organizations of the Treadway Commission) internal control framework. These components allow an entity to analyze their internal control system and evaluate their ability to comply with applicable laws, regulations and program requirements. The five components of the COSO internal control framework are as follows:

Control Environment – The control environment sets the tone of an organization and serves as the foundation for the other components of internal control. Factors which define the control environment of an organization include conducting business ethically through a published code of conduct, positive responsiveness by management and adherence to program compliance requirements, clearly defined responsibilities, adequate knowledge at both the staff and management levels, and adequate training and information systems.

Risk Assessment – Risk assessment entails the identification and evaluation of relevant risks which may have an impact on achieving program objectives. Risk assessment provides a basis for determining how risks should be managed. Risk assessment involves staff understanding of the key program objectives, identifying areas and individuals which require increased supervision, knowledge of status of previous audits and reviews, and ability to implement changes as needs are identified.

Control Activities – These are the organizations' policies and procedures which are implemented to help ensure that organizational directives are followed. Control activities should exist throughout all levels of the organization. Some examples of Control Activities include, but are not limited to, clearly written policies and procedures, reconciliations, approvals, segregation of duties, securing assets, employee supervision, and computer systems controls, including restricted access and override prevention.

Information and Communication – The process of exchanging of information in a format and time frame that enable people to carry out their responsibilities. Exchange of information can be between individuals or through system produced reports. Communication should flow upwards and downwards, and be both internal and external to outside customers and stakeholders. Accurate communication should be timely and should include necessary supporting documentation. Actions should be taken as a result of the communication.

Monitoring – The quality of internal controls should be monitored and evaluated over time. Monitoring may exist in the form of periodic reports and reconciliations, staff review sessions, site visits, and internal audits. Monitoring should include identifying deficiencies to determine the root cause and ensuring that corrective action is implemented.

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SUBRECIPIENT MONITORING

At the time of the award, a pass-through entity is responsible for identifying important Federal award information to the sub-recipient, such as CFDA title and number, award name and number, and applicable compliance requirements.

Risk Monitoring

The pass through entity should take steps to evaluate the level of risk of any potential sub-awards. The following examples are factors that may affect the level of risk and have an impact on nature, timing, and extent of during-the-award monitoring:

- Program complexity – Programs with complex compliance requirements have a higher risk of non-compliance.
- Percentage passed through – Awards with large percentages of program dollars passed through have a greater need for sub-recipient monitoring.
- Amount of award – Larger dollar awards are of greater risk.
- Sub-recipient risk – Certain sub-recipients may carry higher risk. New sub-recipients as well as existing sub-recipients with a history of non-compliance would probably require increased levels of monitoring.

During-the-Award Monitoring

For the duration of the sub-award, the pass-through entity is responsible for monitoring the sub-recipient's use of Federal awards to provide reasonable assurance that the sub-recipient is achieving stated performance goals and demonstrates compliance with laws, regulations, and the provisions of the grant agreement. These monitoring activities are on-going throughout the year, and may consist of:

- Reporting – This requires reviewing established periodic financial and performance reports submitted by the sub-recipient.
- Site Visits – Performing a site visit at the sub-recipient allows for the observation of operations and the review of supporting records.
- Regular Communication and Training – Keeping in regular contact with sub-recipients promotes increased feedback and may include training as appropriate to address sub-recipient concerns.

Sub-recipient Audits

Entities with sub-recipients which have expended \$500,000 or more in Federal awards during the fiscal year, must ensure that the sub-recipient has met the Single Audit requirements outlined in OMB Circular A-133, (located at: <http://www.whitehouse.gov/omb/circulars/a133/a133.html>). Additionally, the pass-through entity should ensure that a management decision is issued after receipt of the sub-recipient's audit report, and that the sub-recipient takes appropriate corrective action in a timely manner.