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SINGLE AUDIT

Single Audit Act Effectiveness Issues

Statement of Sally E. Thompson
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Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to (1) discuss our report,¹ which is being released at this hearing, on the efforts of the Departments of Education, Housing and Urban Development (HUD), and Transportation to ensure that federal award recipients take timely and appropriate actions to correct all single audit findings, and (2) highlight three issues that merit additional attention to ensure that single audit efforts are achieving the full benefits envisioned in the act.

Our review of the efforts of Education, HUD, and Transportation to ensure that federal award recipients corrected single audit findings generally found a lack of the required documentation of management decisions on audit findings and the evaluation of and conclusions on the adequacy of recipient actions to correct single audit findings. In commenting on the report, Education and HUD agreed with the findings and are moving forward to implement the recommendations. Transportation's comments raised several issues concerning both the scope of our audit work and the appropriateness of our conclusions and recommendations. Despite the comments and the issues raised, we continue to believe that our conclusions are sound and that the recommendations for agency actions are needed to help ensure the overall effectiveness of agencies' implementation of the Single Audit Act and their consideration and use of single audit findings.

The Federal Audit Clearinghouse, the organization the Office of Management and Budget (OMB) designated to receive single audit reports from federal award recipients, received about 34,000 single audit reports during calendar year 2000. About 5,500 of these reports contained audit findings. Despite these impressive figures, several single audit-related issues merit additional attention. These issues involve questions about whether (1) all required single audits are performed, (2) federal award recipients are adequately monitoring subrecipient² use of federal awards and the correction of single audit findings, and (3) the audits are performed in accordance with government auditing standards.

¹U.S. General Accounting Office, *Single Audit: Actions Needed to Ensure That Findings Are Corrected*, [GAO-02-705](#) (Washington, D.C.: June 26, 2002).

²A subrecipient is a nonfederal entity that expends federal awards received from another nonfederal entity (i.e., the federal award recipient) that received awards directly from a federal agency to carry out a federal program.

According to OMB, federal awards for fiscal year 2001 totaled about \$325 billion of the \$1.8 trillion federal budget. These awards include grants, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, food commodities, and direct appropriations and federal cost reimbursements. The Single Audit Act, passed in 1984 and amended in 1996, is intended to, among other things, promote sound financial management, including effective internal controls, with respect to federal awards administered by state and local governments and nonprofit organizations. Under OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, those governments or organizations that expend \$300,000 or more in federal awards during the fiscal year shall (1) maintain internal control for federal programs, (2) comply with laws, regulations, and the provisions of contracts or grant agreements, (3) prepare appropriate financial statements, including the Schedule of Expenditures of Federal Awards, (4) ensure that the required single audits are properly performed and submitted when due, and (5) follow up and take corrective actions on audit findings.

Three Agencies' Practices to Ensure Correction of Single Audit Findings

As discussed in the report we are releasing today, our work to review agency actions to ensure that recipients take timely and appropriate corrective actions to fix audit findings contained in single audit reports identified a number of fundamental concerns. Education, HUD, and Transportation had procedures in place to establish responsibility for identifying and reviewing single audit findings and for communicating that information to appropriate officials for action. However, the audit files at these agencies generally did not contain documentary evidence that the agencies had prepared management decisions, as required by OMB Circular A-133, to notify the recipients of the corrective actions the federal agencies deemed necessary to correct the audit findings. Also, the files generally did not contain evidence that agency personnel had evaluated and concluded on the adequacy of the recipients' actions to correct the findings contained in single audit reports.

OMB Circular A-133 requires each federal agency to issue a written management decision on audit findings within 6 months of the receipt of the recipient's single audit report. (It is important to note that as many as 15 months could pass after the recipient's year-end date before the Single Audit Act, as amended, requires a management decision. This occurs because the legislation gives recipients up to 9 months after the period audited to file their single audit reports, and agencies have an additional 6 months to issue the management decisions.) These decisions document

management's conclusions on and notification to recipients on the adequacy of their planned, in progress, or completed actions to correct audit findings. In order to gauge agencies' practices in this area, we selected the 10 grantees awarded the most money for the two largest programs at each of the three agencies. Our analysis of actions related to the 20 single audits from each agency showed that collectively they had issued management decisions for only 75 (31 percent) of the 246 audit findings contained in the single audit reports included in our review.

The agencies noted several reasons for not preparing written management decisions including that (1) they considered the audit findings to be insignificant or not serious, (2) the single audit report stated that the recipient had corrected the finding prior to the report's issuance, and (3) the subsequent year's single audit report indicated that the recipient had corrected the finding. In our view, none of the reasons cited justify the nonissuance of a management decision. For example, by including a finding in a single audit report, auditors are indicating that the finding is significant since government auditing standards require auditors to report all significant findings in the report. The standards identify other means of communicating insignificant findings. Regarding the use of subsequent-year single audit reports to justify the nonissuance of a management decision, it should be noted that single audit reports must be issued no later than 9 months after the recipient's year-end. By waiting for the subsequent year's audit report, as many as 21 months could have expired from the end of the audit period for which the finding was initially reported to the receipt of the subsequent year's audit report. In our opinion, waiting for the subsequent audit report would not result in a timely notification to the recipient of the agency's position on an audit finding and the recipient's planned, in progress, or completed corrective actions.

OMB Circular A-133 does not distinguish between the types of findings or their seriousness when requiring written management decisions. In fact, ensuring that reported problems have been resolved is a central requirement under OMB Circular A-133. The circular requires agencies to ensure that federal award recipients take appropriate and timely corrective action on audit findings. Program officials at Education, HUD, and Transportation told us that they follow up on the implementation of corrective actions through such activities as site visits, phone conversations, and review of the subsequent year's single audit reports. However, we found very little documentation that demonstrated agency follow-up actions to ensure that recipients took the necessary corrective actions on single audit findings or the results of the follow-up activities

cited above. While the audit files contained copies of recipient documents and other records, the files did not contain agency evaluations of or conclusions on the adequacy of the recipient actions cited in those records. This type of documentation is critical because each of the agencies we reviewed relied heavily on program, regional, or field offices to ensure that corrective actions occurred, yet none required reporting on the corrective action status of all single audit findings. We believe that the follow-up efforts should be documented and that doing so is a key to ensuring that agency offices perform their responsibilities to help ensure that recipients take all necessary corrective actions.

Single audits provide valuable information that agency managers can use to make operating decisions, monitor performance, and allocate resources. However, discussions with officials at each of the three agencies revealed that, even when program or other offices had information on single audit results and recipient actions to correct single audit findings, this information was not communicated to top-level agency management for review, analysis, and possible action. This reporting can strengthen accountability and oversight by providing management with information useful in the analyses of both programwide problems and recurring problems at specific recipients. Further, it can provide management officials with information relevant to agency efforts to reduce improper payments—a key element of *The President's Management Agenda, Fiscal Year 2002*, initiative to improve financial performance.

The report we are issuing today contains recommendations that call for the following actions by the Secretaries of Education, HUD, and Transportation.

- Ensure that the agency has established and follows guidance to address the OMB Circular A-133 requirements for all agencies whose awards are subject to the Single Audit Act, as amended. This guidance should address areas such as (1) preparing and issuing timely management decisions that clearly communicate the results of agency analyses of single audit findings and the adequacy of corrective actions implemented or planned by the recipient, (2) performing follow-up procedures to ensure that the recipient implemented adequate corrective action on a timely basis, and (3) documenting the results of evaluations of and conclusions on recipients' actions to correct audit findings.

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- Implement policies and procedures for reporting information to top-level agency management on the (1) types and causes of findings identified in single audit reports and (2) status of corrective actions.

Other Single Audit Issues

Aside from the federal agencies' responsibility for taking all necessary actions to ensure that recipients implement timely and appropriate corrective actions to fix single audit findings, a number of other single audit-related issues exist. These include questions about whether

- all required single audits are conducted,
- recipients perform the required monitoring of subrecipients' uses of federal awards and follow up to ensure that they take timely and appropriate corrective actions on audit findings, and
- all single audits comply with government auditing standards.

The Single Audit Act, as amended, requires audits by recipients that expend \$300,000 or more in federal awards during the fiscal year. Currently, the federal government does not know or have a method for determining the universe of recipients and subrecipients that meet this \$300,000 threshold. In general, while the federal government does have disbursement systems that can identify amounts the federal government awards recipients, it does not have a system or systems to accumulate, track, and report on amounts actually expended by award recipients and subrecipients across the federal government. As a result, it is not possible to determine whether required single audits occur, identify recipients and subrecipients that have not had required single audits, or develop adequate follow-up systems to ensure that all required audits occur. Thus, in many respects, what we have is an honor system as to which recipients are arranging for single audits.

This information on the audit universe is important if federal agencies are to have any assurance that recipients and subrecipients receiving federal awards are receiving the required audits of their financial and internal control systems and of their compliance with applicable program laws and regulations. In addition, by ensuring that all required audits are conducted, federal managers will receive more complete information on audit findings useful in their governmentwide, agencywide, and recipient-specific analyses of single audit results and the \$325 billion in federal awards.

Under OMB Circular A-133, federal agencies are to receive single audit reports with findings relating only to award recipients that received federal awards directly from the agencies. When these recipients, such as states, forward awards to subrecipients such as municipalities, counties, or local governmental units, it becomes the recipient's responsibility under the circular to make sure that the subrecipients obtain single audits and that they take appropriate action to correct single audit findings.

A review of the Federal Audit Clearinghouse database³ for calendar year 2000 showed about 380 cases where the auditors reported that award recipients were not adequately monitoring their subrecipients to ensure that they complied with all of the requirements of the Single Audit Act, as amended. While a very small percentage of the total single audits, these cases can be significant because they often represent recipients that receive large amounts of federal awards, such as states, and pass those awards to subrecipients for program performance purposes. Therefore, it is very important for federal agencies to have assurances that the recipients take actions to ensure that their subrecipients take appropriate and timely actions to correct all single audit findings. Currently, federal agencies do not receive information on recipients' evaluations of and conclusions on the appropriateness of subrecipient actions to correct findings identified in single audit reports. This information is important from a program management standpoint because it could identify areas where the federal government needs to increase its oversight efforts or develop and issue guidance for recipient and subrecipient use when participating in federal programs and using federal awards.

Single audit quality has been a long-standing area of concern and one about which questions have surfaced since the passage of the Single Audit Act in 1984. In this regard, OMB Circular A-133 requires that cognizant agencies (i.e., those agencies with specific single audit oversight responsibilities for recipients expending more than \$25 million annually in federal awards) conduct or obtain quality control reviews of selected single audits.

³The Federal Audit Clearinghouse single audit database was established as a result of the Single Audit Act Amendments of 1996 and contains summary information on the auditor, the recipient and its federal programs, and the audit results.

Quality control reviews are reviews of the audit work supporting an individual audit assignment. They are performed by reviewing the independent auditor's working papers. In our recent survey,⁴ which we conducted at your request, respondents reported that federal agency inspectors general from 10 agencies participated on 109 quality control reviews during fiscal year 2001. However, this total may be overstated since offices of inspectors general occasionally perform joint reviews and our survey did not capture information on the extent of these collaborative efforts. The survey responses noted that the reviews identified a range of audit problems including those involving internal control and/or compliance testing performed by the auditors and auditor compliance with government auditing standards. While this limited information on the current audit quality problems cannot be used to project to or judge the quality of all single audits performed, it at least raises the possibility that problems continue to exist. OMB and federal agencies have recognized this potential problem, but a solution or approach to evaluating the overall quality of single audits conducted and developing a methodology to address all problems identified has not yet been developed.

Mr. Chairman, this concludes my statement. I would be happy to answer any questions you or other members of the subcommittee may have.

Contact and Acknowledgments

For information about this statement, please contact Sally Thompson, Director, Financial Management and Assurance, at (213) 830-1065 or at thompsons@gao.gov. Individuals who made key contributions to this testimony include Tom Broderick, Marian Cebula, and Perry Datwyler.

⁴U.S. General Accounting Office, *Single Audit: Survey of CFO Act Agencies*, [GAO-02-376](#) (Washington, D.C.: Mar. 15, 2002).