Memorandum #2016-11

TO: State Agencies, Independent Auditors, North Carolina Local Governments and Public Authorities, interested parties

FROM: Sharon Edmundson, Director, Fiscal Management Section

SUBJECT: Changes to State Single Audit Implementation Act

DATE: February 26, 2016

In December 2013, the U.S. Office of Management and Budget (OMB) issued *Uniform Administration Requirements, Cost Principles, and Audit Requirements for Federal Awards, Final Rule*, (Uniform Guidance)\(^1\) that establishes uniform cost principles and audit requirements for federal awards to nonfederal entities and administrative requirements for all federal grants and cooperative agreements. Subpart F of the Uniform Guidance addresses the audit requirements. Among the changes, thresholds for federal single audits will increase from $500,000 to $750,000. The Type A/B major program determination has increased from a minimum of $300,000 to $750,000. For auditees not considered low risk, the percentage of coverage rule requirement has been reduced from 50% to 40%. Auditees that are determined to be low-risk may have 20% of federal expenditures audited, a decrease from the current requirement of 25%. The effective date of Subpart F of the Uniform Guidance is for years ending on or after December 15, 2015, which is June 30, 2016 for most local governments and public authorities in North Carolina.\(^2\) We have included in this memo a discussion to changes to federal single audit changes resulting from Subpart F of the Uniform Guidance.

Changes to the State Single Audit requirements

Whenever OMB changes their single audit requirements, we, under the authority of G.S. 159-34, assess the current State Single Audit requirements and make any appropriate changes. State single audit requirements will be adapted to reflect changes resulting from the Uniform Guidance. The effective date for changes to the State Single Audit Implementation Act is for years ending on or after June 30, 2016.

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\(^2\) Units of governments in North Carolina that have years ending December 31 and March 31 include Public Housing Authorities, Hospitals, and one Airport Authority. The changes to the State Single Audit Implementation Act will not affect these entities, so it was decided to implement changes to the State requirements at June 30, 2016 after Subpart F of the Uniform Guidance was implemented.
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The following summarizes the changes to the State Single Audit Implementation Act.

- No change to the current State Single Audit threshold of $500,000.
- Change the threshold to determine a major program to $500,000 from the current threshold of $300,000.
- Reduce the percentage of coverage of State awards to 40% from the current percentage of 50%. As it is currently, there will be no low-risk auditee determination for State awards.

Sections of the Uniform Guidance that will apply to the State Single Audit Implementation Act are as follows:

<table>
<thead>
<tr>
<th>Section</th>
<th>Subpart A</th>
<th>Definitions, as applicable</th>
</tr>
</thead>
<tbody>
<tr>
<td>200.502</td>
<td>Basis for determining awards expended</td>
<td></td>
</tr>
<tr>
<td>200.330</td>
<td>Sub-recipient and contractor determination</td>
<td></td>
</tr>
<tr>
<td>200.503 (a, b, c)</td>
<td>Relation to other audit requirements</td>
<td></td>
</tr>
<tr>
<td>200.505</td>
<td>Sanctions</td>
<td></td>
</tr>
<tr>
<td>200.508</td>
<td>Auditee responsibilities</td>
<td></td>
</tr>
<tr>
<td>200.509</td>
<td>Auditor selection</td>
<td></td>
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<tr>
<td>200.510</td>
<td>Financial statements</td>
<td></td>
</tr>
<tr>
<td>200.511</td>
<td>Audit findings follow-up</td>
<td></td>
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<tr>
<td>200.331</td>
<td>Requirements for pass-through entities</td>
<td></td>
</tr>
<tr>
<td>200.521 (a, c, d, e)</td>
<td>Management decision</td>
<td></td>
</tr>
<tr>
<td>200.514</td>
<td>Scope of the audit</td>
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<tr>
<td>200.515</td>
<td>Audit reporting</td>
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<tr>
<td>200.516</td>
<td>Audit findings</td>
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<tr>
<td>200.517</td>
<td>Audit documentation</td>
<td></td>
</tr>
<tr>
<td>200.519</td>
<td>Criteria for program risk</td>
<td></td>
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</tbody>
</table>

A discussion of each of the sections referred to above can be found in “Discussion of Single Audit in North Carolina”3, which is part of the Audit Manual for Governmental Auditors in North Carolina. Sections of the Uniform Guidance that do not apply to State awards are also discussed, such as audit costs ($200.506) and major program determination ($200.518).

Changes to the Federal Single Audit Requirements

As mentioned before, the audit requirements for federal Single Audits are effective for fiscal years ending on or after December 15, 2015. Some of the more significant changes include:

Audit requirements: The threshold for a federal Single Audit has increased to $750,000 of federal awards expenditures per year. The previous threshold was $500,000.

Type A programs threshold: The thresholds for Type A and Type B programs were revised. The minimum threshold has increased to $750,000 from $300,000. This threshold applies to

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3 As of the date of this memorandum, “Discussion of Single Audit in North Carolina” is being updated and should be available March 1, 2016.
entities with total annual federal award expenditures of $750,000 to $25 million. After $25 million, the threshold increases according to the following:

<table>
<thead>
<tr>
<th>When total federal award expenditures are...</th>
<th>Type A/B threshold will be...</th>
</tr>
</thead>
<tbody>
<tr>
<td>$750,000 ≤ $25 million</td>
<td>$750,000</td>
</tr>
<tr>
<td>$25 million ≤ $100 million</td>
<td>.03 times total federal awards expended</td>
</tr>
<tr>
<td>$100 million ≤ $10 billion</td>
<td>$3 million</td>
</tr>
<tr>
<td>$1 billion ≤ $10 billion</td>
<td>.003 times total federal awards expended</td>
</tr>
<tr>
<td>$10 billion ≤ $20 billion</td>
<td>$30 million</td>
</tr>
<tr>
<td>$100 million ≤ 1 billion</td>
<td>.00015 times total federal awards expended</td>
</tr>
</tbody>
</table>

**Large loan programs:** When a federal program providing loans exceeds four times the largest non-loan program, it is considered a large loan program and the auditor must 1) consider this federal program as a Type A program; and 2) exclude its values in determining other Type A programs. This recalculation of Type A programs is performed after removing the total of all large loan programs.

**Cluster of programs:** A cluster of programs is treated as one program in determining Type A programs. If there is a large loan program that comprises less than 50% of a cluster, a cluster is not considered to be a loan program.

**Type A programs low-risk requirements:** There were changes to the requirements for determining whether a Type A program is to be considered low-risk. Currently, a Type A program may be considered low-risk if it had a significant deficiency in internal controls and/or a material noncompliance finding. In order to be low-risk under Uniform Guidance, the program:

- Must have been audited as major in one of the most recent two years
- Must not have had any of the following in the most recent audit period:
  - Modified opinion (new requirement)
  - Material weakness in internal control
  - Known or likely questioned costs that exceed 5% of total expenditures of the program (new)

**Audit of high risk Type B program requirements:** The Type B program requirements have changed. The maximum number of high-risk Type B programs that the auditor is required to test is one-fourth the number of low-risk Type A programs. The auditor is only required to perform risk assessment on Type B programs that exceed 25% of the Type A threshold. There is no longer an Option 1 or 2. For entities that expend $25M or less, risk assessment is not required on programs with less than $187,500 of expenditures. This should result in less testing of high-risk Type B programs.

**Percentage of coverage rule requirements:** The percentage of coverage rule requirement for auditees not considered low-risk has been reduced from the current 50% to 40%. Auditees that are
determined to be low-risk may audit 20% of federal expenditures, a decrease from 25% under previous guidance.

Criteria for low-risk auditee status: The criteria for low-risk auditee status have changed; there are two new requirements and two of the remaining requirements have been modified. To be a low-risk auditee, the entity must meet the following conditions for each of the two preceding audit periods:

- Timely completion of Single Audits and submission of the Data Collection form to the Federal Single Audit Clearinghouse. This does not apply to the submission to the Local Government Commission.
- Per the auditor’s opinion, the financial statements were prepared in accordance with GAAP or a basis of accounting required by state law \(\text{new requirement}\)
- Unmodified opinion on financial statements and on the schedule of expenditures of federal awards (the cognizant agency or pass-through agency can no longer provide a waiver)
- No deficiencies in internal control identified as material weaknesses under the requirements of GAGAS.
- The auditor did not report a substantial doubt about the auditee’s ability to continue as a going concern. \(\text{new requirement}\)
- No Type A programs had:
  - material weaknesses
  - modified opinion on compliance (this modified the previous requirement of no material noncompliance finding)
  - questioned costs greater than five percent of federal awards expended

Questioned costs threshold: The threshold for reporting questioned costs has increased to $25,000 from $10,000

Schedule of Expenditures of Federal and State Awards (SEFSA): The total federal awards expended for loan and loan guarantees are required to be reported on the face of the schedule. This is in addition to the requirement that that the amount of loan outstanding be included as a note to the schedule.

For a cluster of programs, the total amount expended for the cluster should be presented.

Summary of Prior Audit Findings: If a prior year finding was not fully corrected, a description for the reason for the reoccurrence is required.

Other notable changes:

- Federal agencies (or other agencies) do not have the authority to grant extensions of the due date for submitting reports.
The terms “must” and “should” are included. The term “must” is used in the Uniform Guidance denotes a requirement. “Should” is used to indicate a recommendation, but not a requirement. The terms “must” and “should” differ from those in the auditing standards.

The term “contractor” has replaced the term “vendor.” A sub-recipient may either be a contractor or a sub-recipient. The non-federal entity may concurrently receive federal awards as a recipient, a sub-recipient, and as a contractor.

There are changes to the Single Audit reporting package requirements: Unless restricted by Federal statutes or regulations, the auditee must make copies available for public inspection. Auditees and auditors must ensure that their respective parts of the reporting package do not include protected personally identifiable information.

If you have questions about these changes, please contact Jim Burke at (919) 814-4301 or via email at james.burke@nctreasurer.com or Manasa Cooper at (919) 814-4296 or via email at manasa.cooper@nctreasurer.com.