## OFFICE OF MANAGEMENT AND BUDGET

### Audits of Institutions of Higher Education and Other Non-Profit Institutions

**AGENCY:** Office of Management and Budget.

**ACTION:** Final Revision of OMB Circular A–133, ''Audits of Institutions of Higher Education and Other Non-Profit Institutions.''

**SUMMARY:** This revision of Office of Management and Budget (OMB) Circular A–133 establishes a uniform system of auditing for institutions of higher education and other non-profit organizations. One of the more significant revisions is that the threshold for when an entity is required to have an audit is raised from $25,000 to $300,000. This will significantly reduce audit costs for many small non-profit organizations. Other significant changes are: additional guidance for program-specific audits (§ _____.235), audit findings (§ _____.510), and audit findings follow-up (§ _____.315); a report submission due date which is shortened from 13 to 9 months and a report submission process that includes a certification form and streamlined filing requirements (§ _____.320); and, a new risk-based approach for major program determination (§ _____.520).

**DATES:** The standards set forth in § _____.400 of the Attachment to this Circular, which apply directly to Federal agencies, shall be effective July 1, 1996, and shall apply to audits of fiscal years ending on or after June 30, 1997. The standards set forth in this Circular that Federal agencies are to apply to non-profit organizations shall be adopted by Federal agencies in codified regulations not later than November 30, 1996, so that they will apply to audits of fiscal years ending on or after June 30, 1997, with the exception that § _____.305(b) of the Attachment applies to audits of fiscal years ending on or after June 30, 1999.

**ADDRESSES:** A copy of the Circular may be obtained from the OMB fax information line, 202–395–9068, document number 1133; OMB home page on the internet which is currently located at http://www.whitehouse.gov/WH/EOP/omb; or by writing or calling the Office of Administration, Publications Office, room 2200, New Executive Office Building, Washington, DC 20503, telephone (202) 395–7332.

**FOR FURTHER INFORMATION CONTACT:** Recipients should contact their cognizant or oversight agency for audit, or Federal awarding agency, as may be appropriate in the circumstances. Subrecipients should contact their pass-through entity. Federal agencies should contact Sheila O. Conley, Office of Management and Budget, Office of Federal Financial Management, Financial Standards and Reporting Branch, telephone (202) 395–3993, fax (202) 395–4915.

**SUPPLEMENTARY INFORMATION:**

A. Background

The Office of Management and Budget (OMB) received approximately 150 letters providing approximately 1600 individual comments in response to the Federal Register proposal of March 17, 1995 (60 FR 14594–14606). Letters came from Federal agencies (including Offices of Inspectors General), State governments (including State auditors), certified public accountants (CPAs), internal auditors, non-profit organizations (including colleges and universities), professional organizations, and others. All comments were considered in developing this final revision.

Section B presents a summary of the major public comments grouped by subject and a response to each comment. Other changes were made to increase clarity and readability.

B. Public Comments and Responses

*Common Rule Format*

*Comment*: Several commenters suggested that the implementation of the Circular be done using the ''common rule'' format so that all affected Federal agencies could codify the provisions of the Circular without change and prior to the effective date.

*Response*: Circular A–133 was reformatted to facilitate codification by Federal agencies.

*Uniform Audit Requirements*

*Comment*: In the preamble of the proposed revision, OMB stated a plan to seek modifications to the Single Audit Act of 1984 (31 U.S.C. Chapter 75) and OMB Circular No. A–128, ''Audits of State and Local Governments,'' such that one law and one circular could cover both State and local governments and non-profit organizations. Commenters strongly supported this change.

*Response*s: Even though Circular A–133 does not apply to State and local governments, provisions were made to easily adapt Circular A–133 to include State and local governments if the Single Audit Act is amended. For example, changes were made to the risk-based approach to determine major programs for circumstances that most likely will only occur in large Statewide single audits.

*Increased Threshold for Audit*

*Comment*: Commenters overwhelmingly supported raising the threshold for audit, with the majority supporting the proposed threshold of $300,000. A common statement in favor of this change was that it would reduce audit costs, while still providing adequate audit coverage of Federal programs.

*Response*: This final revision raises the audit threshold to $300,000. Pass-through entities should make appropriate changes in their agreements with subrecipients to reflect that Circular A–133 no longer requires an audit for entities expending less than the $300,000 threshold. Also, pass-through entities will need to consider this change, review their overall subrecipient monitoring process, and decide what, if any, additional monitoring procedures may be necessary to ensure subrecipient compliance for the subrecipients not required to have a Circular A–133 audit. It is expected these monitoring procedures could be more targeted and less costly than the full Circular A–133 audit.

*Special Provision for Certain Small Subrecipients*

*Comment*: Most commenters opposed the provision to allow Federal agencies to require pass-through entities to arrange for audits of subrecipients receiving less than the $300,000. A reason often cited was that this provision defeats the purpose of raising the audit threshold.

*Response*: This provision was included in the proposed revision to provide audit coverage of Federal programs, such as the Job Training Partnership Act (JTPA) programs, which are structured such that substantial service delivery and expenditure of Federal funds are made by subrecipients that expend less than $300,000 in Federal awards.

The provision has not been added to the Circular. However, it is important to note that both the pass-through entity and the pass-through entity's auditor have responsibilities for these funds even when an audit of the subrecipient is not required. The pass-through entity is still responsible to monitor the activities of the subrecipient and ensure that Federal awards are only used for authorized purposes. Additional monitoring procedures may be necessary when a material amount of program funds is passed through to subrecipients which are not audited.

The pass-through entity's auditor is responsible for performing sufficient tests to support an opinion on compliance for each major program. When subrecipients which are not audited expend a material amount of funds from a major program, the auditor will need to consider obtaining compliance assurances by reviewing the pass-through entity's records and monitoring procedures, performing additional procedures to determine compliance, such as testing the subrecipient's records, or a combination of procedures. In addition, the pass-through entity's auditor is responsible for determining whether the pass-through entity's system for monitoring subrecipients is adequate and whether subrecipient noncompliance necessitates adjustment of the pass-through entity's records.

*Consideration of Triennial Audit*

*Comment*: In the preamble of the proposed revision, OMB stated it was considering a triennial audit approach and requested comments on its feasibility. Commenters from non-profit organizations supported a triennial audit approach. Reasons cited were relief of audit burden and a reduction in the number of audits required to be reviewed as part of subrecipient monitoring.

However, Federal agency commenters were opposed to a triennial audit approach and cited problems, such as it would alert the non-profit organization in advance of which years should be audited, significantly complicate the risk-based approach for selecting major programs (e.g., under the risk-based approach a large program is only required to be audited once every three years and with triennial audits this could be once in every nine years), and result in only limited cost savings (e.g., under the triennial audit approach a financial statement audit and testing of internal control would still be required).

*Response*: The triennial audit approach was not added to the Circular. However, the Circular does provide significant audit relief to non-profit organizations by raising the audit threshold from $25,000 to $300,000, allowing a risk-based approach to selecting major programs, and streamlining the report distribution process by use of a certification form. The risk-based approach will permit low-risk non-profit organizations to reduce the percentage of Federal expenditures required to be covered as major programs. The certification form, as discussed later in this supplementary information, will simplify the pass-through entity's review of subrecipient reports which have no audit findings.

*Risk-Based Approach To Determine Major Programs*

*Comment*: Except for comments from CPAs, the commenters supported the risk-based approach as presented. CPA commenters opposed the risk-based approach and cited as reasons that it was inappropriate for the auditor to determine major programs, there could be problems in submitting a proposal to conduct a Circular A–133 audit when it is not known in advance which programs will be audited, and there would possibly be cost increases for the auditor to perform risk assessments. While State auditor commenters supported the risk-based approach, those from the larger States cited implementation problems in performing risk assessments on a large number of Type B programs.

*Response*: The auditor is best suited to determine major programs for reasons, such as independence and the understanding of risk to Federal programs obtained as part of the audit. Therefore, the proposal has been adopted, with no changes made to the requirement for the auditor to determine major programs. However, in recognition of the concerns expressed relative to larger audits, Appendix 1 (§ _____.520), Major Program Determination, was modified as follows:

Step 1 (§ _____.520(b)(1)) was modified to provide a sliding scale in determining Type A programs. This change only affects auditees with Federal expenditures over $100 million.

Step 2 (§ _____.520(c)(2)) was modified to permit a Federal agency, with OMB approval, to designate that a low-risk Type A program could not be considered low-risk. This designation could be for reasons, such as to help the Federal agency comply with Section 405 of the Government Management Reform Act (P.L. 103–356).

Step 3 (§ _____.520(d)(2)) was modified to add a sliding scale which defines relatively small Federal programs in terms of a percentage of total Federal expenditures. This benefits very large audits by reducing the number of Type B programs for which the auditor must perform risk assessments. The decrease in the total amount of Federal expenditures subject to audit will be relatively small because of the wide difference in size between the largest and smallest Federal programs.

Step 4 (§ _____.520(e)) was modified to only require one-half of the high-risk Type B programs to be audited as major and provide a limit that the number of these Type B programs audited as major need not exceed the number of low-risk Type A programs.

However, should the auditor choose not to exclude a low-risk Type A program, this would not affect the limit. The limit is on the number of low-risk Type A programs, not the number excluded. Also, even though larger dollar Type A programs may be excluded as low-risk, they may still need to be audited to meet the 50 percent rule.

To mitigate any implementation problems with the risk-based approach, the provision for deviation from use of risk criteria provided in § _____.520(i) applies to the first year this Circular is applicable and permits auditors to defer implementation of the risk-based approach for one year.

*Implementation of the Risk-Based Approach To Determining Major Programs*

*Comment*: A commenter inquired whether a Type A program may be considered low-risk when it was audited as a major program in accordance with the prior Circular A–133, issued March 8, 1990, and otherwise met the criteria in Appendix 1, step 2 to be classified as low-risk.

*Response*: The reference in Appendix 1, step 2 (§ _____.520(c)(1)) to the two most recent audit periods means audit periods in which the audit was performed either under the prior Circular A–133 or this revision. Therefore, a Type A program which meets the Appendix 1, step 2 (§ _____.520(c)(1)) criteria for low-risk based on the results of an audit performed in accordance with the prior Circular A–133 may be considered low-risk. Similarly, the reference in the criteria for a low-risk auditee in Appendix 3 (§ _____.530) to the preceding two years applies to audits performed either under the prior Circular A–133 or this revision.

*Request for a Program To Be Audited as a Major Program*

*Comment*: Several commenters expressed concern that the provision for a Federal agency or pass-through entity to request a program to be audited as a major program would significantly increase the work required for single audits and requested that it be removed. A few commenters also expressed concern that these programs would not count towards meeting the 50 percent rule.

*Response*: This provision has been adopted; however, a change was made to allow programs audited as major under this process to count towards

meeting the 50 percent rule. This process does not significantly change the authority Federal agencies and pass-through entities now have to perform additional audits as long as they pay for them. The addition is that these audits may be incorporated within the framework of the single audit and thereby eliminate duplicative audit planning and reporting. Since the Federal agency or pass-through entity must still pay the full incremental audit cost, OMB does not expect a significant increase in major programs from this provision.

It should be pointed out that any Type A program selected to be audited under this provision must be low-risk. If it were not low-risk, it would have been audited as a major program under the risk-based approach. Therefore, this provision will not reduce the number of high-risk Type B programs audited as major.

*Required Level of Internal Control Testing*

*Comment*: All CPA commenters and over half of the State auditor commenters opposed the proposed requirement for the auditor to plan the testing of internal control over Federal programs to achieve a low assessed level of control risk. Concerns included that it increases the amount of audit work, limits auditor's judgment, and is arbitrary. By contrast, one commenter stated support for the proposed requirement because it would force the auditor to look at internal control over Federal programs and to note reportable conditions when internal control is not adequate.

*Response*: The proposal has been adopted, with no changes. Some commenters appeared to understand this provision to mean that, when control exceptions are found, the auditor is required to continue testing until a low level of risk is achieved. This is not the case. The auditor is not required to expand testing to try to achieve a low level of risk. The auditor is only required to plan the audit for a low level of assessed risk and report the results of this testing.

It has been a longstanding Federal policy that the recipient of Federal funds is required to establish internal control systems to provide reasonable assurance that it is managing Federal funds in compliance with applicable laws and regulations. Also, the Single Audit Act (31 U.S.C. Chapter 75) requires the auditor to test internal control over Federal funds subject to that Act. Therefore, it is reasonable to require the auditor to plan the audit consistent with the level of internal control the recipient of Federal funds is required to maintain. Also, the Circular permits the auditor to not test internal controls which are inadequate and instead disclose a reportable condition or material weakness and perform additional tests of compliance as necessary in the auditor's judgment.

*Schedule of Expenditures of Federal Awards*

*Comment*: Most commenters supported the level of detail included in the proposal for the schedule of expenditures of Federal awards. One commenter suggested that it would be beneficial for pass-through entities to identify in the schedule the amount passed-through to subrecipients. This disclosure would tell program managers the amount of program expenditures that was subject to audit at the pass-through entity level.

*Response*: A provision has been added to encourage, but not require, pass-through entities to disclose in the schedule the total amount provided to subrecipients from each Type A program and from each Type B program which is audited as a major program. In most cases this information should be readily available and would improve the usefulness of the schedule.

*Attestation on Internal Control and Compliance*

*Comment*: The preamble to the proposed revision requested comments as to whether a requirement should be added for the audits to include a management assertion and auditor attestation for internal control or compliance. The majority of commenters were opposed to this change because it would impose additional requirements on entity management and increase audit cost.

*Response*: In light of the concerns raised, this proposed revision has not been added to the Circular.

*Criteria for Reporting Questioned Costs*

*Comment*: Commenters' views on the proposed $10,000 threshold for reporting known or likely questioned costs varied from describing it as too high, too low, or just right. Commenters expressed concern that the concept of likely questioned costs needed further clarification.

*Response*: OMB believes that the $10,000 threshold for reporting questioned costs provides the appropriate balance between reporting all questioned costs and only reporting large questioned costs. Also, audit findings which do not result in questioned costs but are material to the types of compliance requirements or an audit objective in the compliance supplements will still be reported as reportable conditions under § _____.510(a)(1) or material noncompliance under § _____.510(a)(2).

Generally accepted auditing standards require the auditor to project the amount of known questioned costs identified in the sample to the items in the major program and to consider the best estimate of total questioned costs (both known and likely) in determining an opinion on compliance. The Circular does not require the auditor to report an exact amount or statistical projection of likely questioned costs, but rather to include an audit finding when the auditor's extrapolation of these likely questioned costs is greater than $10,000.

Since the requirement for the auditor to consider likely questioned costs is not new, and since likely questioned costs which are greater than $10,000 may be significant to a Federal program, OMB believes they should be included in audit findings. In reporting likely questioned costs, it is important that the auditor follows the requirements of § _____.510(b) and provides appropriate information for judging the prevalence and consequences of the audit finding.

*Requirement To Follow Up on Prior Audit Findings*

*Comment*: One commenter expressed concern that the requirement for the summary schedule of prior audit findings to include audit findings from before the prior year may result in many old audit findings being reported year after year.

*Response*: As a practical matter, unless an audit finding is repeated in a subsequent year, there is limited value in continuing to follow up on an audit finding when the Federal agency or pass-through entity chooses to take no action. Therefore, a provision has been added stating that a valid reason for considering an audit finding as not warranting further action is that: (a) two years have passed since the audit report was filed with the central clearinghouse designated by OMB, (b) the Federal agency or pass-through entity is not currently following up on the audit finding, and (c) a management decision was not issued.

Also, for the first year the entity is audited under this Circular, the prior year report may not have included the equivalent of a summary schedule of prior audit findings. In these cases, the auditee may exercise judgment and only include, to the extent practical, audit findings before the prior year.

*Corrective Action Plan*

*Comment*: Some college and university commenters expressed concern that the requirement to list the name of the contact person responsible for corrective action precluded a non-profit organization from naming one person responsible for all audit findings.

*Response*: The proposal has been adopted, with no changes. Some commenters appeared to misunderstand this provision. It is important that a non-profit organization name a contact person or persons to be responsible for corrective action. However, contrary to the commenters' understanding, the non-profit organization has discretion to determine whether one person should be responsible for all or a group of audit findings or whether a separate person should be responsible for each audit finding.

*Pass-Through Entity's Responsibility for Subrecipient Audit*

*Comment*: A few commenters expressed concern that, unless the pass-through entity gave the subrecipient $300,000, it would be difficult to determine whether the subrecipient was required to have an audit under the Circular. Specifically, the commenters asked for guidance on how the pass-through entity could determine if the subrecipient received other Federal awards which cumulatively added up to the $300,000 threshold for audit.

*Response*: This provision has been adopted, with no changes. There was no intention that this provision require the passthrough entity to perform extensive verification procedures to determine the total Federal expenditures of a subrecipient. OMB expects that, in many cases, the pass-through entity will have knowledge of the subrecipient sufficient to estimate the subrecipient's total Federal expenditures. Another technique would be for the pass-through entity to clearly explain the audit requirements to the subrecipient and then ask the subrecipient the amount of its total Federal expenditures.

*Audit Cognizance*

*Comment*: Some college and university commenters expressed concern that the cognizant agency determination was not consistent with the proposed revision to OMB Circular A–21, ''Cost Principles for Educational Institutions'' (60 FR 7105; February 6, 1995), and could result in an entity having one cognizant agency for audit purposes and another for indirect cost rate negotiation.

*Response*: The responsibilities for audit cognizance and indirect cost negotiation are different and, therefore, the same Federal agency does not need to be cognizant for both. The name for the cognizant agency has been changed to the cognizant agency for audit to clearly distinguish it from the cognizant agency for indirect cost rate negotiation.

*Provision for Small and Minority Audit Firms*

*Comment*: One commenter expressed concern that the provision for small and minority audit firms was proposed for deletion.

*Response*: As explained in the preamble to the proposed revision, this provision was proposed to be deleted because the requirements related to small and minority audit firms are more fully covered in § _____.44(b)(4) of OMB Circular A–110, ''Uniform Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals and Other Non-Profit Organizations'' (58 FR 62992; November 29, 1993). There was no intention to change or diminish the requirements for using small and minority audit firms. To ensure that these requirements continue to receive consideration, a provision has been added to the auditor selection paragraph that, whenever possible in procuring audit services, non-profit organizations shall make positive efforts to utilize small businesses, minority-owned firms, and women's business enterprises, as stated in OMB Circular A–110.

*Restriction on Auditor Also Preparing Indirect Cost Proposal*

*Comment*: The preamble to the proposed revision requested comments on whether the auditor should also be permitted to prepare the indirect cost proposal (including similar documents, such as the cost allocation plan, or the disclosure statement required by OMB Circular A–21). All Federal agency commenters and most State auditor commenters cited at least an appearance of lack of independence when the same auditor both performed the audit and prepared the indirect cost proposal. One Federal agency commenter stated, ''In preparing the indirect cost proposal, the auditor is an advocate for the client before the Federal Government. We believe it stretches the bounds of standards for the auditor to be considered independent to audit this same indirect cost proposal for the purpose of providing assurances to the Federal Government.'' In contrast, CPAs and non-profit organizations did not see an independence problem and stated there were significant efficiency advantages for the same firm to both perform the audit and prepare the indirect cost proposal.

*Response*: A provision (§ _____.305(b)) has been added to preclude the same auditor from preparing the indirect cost proposal or cost allocation plan when indirect costs exceeded $1 million in the prior year. This threshold was chosen to limit this restriction to a relatively small number of entities, while still protecting the Federal interest. The prior year was chosen because non-profit organizations often engage the auditor before the end of the year and at this time it may be unknown whether the current year's indirect costs will exceed the $1 million threshold. Based on available data, OMB estimates that entities with indirect costs exceeding $1 million cumulatively receive approximately 90 percent of the total indirect costs charged by non-profit organizations.

This restriction applies to the base year from which financial data is used to compute the rates even though the audit of the base year financial statements is often completed before the indirect cost proposal or cost allocation plan is prepared. The base year was included to enhance the appearance of independence to the Federal agencies which rely upon the auditor's testing of information used in both the calculation and application of indirect cost rates.

The disclosure statements required by OMB Circular A–21 have been excluded from this restriction because the disclosure statement is new, many of the statements will be submitted before the effective date of this Circular A–133 revision, and the disclosure statements are expected to have a long life. Under these circumstances, it does not seem appropriate public policy to restrict auditors who prepared the original disclosure statements from performing the audit for a long period of time. Therefore, the disclosure statements required by OMB Circular A–21 have been excluded from this restriction on auditor selection. OMB will monitor these disclosure statements and may revisit this issue again at a later date.

The implementation date for this provision is delayed two years until audits of fiscal years ending on or after June 30, 1999, to minimize any effect this provision could have on existing contracts for audit services. For example, an auditor that prepared an indirect cost proposal or cost allocation which is used as the basis for charging indirect costs in the fiscal year ending June 30, 1999, is not permitted to perform the 1999 audit.

*Report Due Date*

*Comment*: Most State auditor and college and university commenters expressed opposition to shortening the due date for reports from 13 to 9 months. However, most State manager and non-profit organization commenters supported the change. The view appeared to be that those receiving and relying on the reports and those currently completing the audit in 9 months liked the change. By contrast, it appears that those who were not currently completing the audit in 9 months opposed the change.

*Response*: This proposal has been adopted, with a change. The provision retains the requirement in the Circular that, when the audit is completed earlier than the due date, the reporting package must be submitted within 30 days of audit report issuance.

*Certification*

*Comment*: Comments were mixed on the certification form. Most State auditor and CPA commenters opposed the certification form, citing it as an increased burden on them to prepare and duplicative of information in the audit reports. Most college and university commenters supported the use of the certification form as a method of reducing the volume of paper in single audits.

On a related issue, some State auditor and CPA commenters cited a possible logistical problem that the auditor would not be able to complete the audit report until the certification form was prepared (because the auditor must read the certification form and report as an audit finding material inconsistencies with the audit) and the certification form could not be prepared until the audit is completed.

*Response*: The requirements for the auditor to read the certification form and report as an audit finding any material inconsistencies has not been adopted. As a preventive control to ensure proper distribution of audit reports, a requirement (§ _____.500(f)) has been added for the auditor to identify to the auditee those Federal awarding agencies and pass-through entities which are required to receive a copy of the reporting package. Also, a requirement (§ _____.505(b)) was added for the schedule of findings and questioned costs prepared by the auditor to include a summary of the auditor's results. This summary will facilitate preparation of the certification form by the auditee.

*Management Letter*

*Comment*: Most commenters expressed concern that routinely including management letters as part of a public filing of the auditor's reports could reduce the effectiveness of management letters.

*Response*: OMB agrees that it is not necessary to routinely include auditor's management letters as part of the report submission. Therefore, this provision has not been adopted. However, because management letters may contain information relevant to the needs of Federal agencies and pass-through entities to monitor Federal awards, a provision has been added that Federal agencies and pass-through entities can request a copy of management letters.

*Coordinated Audit Approach*

*Comment*: A few commenters expressed concern that the term *coordinated audit approach* was not used in the proposed revision and whether the removal of this term precluded Federal auditors from participating in audits required by this Circular.

*Response*: The proposed revision does not prohibit the participation of Federal auditors in audits required by the Circular, a concept referred to as the *coordinated audit approach*. This term was not included in the proposed revision because the definition of auditor clearly includes Federal audit organizations and further reference to the term *coordinated audit approach was not considered necessary. A provision (§ _____.305(c))* has been added to clarify that Federal auditors may perform all or part of the work required under the Circular if they fully comply with the requirements of the Circular.

*GOCOs and FFRDCs*

*Comment*: A few Federal agency and non-profit organization commenters expressed concern that the proposed revision did not specifically address Federal Government owned, contractor operated facilities (GOCOs) or Federally Funded Research and Development Centers (FFRDCs).

*Response*: A provision has been added to the definition of the term *Federal award* that contracts to operate GOCOs are excluded from the requirements of this Circular. Also, paragraph § _____.200(e) has been added to allow management of an auditee that owns or operates a FFRDC to elect to treat the FFRDC as a separate entity for purposes of this Circular. If the FFRDC is treated as a separate entity, the determination of cognizant agency for audit would be based upon this separate entity.

*Questions and Answers on OMB Circular A–133*

*Comment*: In May 1992, the Standards Subcommittee of the President's Council on Integrity and Efficiency (PCIE) issued PCIE Position Statement No. 6, titled ''Questions and Answers on OMB Circular A–133'' (A–133 Q&A). A commenter inquired whether this document could be used as guidance in performing audits under the revised Circular A–133.

*Response*: Since this revision makes significant changes in OMB Circular A–133, the May 1992 A–133 Q&A should not be used as a primary source of guidance for audits performed under this revision. However, many items in the A–133 Q&A were incorporated in this revision and the A–133 Q&A may be a useful historical reference of the single audit process. If there are significant questions concerning the revised Circular A–133, OMB will consider issuing a revised A–133 Q&A.

*Compliance Supplements*

*Comment*: Some CPA and State auditor commenters expressed concern that Federal agencies should keep the compliance supplements current.

*Response*: OMB recognizes the need for updated compliance supplements and is working with Federal agencies and the PCIE to complete this task. OMB's current plans are to issue a revised compliance supplement by the end of 1996.

*Public Information Collection*

The revision includes an information collection requirement for reports from auditors concerning their audit findings to auditees (§ _____.235(b)(4), § _____.505, and § _____.510) and reports from auditees to the Federal Government concerning these report (§ _____.235(c) and § _____.320). OMB requested comments on the proposed information collection described in the Circular in a April 1, 1996 Federal Register notice (61 FR 14338) in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35 et seq). The proposed information collection requirement will not be effective until another notice is published in the Federal Register. The subsequent notice will provide the effective date and the OMB control number.

Alice M. Rivlin,

*Director.*

April 22, 1996.

Circular No. A–133, Revised

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Audits of Institutions of Higher Education and Other Non-Profit Institutions

1. *Purpose.* This Circular sets forth standards for obtaining consistency and uniformity among Federal agencies for the audit of non-profit organizations expending Federal awards.

2. *Authority.* Circular A–133 is issued under the authority of sections 503 and 1111 of title 31, United States Code, and Executive Orders 8248 and 11541.

3. *Supersession.* This Circular supersedes the prior Circular A–133, issued March 8, 1990. For effective dates, see paragraph 10.

4. *Policy.* Except as provided herein, the standards set forth in this Circular shall be applied by all Federal agencies. If any statute specifically prescribes policies or specific requirements that differ from the standards provided herein, the provisions of the statute shall govern.

Federal agencies shall apply the provisions of the sections of this Circular to non-profit organizations, whether they are recipients expending Federal awards received directly from Federal awarding agencies, or are subrecipients expending Federal awards received from a pass-through entity (a recipient or another subrecipient). Therefore, whereas this Circular does not apply to grants, contracts, or other agreements between the Federal Government and State or local governments (which are covered by Circular A–128, ''Audits of State and Local Governments''), this Circular does apply to awards that State and local governments make to non-profit organizations covered by this Circular. This Circular does not apply to public institutions of higher education and hospitals which are audited under Office of Management and Budget (OMB) Circular A–128.

This Circular does not apply to non-U.S. based entities expending Federal awards received either directly as a recipient or indirectly as a subrecipient.

5. *Definitions.* The definitions of key terms used in this Circular are contained in § _____.105 in the Attachment to this Circular.

6. *Required Action.* The specific requirements and responsibilities of Federal agencies and non-profit organizations are set forth in the Attachment to this Circular. Federal agencies making awards to non-profit organizations, either directly or indirectly, shall adopt the language in the Circular in codified regulations not later than November 30, 1996, unless different provisions are required by Federal statute or are approved by OMB.

7. *OMB Responsibilities.* OMB will review Federal agency regulations and implementation of this Circular, and will provide interpretations of policy requirements and assistance to ensure effective and efficient implementation.

8. *Information Contact.* Further information concerning Circular A–133 may be obtained by contacting the Financial Standards and Reporting Branch, Office of Federal Financial Management, Office of Management and Budget, Washington, DC 20503, telephone (202) 395–3993.

9. *Termination Review Date.* This Circular will have a policy review three years from the date of issuance.

10. *Effective Dates.* The standards set forth in § _____.400 of the Attachment to this Circular, which apply directly to Federal agencies, shall be effective July 1, 1996, and shall apply to audits of fiscal years ending on or after June 30, 1997.

The standards set forth in this Circular that Federal agencies are to apply to non-profit organizations shall be adopted by Federal agencies in codified regulations not later than November 30, 1996, so that they will apply to audits of fiscal years ending on or after June 30, 1997, with the exception that § _____.305(b) of the Attachment applies to audits of fiscal years ending on or after June 30, 1999. In the interim period, until the standards in this Circular are adopted and become applicable, the audit provisions of Circular A–133, issued March 8, 1990, shall continue in effect.

Alice M. Rivlin,

*Director.*

Attachment

## PART____—AUDITS OF INSTITUTIONS OF HIGHER EDUCATION AND OTHER NON-PROFIT INSTITUTIONS

### Subpart A—General

Sec.

____.100 Purpose.
____.105 Definitions.

### Subpart B—Audits

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____.205 Basis for determining Federal awards expended.
____.210 Subrecipient and vendor determinations.
____.215 Relation to other audit requirements.
____.220 Frequency of audits.
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### Subpart C—Auditees

____.300 Auditee responsibilities.
____.305 Auditor selection.
____.310 Financial statements.
____.315 Audit findings follow-up.
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### Subpart D—Federal Agencies and Pass-Through Entities

____.400 Responsibilities.
____.405 Management decision.

### Subpart E—Auditors

____.500 Scope of audit.
____.505 Audit reporting.
____.510 Audit findings.
____.515 Audit working papers.
____.520 Major program determination.
____.525 Criteria for Federal program risk.
____.530 Criteria for a low-risk auditee.

Authority: [Each Federal agency should insert its own rule making authority using appropriate United States Code citations.]

## Subpart A—General

### § _____.100 Purpose.

This part sets forth standards for obtaining consistency and uniformity among Federal agencies for the audit of non-profit organizations expending Federal awards.

### § _____.105 Definitions.

*Auditee* means any organization that expends Federal awards which must be audited under this part.

*Auditor* means an auditor, that is a public accountant or a Federal, State or local government audit organization, which meets the general standards specified in generally accepted government auditing standards (GAGAS). The term *auditor* does not include internal auditors of non-profit organizations.

*Audit finding* means deficiencies which the auditor is required by § _____.510(a) to report in the schedule of findings and questioned costs.

*CFDA number* means the number assigned to a Federal program in the *Catalog of Federal Domestic Assistance* (CFDA).

*Cluster of programs* means Federal programs with different CFDA numbers that are defined as a cluster of programs in the compliance supplements because they are closely related programs and share common compliance requirements. A cluster of programs shall be considered as one program for determining major programs, as described in § _____.520, and whether a program-specific audit may be elected under § _____.200(c).

*Cognizant agency for audit* means the Federal agency designated to carry out the responsibilities described in § _____.400(a).

*Compliance supplements* refers to the *Compliance Supplement for Audits of Institutions of Higher Learning and Other Non-Profit Institutions* and the *Compliance Supplement for Single*

*Audits of State and Local Governments* or such documents as the Office of Management and Budget (OMB) or its designee may issue to replace them. These documents are available from the Government Printing Office, Superintendent of Documents, P.O. Box 371954, Pittsburgh, PA 15250–7954, telephone (202) 512–1800.

*Corrective action* means action taken by the auditee that:

(1) Corrects identified deficiencies;

(2) Produces recommended improvements; or

(3) Demonstrates that audit findings are either invalid or do not warrant auditee action.

*Federal agency* has the same meaning as the term *agency* in Section 551(1) of title 5, United States Code.

*Federal award* means Federal financial assistance and Federal cost-reimbursement contracts. It includes Federal awards made directly by Federal awarding agencies or indirectly by recipients of Federal awards or subrecipients. It does not include procurement contracts, under grants or contracts, used to buy goods or services from vendors. Any audits of such vendors shall be covered by the terms and conditions of the contract. Contracts to operate Federal Government owned, contractor operated facilities (GOCOs) are excluded from the requirements of this part.

*Federal awarding agency* means the Federal agency that provides an award directly to the recipient.

*Federal financial assistance* means assistance received or administered to carry out a program. Such assistance may be in the form of grants, cooperative agreements, donated surplus property, food commodities, loans, loan guarantees, property, interest subsidies, insurance, direct appropriations, and other assistance.

*Federal program* means:

(1) All Federal awards under the same CFDA number. When no CFDA number is assigned, all Federal awards from the same agency made for the same purpose should be combined and considered one program. State governments may combine funding from different Federal awards in providing assistance to their subrecipients when the awards are closely related programs and share common compliance requirements. In this case, the State government may require the subrecipient to treat the combined Federal awards as a single program.

(2) A category of Federal awards which is a group of awards in the categories of:

(i) Research and development;

(ii) Student financial aid; or

(iii) Cluster of programs.

*GAGAS* means generally accepted government auditing standards issued by the Comptroller General of the United States, which are applicable to financial audits.

*Generally accepted accounting principles* has the meaning specified in generally accepted auditing standards issued by the American Institute of Certified Public Accountants (AICPA).

*Internal control* has the meaning specified in generally accepted auditing standards issued by the AICPA.

*Internal control over Federal programs* means a process—effected by an entity's management and other personnel—designed to provide reasonable assurance regarding the achievement of the following objectives for Federal programs:

(1) Transactions are properly recorded and accounted for to:

(i) Permit the preparation of reliable financial statements and Federal reports;

(ii) Maintain accountability over assets; and

(iii) Demonstrate compliance with laws, regulations, and other compliance requirements;

(2) Transactions are executed in compliance with:

(i) Laws, regulations, and the provisions of contracts or grant agreements that could have a direct and material effect on a Federal program; and

(ii) Any other laws and regulations that are identified in the compliance supplements; and

(3) Funds, property, and other assets are safeguarded against loss from unauthorized use or disposition.

*Loan* means a Federal loan or loan guarantee received or administered by a non-profit organization.

*Major program* means a Federal program determined by the auditor to be a major program in accordance with § _____.520 or a program identified as a major program by a Federal agency or pass-through entity in accordance with § _____.215(c).

*Management decision* means the evaluation by the Federal awarding agency or pass-through entity of the audit findings and corrective action plan and the issuance of a written decision as to what corrective action is necessary.

*Non-profit organization* means: (1) any corporation, trust, association, cooperative, or other organization which:

(i) Is operated primarily for scientific, educational, service, charitable, or similar purposes in the public interest;

(ii) Is not organized primarily for profit; and

(iii) Uses its net proceeds to maintain, improve, or expand its operations; and

(2) The term *non-profit organization* includes both non-profit institutions of higher education and hospitals, and public institutions of higher education and hospitals that are not audited in accordance with Circular A–128, ''Audits of State and Local Governments'' (Available from Office of Administration, Publications Office, room 2200, New Executive Office Building, Washington, DC 20503; telephone (202) 395–7332).

*OMB* means the Executive Office of the President, Office of Management and Budget.

*Oversight agency for audit* means the Federal awarding agency that provides the predominant amount of direct funding to a recipient not assigned a cognizant agency for audit. When there is no direct funding, the Federal agency with the predominant indirect funding shall assume the oversight responsibilities. The duties of the oversight agency for audit are described in § _____.400(b).

*Pass-through entity* means a non-profit organization or other entity that provides a Federal award to a subrecipient.

*Program-specific audit* means an audit of one Federal program as provided for in § _____.200(c) and § _____.235.

*Questioned cost* means a cost that is questioned by the auditor because of an audit finding:

(1) Which resulted from a possible violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the use of Federal funds, including funds used to match Federal funds;

(2) Where the costs, at the time of the audit, are not supported by adequate documentation; or

(3) Where the costs incurred appear unreasonable and do not reflect the actions a prudent person would take in the circumstances.

*Recipient* means a non-profit organization that expends Federal awards received directly from a Federal awarding agency to carry out a Federal program.

*Research and development* (R&D) means all research activities, both basic and applied, and all development activities that are performed by a non-profit organization. *Research* is defined as a systematic study directed toward fuller scientific knowledge or understanding of the subject studied. The term research also includes activities involving the training of individuals in research techniques

where such activities utilize the same facilities as other research and development activities and where such activities are not included in the instruction function. *Development* is the systematic use of knowledge and understanding gained from research directed toward the production of useful materials, devices, systems, or methods, including design and development of prototypes and processes.

*Single audit* means an audit which includes both the entity's financial statements and the Federal awards as described in § _____.500.

*Student Financial Aid* (SFA) includes those programs of general student assistance, such as those authorized by Title IV of the Higher Education Act of 1965, as amended, (20 U.S.C. 1070 *et seq.*) which is administered by the U.S. Department of Education, and similar programs provided by other Federal agencies. It does not include programs which provide fellowships or similar Federal awards to students on a competitive basis, or for specified studies or research.

*Subrecipient* means the entity that expends Federal awards received from a pass-through entity to carry out a Federal program, but does not include an individual that is a beneficiary of such a program. A subrecipient may also be a recipient of other Federal awards directly from a Federal awarding agency. Guidance on distinguishing between a subrecipient and a vendor is provided in § _____.210.

*Types of compliance requirements* refers to the types of compliance requirements listed in the compliance supplements. Examples include cash management, Federal financial reporting, allowable costs/cost principles, types of services allowed or unallowed, eligibility, and matching.

*Vendor* means a dealer, distributor, merchant, or other seller providing goods or services that are required for the conduct of a Federal program. These goods or services may be for an organization's own use or for the use of beneficiaries of the Federal program. Additional guidance on distinguishing between a subrecipient and a vendor is provided in § _____.210.

## Subpart B—Audits

### § _____.200 Audit requirements.

(a) *Audit required.* Non-profit organizations that expend $300,000 or more in a year in Federal awards shall have a single or program-specific audit conducted for that year in accordance with the provisions of this part. Guidance on determining Federal awards expended is provided in § _____.205.

(b) *Single audit.* Non-profit organizations that expend $300,000 or more in a year in Federal awards shall have a single audit conducted in accordance with § _____.500 except when they elect to have a program-specific audit conducted in accordance with paragraph (c) of this section.

(c) *Program-specific audit election.* When an auditee expends Federal awards under only one Federal program (excluding R&D) and the Federal program's laws, regulations, or grant agreements do not require a financial statement audit of the auditee, the auditee may elect to have a program-specific audit conducted in accordance with § _____.235. A program-specific audit may not be elected for R&D unless all expenditures are for Federal awards received from the same Federal agency, or the same Federal agency and the same pass-through entity, and that Federal agency, or pass-through entity in the case of a subrecipient, approves in advance a program-specific audit.

(d) *Exemption when expenditures are less than $300,000.* Non-profit organizations that expend less than $300,000 a year in Federal awards are exempt from Federal audit requirements for that year, except as noted in § _____.215(a), but records must be available for review or audit by appropriate officials of the Federal agency, pass-through entity, and General Accounting Office (GAO).

(e) *Federally Funded Research and Development Centers (FFRDC).* Management of an auditee that owns or operates a FFRDC may elect to treat the FFRDC as a separate entity for purposes of this part.

### § _____.205 Basis for determining Federal awards expended.

(a) *Determining Federal awards expended.* The determination of when an award is expended should be based on when the activity related to the award occurs. Generally, the activity pertains to events that require the non-profit organization to comply with laws, regulations, and the provisions of contracts or grant agreements, such as: expenditure/expense transactions associated with grants, cost-reimbursement contracts, cooperative agreements, and direct appropriations; the disbursement of funds passed through to subrecipients; the use of loan proceeds under loan and loan guarantee programs; the receipt of property; the receipt of surplus property; the receipt or use of program income; the distribution or consumption of food commodities; the disbursement of amounts entitling the non-profit organization to an interest subsidy; and, the period when insurance is in force.

(b) *Loan and loan guarantees (loans).* Since the Federal Government is at risk for loans until the debt is repaid, the following guidelines shall be used to calculate the value of Federal awards expended under loan programs, except as noted in paragraphs (c) and (d) of this section:

(1) Value of new loans made or received during the fiscal year; plus

(2) Balance of loans from previous years for which the Federal Government imposes continuing compliance requirements; plus

(3) Any interest subsidy, cash, or administrative cost allowance received.

(c) *Loan and loan guarantees (loans) at institutions of higher education.* When loans are made to students of an institution of higher education but the institution does not make the loans, then only the value of loans made during the year shall be considered Federal awards expended in that year. The balance of loans for previous years is not included as Federal awards expended because the lender accounts for the prior balances.

(d) *Prior loan and loan guarantees (loans).* Loans, the proceeds of which were received and expended in prior-years, are not considered Federal awards expended under this part when the laws, regulations, and the provisions of contracts or grant agreements pertaining to such loans impose no continuing compliance requirements other than to repay the loans.

(e) *Endowment funds.* The cumulative balance of Federal awards for endowment funds which are federally restricted are considered awards expended in each year in which the funds are still restricted.

(f) *Free rent.* Free rent received by itself is not considered an award expended under this part. However, free rent received as part of an award to carry out a Federal program shall be included in determining Federal awards expended and subject to audit under this part.

(g) *Valuing non-cash assistance.* Federal non-cash assistance, such as free rent, food stamps, food commodities, donated property, or donated surplus property, shall be valued at fair market value at the time of receipt or the assessed value provided by the Federal agency.

(h) *Medicare.* Medicare payments to a non-profit organization for providing patient care services to Medicare eligible individuals are not considered Federal awards expended under this part.

(i) *Medicaid.* Medicaid payments to a non-profit organization for providing patient care services to Medicaid eligible individuals are not considered Federal awards expended under this part unless a State requires the funds to be treated as Federal awards expended because reimbursement is on a cost-reimbursement basis.

**§ _____.210 Subrecipient and vendor determinations.**

(a) *General.* An auditee may be a recipient, a subrecipient, and a vendor. Federal awards expended as a recipient or a subrecipient would be subject to audit under this part. The payments received for goods or services provided as a vendor would not be considered Federal awards. The guidance in paragraphs (b) and (c) of this section should be considered in determining whether payments constitute a Federal award or a payment for goods and services.

(b) *Federal award.* Characteristics indicative of a Federal award received by a subrecipient are when the organization:

(1) Determines who is eligible to receive what Federal financial assistance;

(2) Has its performance measured against whether the objectives of the Federal program are met;

(3) Has responsibility for programmatic decision making;

(4) Has responsibility for adherence to applicable Federal program compliance requirements; and

(5) Uses the Federal funds to carry out a program of the organization as compared to providing goods or services for a program of the pass-through entity.

(c) *Payment for goods and services.* Characteristics indicative of a payment for goods and services received by a vendor are when the organization:

(1) Provides the goods and services within normal business operations;

(2) Provides similar goods or services to many different purchasers;

(3) Operates in a competitive environment;

(4) Provides goods or services that are ancillary to the operation of the Federal program; and

(5) Is not subject to compliance requirements of the Federal program.

(d) *Use of judgment in making determination.* There may be unusual circumstances or exceptions to the listed characteristics. In making the determination of whether a subrecipient or vendor relationship exists, the substance of the relationship is more important than the form of the agreement. It is not expected that all of the characteristics will be present and judgment should be used in determining whether an entity is a subrecipient or vendor.

(e) *For-profit subrecipient.* Since this part does not apply to for-profit subrecipients, the pass-through entity is responsible for establishing requirements, as necessary, to ensure compliance by for-profit subrecipients. The contract with the for-profit subrecipient should describe applicable compliance requirements and the for-profit subrecipient's compliance responsibility. Methods to ensure compliance for Federal awards made to for-profit subrecipients may include pre-award audits, monitoring during the contract, and post-award audits.

(f) *Compliance responsibility for vendors.* In most cases, the auditee's compliance responsibility for vendors is only to ensure that the procurement, receipt, and payment for goods and services comply with laws, regulations, and the provisions of contracts or grant agreements. Program compliance requirements normally do not pass through to vendors. However, the auditee is responsible for ensuring compliance for vendor transactions which are structured such that the vendor is responsible for program compliance or the vendor's records must be reviewed to determine program compliance. Also, when these vendor transactions relate to a major program, the scope of the audit shall include determining whether these transactions are in compliance with laws, regulations, and the provisions of contracts or grant agreements.

**§ _____.215 Relation to other audit requirements.**

(a) *Audit under this part in lieu of other audits.* An audit made in accordance with this part shall be in lieu of any financial audit required under individual Federal awards. To the extent this audit meets a Federal agency's needs, it shall rely upon and use such audits. The provisions of this part neither limit the authority of Federal agencies, including their Inspectors General, or GAO to conduct or arrange for additional audits (e.g., financial audits, performance audits, evaluations, inspections, or reviews) nor authorize any auditee to constrain Federal agencies from carrying out additional audits. Any additional audits shall be planned and performed in such a way as to build upon work performed by other auditors.

(b) *Federal agency to pay for additional audits.* A Federal agency that conducts or contracts for additional audits shall, consistent with other applicable laws and regulations, arrange for funding the cost of such additional audits.

(c) *Request for a program to be audited as a major program.* A Federal agency may request an auditee to have a particular Federal program audited as a major program in lieu of the Federal agency conducting or arranging for the additional audits. To allow for planning, such requests should be made at least 180 days prior to the end of the fiscal year to be audited. The auditee, after consultation with its auditor, should promptly respond to such request by informing the Federal agency whether the program would otherwise be audited as a major program using the risk-based audit approach described in § _____.520 and, if not, the estimated incremental cost. The Federal agency shall then promptly confirm to the auditee whether it wants the program audited as a major program. If the program is to be audited as a major program based upon this Federal agency request, and the Federal agency agrees to pay the full incremental costs, then the auditee shall have the program audited as a major program. A pass-through entity may use the provisions of this paragraph for a subrecipient.

**§ _____.220 Frequency of audits.**

Audits required by this part shall be performed annually. However, a Federal agency or pass-through entity may allow an auditee that elects a program-specific audit under § _____.200(c) to perform the audit every two years. Two-year audits must cover both years.

**§ _____.225 Sanctions.**

No audit costs may be charged to Federal awards when audits required by this part have not been made or have been made but not in accordance with this part. In cases of continued inability or unwillingness to have an audit conducted in accordance with this part, Federal agencies and pass-through entities shall take appropriate action using sanctions such as:

(a) Withholding a percentage of Federal awards until the audit is completed satisfactorily;

(b) Withholding or disallowing overhead costs;

(c) Suspending Federal awards until the audit is conducted; or

(d) Terminating the Federal award.

**§ _____.230 Audit costs.**

Unless prohibited by law, the cost of audits made in accordance with the provisions of this part are allowable charges to Federal awards. The charges may be considered a direct cost or an allocated indirect cost, as determined in accordance with the provisions of

applicable OMB cost principles circulars, Federal Acquisition Regulation (48 CFR part 31), or other applicable cost principles or regulations.

**§ _____.235 Program-specific audits.**

(a) *Program-specific audit guide available.* In many cases, a program-specific audit guide will be available to provide specific guidance to the auditor with respect to internal control, compliance requirements, suggested audit procedures, and audit reporting requirements. The auditor should contact the Office of Inspector General of the Federal agency to determine whether such a guide is available. When a current program-specific audit guide is available, the auditor shall follow GAGAS and the guide when performing a program-specific audit.

(b) *Program-specific audit guide not available.* (1) When a program-specific audit guide is not available, the auditee and auditor shall have basically the same responsibilities for the Federal program as they would have for an audit of a major program in a single audit.

(2) The auditee shall prepare the financial statement(s) for the Federal program that includes, at a minimum, a schedule of the Federal program's expenditures and notes that describe the significant accounting policies used in preparing the schedule, a summary schedule of prior audit findings consistent with the requirements of § _____.315(b), and a corrective action plan consistent with the requirements of § _____.315(c).

(3) The auditor shall:

(i) Perform an audit of the financial statement(s) for the Federal program in accordance with GAGAS;

(ii) Obtain an understanding of internal control and perform tests of internal control over the Federal program consistent with the requirements of § _____.500(c) for a major program;

(iii) Perform procedures to determine whether the auditee has complied with laws, regulations, and the provisions of contracts or grant agreements that could have a direct and material effect on the Federal program consistent with the requirements of § _____.500(d) for a major program; and

(iv) Follow up on prior audit findings, perform procedures to assess the reasonableness of the summary schedule of prior audit findings prepared by the auditee, and report, as a current year audit finding, when the auditor concludes that the summary schedule of prior audit findings materially misrepresents the status of any prior audit finding in accordance with the requirements of § _____.500(e).

(4) The auditor's report(s) may be in the form of either combined or separate reports and may be organized differently from the manner presented in this section. The auditor's report(s) shall state that the audit was conducted in accordance with this part and include the following:

(i) An opinion (or disclaimer of opinion) as to whether the financial statement(s) of the Federal program is presented fairly in all material respects in accordance with the stated accounting policies;

(ii) A report on internal control related to the Federal program, which shall describe the scope of testing of internal control and the results of the tests;

(iii) A report on compliance which includes an opinion (or disclaimer of opinion) as to whether the auditee complied with laws, regulations, and the provisions of contracts or grant agreements which could have a direct and material effect on the Federal program; and

(iv) A schedule of findings and questioned costs for the Federal program that is consistent with the requirements of § _____.505(a)(4) and includes a summary of the auditor's results applicable to the audit of the Federal program and in a format consistent with § _____.505(b).

(c) *Report submission for program-specific audits.* (1) The audit shall be completed and the reporting required by paragraph (c)(2) or (c)(3) of this section submitted within nine months after the end of the audit period, unless a longer period is agreed to in advance by the Federal agency that provided the funding or a different period is specified in a program-specific audit guide. Also, this required reporting shall be submitted within 30 days after the issuance of the auditor's report(s) to the auditee. Unless restricted by law or regulation, the auditee shall make report copies available for public inspection.

(2) When a program-specific audit guide is available, the auditee shall submit to the central clearinghouse designated by OMB one copy of the certification prepared in accordance with § _____.320(b), as applicable to a program-specific audit, and the reporting required by the program-specific audit guide to be retained as an archival copy. Also, the auditee shall submit to the Federal awarding agency or pass-through entity the reporting required by the program-specific audit guide.

(3) When a program-specific audit guide is not available, the reporting package for a program-specific audit shall consist of the certification prepared in accordance with § _____.320(b), as applicable to a program-specific audit, the financial statement(s) of the Federal program, a summary schedule of prior audit findings, and a corrective action plan as described in paragraph (b)(2) of this section, and the auditor's report(s) described in paragraph (b)(4) of this section. One copy of this reporting package shall be submitted to the central clearinghouse designated by OMB to be retained as an archival copy. Also, when the schedule of findings and questioned costs disclosed audit findings or the summary schedule of prior audit findings reported the status of any audit findings, the auditee shall submit one copy of the reporting package to the central clearinghouse on behalf of the Federal awarding agency, or directly to the pass-through entity in the case of a subrecipient.

(d) *Other sections of this part may apply.* Program-specific audits are subject to § _____.100 through § _____.215(b), § _____.220 through § _____.230, § _____.300 through § _____.305, § _____.315, § _____.320(f) through § _____.320(j), § _____.400 through § _____.405, § _____.510 through § _____.515, and other referenced provisions of this part unless contrary to the provisions of this section, a program-specific audit guide, or program laws and regulations.

## Subpart C—Auditees

**§ _____.300 Auditee responsibilities.**

The auditee shall:

(a) Identify, in its accounts, all Federal awards received and expended and the Federal programs under which they were received. Federal program and award identification shall include, as applicable, the CFDA title and number, award number and year, name of the Federal agency, and name of the pass-through entity.

(b) Maintain internal control over Federal programs that provides reasonable assurance that the auditee is managing Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its Federal programs.

(c) Comply with laws, regulations, and the provisions of contracts or grant agreements related to each of its Federal programs.

(d) Prepare appropriate financial statements, including the schedule of expenditures of Federal awards in accordance with § _____.310.

(e) Ensure that the audits required by this part are properly performed and submitted when due. When extensions to the report submission due date required by § _____.320(a) are granted by the cognizant or oversight agency for audit, promptly notify the central clearinghouse designated by OMB and each pass-through entity providing Federal awards of the extension.

(f) Follow up and take corrective action on audit findings, including preparation of a summary schedule of prior audit findings and a corrective action plan in accordance with § _____.315(b) and § _____.315(c), respectively.

**§ _____.305 Auditor selection.**

(a) *Auditor procurement.* In arranging for audit services, auditees shall follow the procurement standards prescribed by Circular A–110, ''Uniform Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals and Other Non-Profit Organizations,'' or the Federal Acquisition Regulation (48 CFR part 42), as applicable. (Circular available from Office of Administration, Publications Office, room 2200, New Executive Office Building, Washington, DC 20503; telephone (202) 395–7332.) Whenever possible, auditees shall make positive efforts to utilize small businesses, minority-owned firms, and women's business enterprises, in procuring audit services as stated in OMB Circular A–110 or the Federal Acquisition Regulation (48 CFR part 42), as applicable. In requesting proposals for audit services, the objectives and scope of the audit should be made clear. Factors to be considered in evaluating each proposal for audit services include the responsiveness to the request for proposal, relevant experience, availability of staff with professional qualifications and technical abilities, the results of external quality control reviews, and price.

(b) *Restriction on auditor preparing indirect cost proposals.* An auditor who prepares the indirect cost proposal or cost allocation plan may not also be selected to perform the audit required by this part when the indirect costs recovered by the auditee during the prior year exceeded $1 million. This restriction applies to the base year used in the preparation of the indirect cost proposal or cost allocation plan and any subsequent years in which the resulting indirect cost agreement or cost allocation plan is used to recover costs. To minimize any disruption in existing contracts for audit services, this paragraph applies to audits of fiscal years ending on or after June 30, 1999.

(c) *Use of Federal auditors.* Federal auditors may perform all or part of the work required under this part if they comply fully with the requirements of this part.

**§ _____.310 Financial statements.**

(a) *Financial statements.* The auditee shall prepare financial statements that reflect its financial position, results of operations, and, where appropriate, cash flows for the fiscal year audited. The financial statements shall be for the same organizational unit and fiscal year that is chosen to meet the requirements of this part.

(b) *Schedule of expenditures of Federal awards.* The auditee shall also prepare a schedule of expenditures of Federal awards for the period covered by the auditee's financial statements. While not required, it is appropriate for the auditee to provide information requested to make the schedule easier to use by Federal awarding agencies and pass-through entities. For example, when a Federal program has multiple award years, the auditee may list the amount of each award year separately. At a minimum, the schedule shall:

(1) List individual Federal programs by Federal agency and major subdivision within a Federal agency. For Federal awards received as a subrecipient, the name of the pass-through entity and identifying number assigned by the pass-through entity shall be included.

(2) Provide total expenditures for each individual Federal program and the CFDA number or other identifying number when the CFDA information is not available.

(3) Identify major programs.

(4) Include notes that describe the significant accounting policies used in preparing the schedule and identify in the notes the dollar threshold used to distinguish between Type A and Type B programs, as described in § _____.520(b).

(5) To the extent practical, pass-through entities should identify in the schedule the total amount provided to subrecipients from each Type A program and from each Type B program which is audited as a major program.

(6) List individual Federal awards within a category of Federal awards. However, when it is not practical to list each individual Federal award for R&D, total expenditures shall be shown by Federal agency and major subdivision within the Federal agency. For example, the National Institutes of Health is a major subdivision in the Department of Health and Human Services.

(7) Include, in either the schedule or a note to the schedule, the value of non-cash assistance expended, insurance in effect during the year, and loans or loan guarantees outstanding at year end.

**§ _____.315 Audit findings follow-up.**

(a) *General.* The auditee is responsible for follow-up and corrective action on all audit findings. As part of this responsibility, the auditee shall prepare a summary schedule of prior audit findings. The auditee shall also prepare a corrective action plan for current year audit findings. The summary schedule of prior audit findings and the corrective action plan shall include the reference numbers the auditor assigns to audit findings under § _____.510(c). Since the summary schedule may include audit findings from multiple years, it shall include the fiscal year in which the finding initially occurred.

(b) *Summary schedule of prior audit findings.* The summary schedule of prior audit findings shall report the status of all audit findings included in the prior audit's schedule of findings and questioned costs. The summary schedule shall also include audit findings reported in the prior audit's summary schedule of prior audit findings except audit findings listed as corrected in accordance with paragraph (b)(1), or no longer valid or not warranting further action in accordance with paragraph (b)(4) of this section.

(1) When audit findings were fully corrected, the summary schedule need only list the audit findings and state that corrective action was taken.

(2) When audit findings were not corrected or were only partially corrected, the summary schedule shall describe the planned corrective action as well as any partial corrective action taken.

(3) When corrective action taken is significantly different from corrective action previously reported in a corrective action plan or in the Federal agency's or pass-through entity's management decision, the summary schedule shall provide an explanation.

(4) When the auditee believes the audit findings are no longer valid or do not warrant further action, the reasons for this position shall be described in the summary schedule. A valid reason for considering an audit finding as not warranting further action is that all of the following have occurred:

(i) Two years have passed since the audit report in which the finding occurred was submitted to the central clearinghouse;

(ii) The Federal agency or pass-through entity is not currently following up with the auditee on the audit finding; and

(iii) A management decision was not issued.

(c) *Corrective action plan.* At the completion of the audit, the auditee shall prepare a corrective action plan to address each audit finding included in the current year auditor's reports. The corrective action plan shall provide the name(s) of the contact person(s) responsible for corrective action, the corrective action planned, and the anticipated completion date. If the auditee does not agree with the audit findings or believes corrective action is not required, then the corrective action plan shall include an explanation and specific reasons.

**§ _____.320 Report submission.**

(a) *General.* The audit shall be completed and the reporting package described in paragraph (c) of this section submitted within nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audit. Also, the reporting package shall be submitted within 30 days after issuance of the auditor's report(s) to the auditee. Unless restricted by law or regulation, the auditee shall make copies available for public inspection.

(b) *Certification.* The auditee shall complete a certification form which states whether the audit was completed in accordance with this part and provides information about the auditee, its Federal programs, and the results of the audit. The form shall be approved by OMB, available from the central clearinghouse designated by OMB, include data elements similar to those presented in this paragraph, and use a machine-readable format. The auditee's chief executive officer or chief financial officer shall sign a statement that the information on the form is accurate and complete as follows:

Certificate of Audit

This is to certify that, to the best of my knowledge and belief, the [specify name of the auditee] has: (1) engaged an auditor to perform an audit in accordance with the provisions of OMB Circular A–133 for the [specify number] months ended [specify date]; (2) the auditor has completed such audit and presented a signed audit report which states that the audit was conducted in accordance with the provisions of the Circular; and, (3) the information on the attached form accurately and completely reflects the results of this audit, as presented in the auditor's report. I declare that the foregoing is true and correct.

Attachment to Certificate

Information Accompanying Certificate of Audit

1. The type of report the auditor issued on the financial statements of the auditee (i.e., unqualified opinion, qualified opinion, adverse opinion, or disclaimer of opinion).

2. A yes or no statement as to whether the auditor's report on the financial statements indicated that the auditor has substantial doubt about the auditee's ability to continue as a going concern.

3. The type of report the auditor issued on compliance for major programs (i.e., unqualified opinion, qualified opinion, adverse opinion, or disclaimer of opinion).

4. A list of the Federal awarding agencies and pass-through entities which will receive a copy of the reporting package pursuant to § _____.320(d)(2) and § _____.320(e)(2) of OMB Circular A–133. An explanation should be provided if this list is different from the communication the auditor provides to the auditee under § _____.500(f) of OMB Circular A–133.

5. A yes or no statement as to whether the auditee qualified as a low-risk auditee under § _____.530 of OMB Circular A–133.

6. The dollar threshold used to distinguish between Type A and Type B programs as defined in § _____.520(b) of OMB Circular A–133.

7. The *Catalog of Federal Domestic Assistance* (CFDA) number for each Federal program, as applicable.

8. The name of each Federal program and identification of each major program. Individual awards within a category of awards should be listed in the same level of detail as they are listed in the schedule of expenditures of Federal awards.

9. The amount of expenditures in the schedule of expenditures of Federal awards associated with each Federal program.

10. A yes or no statement as to whether there are audit findings and the amount of any questioned costs related to the following for each Federal program:

a. Types of services allowed or unallowed.
b. Eligibility.
c. Matching, maintenance of level of effort, or earmarking.
d. Federal financial reporting.
e. Program income.
f. Procurement.
g. Subrecipient monitoring.
h. Allowable costs/cost principles.
i. Other.

11. Auditee Name:

_____

Employer Identification Number:

_____

Name and Title of Responsible Official:

_____

Telephone Number:

_____

Signature:

_____

Date:

_____

12. Auditor Name:

_____

Name and Title of Contact Person:

_____

Auditor Address:

_____

Auditor Telephone Number:

_____

(c) *Reporting Package.* The reporting package shall include the:

(1) Certification discussed in paragraph (b) of this section;

(2) Financial statements and schedule of expenditures of Federal awards discussed in § _____.310(a) and § _____.310(b), respectively;

(3) Summary schedule of prior audit findings discussed in § _____.315(b);

(4) Auditor's report(s) discussed in § _____.505; and

(5) Corrective action plan discussed in § _____.315(c).

(d) *Submission to clearinghouse.* All auditees shall submit to the central clearinghouse designated by OMB one copy of the reporting package described in paragraph (c) of this section for:

(1) The central clearinghouse to retain as an archival copy; and

(2) Each Federal awarding agency when the schedule of findings and questioned costs disclosed audit findings relating to Federal awards that the Federal awarding agency provided directly or the summary schedule of prior audit findings reported the status of any audit findings relating to Federal awards that the Federal awarding agency provided directly.

(e) *Additional submission by subrecipients.* In addition to the requirements discussed in paragraph (d) of this section, subrecipients shall submit to each pass-through entity one copy of the:

(1) Certification discussed in paragraph (b) of this section; and

(2) Reporting package described in paragraph (c) of this section for each pass-through entity when the schedule of findings and questioned costs disclosed audit findings relating to Federal awards that the pass-through entity provided or the summary schedule of prior audit findings reported the status of any audit findings relating to Federal awards that the passthrough entity provided.

(f) *Requests for report copies.* In response to requests by a Federal agency or pass-through entity, auditees shall submit the appropriate copies of the reporting package described in paragraph (c) of this section and, if requested, a copy of any management letters issued by the auditor.

(g) *Report retention requirements.* Auditees shall keep one copy of the reporting package described in paragraph (c) of this section on file for three years from the date of submission to the central clearinghouse designated by OMB. Pass-through entities shall keep subrecipients' submissions on file for three years from date of receipt.

(h) *Clearinghouse responsibilities.* The central clearinghouse designated by OMB shall distribute the reporting packages received in accordance with

paragraph (d)(2) of this section and § _____.235(c)(3) to applicable Federal awarding agencies, maintain a data base of completed audits, provide appropriate information to Federal agencies, and follow up with known auditees which have not submitted the required certifications and reporting packages.

(i) *Clearinghouse address.* The address of the central clearinghouse currently designated by OMB is Federal Audit Clearinghouse, Bureau of the Census, 1201 E. 10th Street, Jeffersonville, IN 47132.

(j) *Electronic filing.* Nothing in this part shall preclude electronic submissions to the central clearinghouse in such manner as may be approved by OMB. With OMB approval, the central clearinghouse may pilot test methods of electronic submissions.

## Subpart D—Federal Agencies and Pass-Through Entities

### § _____.400 Responsibilities.

(a) *Cognizant agency for audit responsibilities.* Recipients expending more than $25 million a year in Federal awards shall have a cognizant agency for audit. The designated cognizant agency for audit shall be the Federal awarding agency that provides the predominant amount of direct funding to a recipient unless OMB makes a specific cognizant agency for audit assignment and provides notice in the Federal Register. To provide for continuity of cognizance, the determination of the predominant amount of direct funding shall be based upon direct Federal awards expended in the recipient's fiscal years ending in 1995, 2000, 2005, and every fifth year thereafter. For example, audit cognizance for periods ending in 1996 through 2000 will be determined based on Federal awards expended in 1995. A Federal awarding agency with cognizance for an auditee may reassign cognizance to another Federal awarding agency which provides substantial direct funding and agrees to be the cognizant agency for audit. Within 30 days after any reassignment, both the old and the new cognizant agency for audit shall notify the auditee, and, if known, the auditor of the reassignment. The cognizant agency for audit shall:

(1) Provide technical audit advice and liaison to auditees and auditors.

(2) Consider auditee requests for extensions to the report submission due date required by § _____.320(a). The cognizant agency for audit may grant extensions for good cause.

(3) Obtain or conduct quality control reviews of selected audits made by non-Federal auditors, and provide the results, when appropriate, to other interested organizations.

(4) Promptly inform other affected Federal agencies and appropriate Federal law enforcement officials of any direct reporting by the auditee or its auditor of irregularities or illegal acts, as required by GAGAS or laws and regulations, when such reporting is not included in the reporting package described in § _____.320(c).

(5) Advise the auditor and, where appropriate, the auditee of any deficiencies found in the audits when the deficiencies require corrective action by the auditor. When advised of deficiencies, the auditee shall work with the auditor to take corrective action. If corrective action is not taken, the cognizant agency for audit shall notify the auditor, the auditee, and applicable Federal awarding agencies and pass-through entities of the facts and make recommendations for follow-up action. Major inadequacies or repetitive substandard performance by auditors shall be referred to appropriate State licensing agencies and professional bodies for disciplinary action.

(6) Coordinate, to the extent practical, audits or reviews made by or for Federal agencies that are in addition to the audits made pursuant to this part, so that the additional audits or reviews build upon audits performed in accordance with this part.

(7) Coordinate a management decision for audit findings that affect the Federal programs of more than one agency.

(8) Coordinate the audit work and reporting responsibilities among auditors to achieve the most costeffective audit.

(b) *Oversight agency for audit responsibilities.* An auditee which does not have a designated cognizant agency for audit will be under the general oversight of the Federal agency determined in accordance with § _____.105 (*Oversight agency for audit*). The oversight agency for audit:

(1) Shall provide technical advice to auditees and auditors as requested.

(2) May assume all or some of the responsibilities normally performed by a cognizant agency for audit.

(c) *Federal awarding agency responsibilities.* The Federal awarding agency shall perform the following for the Federal awards it makes:

(1) Identify Federal awards made by informing each recipient of the CFDA title and number, award name and number, award year, and if the award is for R&D. When some of this information is not available, the Federal agency shall provide information necessary to clearly describe the Federal award.

(2) Ensure that audits are completed and reports are received in a timely manner and in accordance with the requirements of this part.

(3) Provide technical advice and counsel to auditees and auditors as requested.

(4) Issue a management decision on audit findings within six months after receipt of the audit report and ensure that the recipient takes appropriate and timely corrective action.

(5) Assign a person responsible to inform OMB annually of any updates needed to the compliance supplements.

(d) *Pass-through entity responsibilities.* A non-profit pass-through entity shall perform the following for the Federal awards it makes:

(1) Identify Federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is R&D, and name of Federal agency. When some of this information is not available, the pass-through entity shall provide the best information available to describe the Federal award.

(2) Advise subrecipients of requirements imposed on them by Federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.

(3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

(4) Ensure that non-profit subrecipients expending $300,000 or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year, and that subrecipients subject to Circular A–128 have met the requirements of Circular A–128.

(5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.

(6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.

(7) Require each subrecipient to permit the pass-through entity and auditors to have access to the records and financial statements as necessary for the pass-through entity to comply with this part.

**§ _____.405 Management decision.**

(a) *General.* The management decision shall clearly state whether or not the audit finding is sustained, the reasons for the decision, and the expected auditee action to repay disallowed costs, make financial adjustments, or take other action. If the auditee has not completed corrective action, a timetable for follow-up should be given. Prior to issuing the management decision, the Federal agency or pass-through entity may request additional information or documentation from the auditee, including a request that the documentation be audited, as a way of mitigating disallowed costs. The management decision should describe any appeal process available to the auditee.

(b) *Federal agency.* As provided in § _____.400(a)(7), the cognizant agency for audit shall be responsible for coordinating a management decision for audit findings that affect the programs of more than one Federal agency. As provided in § _____.400(c)(4), a Federal awarding agency is responsible for issuing a management decision for findings that relate to Federal awards it makes to recipients. Alternate arrangements may be made on a case-by-case basis by agreement among the Federal agencies concerned.

(c) *Pass-through entity.* As provided in § _____.400(d)(5), the pass-through entity shall be responsible for making the management decision for audit findings that relate to Federal awards it makes to subrecipients.

(d) *Time requirements.* The entity responsible for making the management decision shall do so within six months of receipt of the audit report. Corrective action should be initiated within six months and proceed as rapidly as possible.

(e) *Reference numbers.* Management decisions shall include the reference numbers the auditor assigned to each audit finding in accordance with § _____.510(c).

## Subpart E—Auditors

**§ _____.500 Scope of audit.**

(a) *General.* The audit shall be conducted in accordance with GAGAS.

(b) *Financial statements.* The auditor shall determine whether the financial statements of the auditee are presented fairly in all material respects in conformity with generally accepted accounting principles. The auditor shall also determine whether the schedule of expenditures of Federal awards is presented fairly in all material respects in relation to the auditee's financial statements taken as a whole.

(c) *Internal control.* (1) In addition to the requirements of GAGAS, the auditor shall perform procedures to obtain an understanding of internal control over Federal programs sufficient to plan the audit to achieve a low assessed level of control risk for major programs.

(2) Except as provided in paragraph (c)(3) of this section, the auditor shall:

(i) Plan the testing of internal control over major programs to achieve a low assessed level of control risk for the assertions relevant to the compliance requirements for each major program; and

(ii) Perform testing of internal control over major programs as planned in paragraph (c)(2)(i) of this section.

(3) When internal control over some or all of the compliance requirements for a major program are likely to be ineffective in preventing or detecting noncompliance, the planning and performing of testing described in paragraph (c)(2) of this section are not required for those compliance requirements. However, the auditor shall report a reportable condition or a material weakness in accordance with § _____.510, assess the related control risk at the maximum, and consider whether additional compliance tests are required because of ineffective internal control over the major program.

(d) *Compliance.* (1) In addition to the requirements of GAGAS, the auditor shall determine whether the auditee has complied with laws, regulations, and the provisions of contracts or grant agreements that may have a direct and material effect on each of its major programs.

(2) The compliance testing shall include tests of transactions and such other auditing procedures necessary to provide the auditor sufficient evidence to support an opinion on compliance for each major program.

(3) The principal compliance requirements of the largest Federal programs are included in the compliance supplements.

(4) For Federal programs contained in the compliance supplements, an audit of the compliance requirements contained in the compliance supplements will meet the requirements of this part. Where there have been changes to the compliance requirements and the changes are not reflected in the compliance supplements, the auditor shall determine the current compliance requirements and modify the audit procedures accordingly. For those Federal programs not covered in the compliance supplements, the auditor should use the types of compliance requirements (e.g., cash management, Federal financial reporting, allowable costs/cost principles, types of services allowed or unallowed, eligibility, and matching) contained in the compliance supplements as guidance for identifying the types of compliance requirements to test, and determine the requirements governing the Federal program by reviewing the provisions of contracts and grant agreements and the laws and regulations referred to in such contracts and grant agreements. The auditor should consult with the applicable Federal agency to determine the availability of agency-prepared supplements or audit guides.

(e) *Audit follow-up.* The auditor shall follow-up on prior audit findings, perform procedures to assess the reasonableness of the summary schedule of prior audit findings prepared by the auditee in accordance with § _____.315(b), and report, as a current year audit finding, when the auditor concludes that the summary schedule of prior audit findings materially misrepresents the status of any prior audit finding. The auditor shall perform audit follow-up procedures regardless of whether a prior audit finding relates to a major program in the current year.

(f) *Communication.* The auditor shall communicate, preferably in writing, to the auditee which Federal awarding agencies and pass-through entities are required to receive a copy of the reporting package pursuant to § _____.320(d)(2) and § _____.320(e)(2), respectively. The auditor shall retain a record of this communication in the auditor's working papers.

**§ _____.505 Audit reporting.**

(a) *Auditor's reports.* The auditor's report(s) may be in the form of either combined or separate reports and may be organized differently from the manner presented in this section. The auditor's report(s) shall state that the audit was conducted in accordance with this part and include the following:

(1) An opinion (or disclaimer of opinion) as to whether the financial statements are presented fairly in all material respects in conformity with generally accepted accounting principles and an opinion (or disclaimer of opinion) as to whether the schedule of expenditures of Federal awards is presented fairly in all material respects in relation to the financial statements taken as a whole.

(2) A report on internal control related to the financial statements and major programs. This report shall describe the scope of testing of internal control and the results of the tests, and, where applicable, refer to the separate

schedule of findings and questioned costs described in paragraph (a)(4) of this section.

(3) A report on compliance with laws, regulations, and the provisions of contracts or grant agreements, noncompliance with which could have a material effect on the financial statements. This report shall also include an opinion (or disclaimer of opinion) as to whether the auditee complied with laws, regulations, and the provisions of contracts or grant agreements which could have a direct and material effect on each major program, and, where applicable, refer to the separate schedule of findings and questioned costs described in paragraph (a)(4) of this section.

(4) A schedule of findings and questioned costs which includes a summary of the auditor's results as described in paragraph (b) of this section and all audit findings as defined in § _____.510(a). Any findings (e.g., internal control findings, compliance findings, questioned costs, or fraud) which relate to the same issue should be presented as a single finding. Where practical, audit findings should be organized by Federal agency or pass-through entity.

(b) *Summary of the auditor's results.* The summary of the auditor's results shall include:

(1) The type of report the auditor issued on the financial statements of the auditee (i.e., unqualified opinion, qualified opinion, adverse opinion, or disclaimer of opinion);

(2) Where applicable, a statement that the auditor's report on the financial statements indicated that the auditor has substantial doubt about the auditee's ability to continue as a going concern;

(3) The type of report the auditor issued on compliance for major programs (i.e., unqualified opinion, qualified opinion, adverse opinion, or disclaimer of opinion);

(4) Where applicable, a statement that reportable conditions in internal control over major programs were disclosed by the audit and whether any such conditions were material weaknesses, as described in § _____.510(a)(1);

(5) A statement as to whether the audit disclosed any material noncompliance in major programs, as described in § _____.510(a)(2);

(6) A statement as to whether the audit disclosed any questioned costs, as described in § _____.510(a)(3);

(7) Where applicable, a statement that the schedule of findings and questioned costs contains instances of known fraud, as described in § _____.510(a)(5); and

(8) Where applicable, a statement that the audit follow-up procedures disclosed that the summary schedule of prior audit findings materially misrepresents the status of any prior audit finding, as described in § _____.510(a)(6).

**§ _____.510 Audit findings.**

(a) *Audit findings reported.* The auditor shall report the following as audit findings in a schedule of findings and questioned costs:

(1) Reportable conditions in internal control over major programs. The auditor's determination of whether to report a deficiency in internal control as a reportable condition is in relation to a type of compliance requirement for a major program or an audit objective identified in the compliance supplements. The auditor shall identify reportable conditions which are individually or cumulatively material weaknesses.

(2) Material noncompliance with the provisions of laws, regulations, contracts, or grant agreements which the auditor concludes, based on evidence obtained, has occurred or is likely to have occurred. The auditor's determination of whether a noncompliance with the provisions of laws, regulations, contracts, or grant agreements is material for the purpose of reporting an audit finding is in relation to a type of compliance requirement for a major program or an audit objective identified in the compliance supplements.

(3) Known questioned costs which are greater than $10,000 for a type of compliance requirement for a major program. Known questioned costs are those specifically identified by the auditor. In evaluating the effect of questioned costs on the opinion on compliance for each major program, the auditor considers the best estimate of total costs questioned (likely questioned costs), not just the questioned costs specifically identified (known questioned costs). The auditor shall also report known questioned costs when likely questioned costs are greater than $10,000 for a type of compliance requirement for a major program. In reporting questioned costs, the auditor shall include information to provide proper perspective for judging the prevalence and consequences of the questioned costs.

(4) The circumstances concerning why the auditor's report on compliance for major programs is other than an unqualified opinion, unless such circumstances are otherwise reported as audit findings in the schedule of findings and questioned costs.

(5) Known fraud affecting a Federal award, unless such fraud is otherwise reported as an audit finding in the schedule of findings and questioned costs. Fraud is a type of illegal act involving the obtaining of something of value through willful misrepresentation. This paragraph does not require the auditor to make an additional reporting when the auditor confirms that the fraud was reported outside of the auditor's reports under the direct reporting requirements of GAGAS.

(6) Instances where the results of audit follow-up procedures disclosed that the summary schedule of prior audit findings prepared by the auditee in accordance with § _____.315(b) materially misrepresents the status of any prior audit finding.

(b) *Audit finding detail.* Audit findings shall be presented in sufficient detail for the auditee to prepare a corrective action plan and take corrective action and for Federal agencies and pass-through entities to arrive at a management decision. The following specific information shall be included, as applicable, in audit findings:

(1) Federal program and specific Federal award identification including the CFDA title and number, Federal award number and year, name of Federal agency, and name of the applicable pass-through entity. When information, such as the CFDA title and number or Federal award number, is not available, the auditor shall provide the best information available to describe the Federal award.

(2) The criteria or specific requirement upon which the audit finding is based, including statutory, regulatory, or other citation.

(3) The condition found, including facts that support the deficiency identified in the audit finding.

(4) Identification of questioned costs and how they were computed.

(5) Information to provide proper perspective for judging the prevalence and consequences of the audit findings, such as whether the audit findings represent an isolated instance or a systemic problem. Where appropriate, instances identified shall be related to the universe and the number of cases examined and be quantified in terms of dollar value.

(6) The possible asserted effect to provide sufficient information to the auditee and Federal agency, or pass-through entity in the case of a subrecipient, to permit them to determine the cause and effect to facilitate prompt and proper corrective action.

(7) Recommendations to prevent future occurrences of the deficiency identified in the audit finding.

(8) Views of responsible officials of the auditee when there is disagreement with the audit findings, to the extent practical.

(c) *Reference numbers.* Each audit finding in the schedule of findings and questioned costs shall include a reference number to allow for easy referencing of the audit findings during follow-up.

**§ _____.515 Audit working papers.**

(a) *Retention of working papers.* The auditor shall retain working papers and reports for a minimum of three years after the date of issuance of the auditor's report(s) to the auditee, unless the auditor is notified in writing by the cognizant agency for audit, oversight agency for audit, or pass-through entity to extend the retention period. When the auditor is aware that the Federal awarding agency, pass-through entity, or auditee is contesting an audit finding, the auditor shall contact the parties contesting the audit finding for guidance prior to destruction of the working papers and reports.

(b) *Access to working papers.* Audit working papers shall be made available upon request to the cognizant or oversight agency for audit or its designee, a Federal agency providing direct or indirect funding, or GAO at the completion of the audit. Access to working papers includes the right of Federal agencies to obtain copies of working papers, as is reasonable and necessary.

**§ _____.520 Major program determination.**

(a) *General.* The auditor shall use a risk-based approach to determine which Federal programs are major programs. This risk-based approach shall include consideration of: Current and prior audit experience, oversight by Federal agencies and passthrough entities, and the inherent risk of the Federal program. The process in paragraphs (b) through (i) of this section shall be followed.

(b) *Step 1.* (1) The auditor shall identify the larger Federal programs, which shall be labeled Type A programs. Type A programs are defined as Federal programs with Federal expenditures during the audit period exceeding the larger of:

(i) $300,000 or three percent (.03) of total Federal expenditures in the case of an auditee for which total Federal expenditures equal or exceed $300,000 but are less than or equal to $100 million.

(ii) $3 million or three-tenths of one percent (.003) of total Federal expenditures in the case of an auditee for which total Federal expenditures exceed $100 million but are less than or equal to $10 billion.

(iii) $30 million or 15 hundredths of one percent (.0015) of total Federal expenditures in the case of an auditee for which total Federal expenditures exceed $10 billion.

(2) Federal programs not labeled Type A under paragraph (b)(1) of this section shall be labeled Type B programs.

(3) The inclusion of large insurance programs or loan and loan guarantees (loans) should not result in the exclusion of other programs as Type A programs. When a Federal program providing insurance or loans significantly affects the number or size of Type A programs, the auditor shall consider this Federal program as a Type A program and exclude its values in determining other Type A programs.

(c) *Step 2.* (1) The auditor shall identify Type A programs which are low-risk. For a Type A program to be considered low-risk, it shall have been audited as a major program in at least one of the two most recent audit periods, and, in the most recent audit period, it shall have had no audit findings under § _____.510(a). However, the auditor may use judgment and consider that audit findings from questioned costs under § _____.510(a)(3), fraud under § _____.510(a)(5), and audit follow-up for the summary schedule of prior audit findings under § _____.510(a)(6) do not preclude the Type A program from being lowrisk. The auditor shall consider: the criteria in § _____.525(c), § _____.525(d)(1), § _____.525(d)(2), and § _____.525(d)(3); the results of audit follow-up; whether any changes in personnel or systems affecting a Type A program have significantly increased risk; and apply professional judgment in determining whether a Type A program is low-risk.

(2) Notwithstanding paragraph (c)(1) of this section, OMB may approve a Federal awarding agency's request that a Type A program at certain recipients may not be considered low-risk. For example, it may be necessary for a large Type A program to be audited as major each year at particular recipients to allow the Federal agency to comply with the Government Management Reform Act of 1994 (31 U.S.C. 3515). The Federal agency shall notify the recipient and, if known, the auditor at least 120 days prior to the end of the fiscal year to be audited of OMB's approval.

(d) *Step 3.* (1) The auditor shall identify Type B programs which are high-risk using professional judgment and the criteria in § _____.525. Except for known reportable conditions in internal control or compliance problems as discussed in § _____.525(b)(1), § _____.525(b)(2), and § _____.525(c)(1), a single criteria in § _____.525 would seldom cause a Type B program to be considered high-risk.

(2) An audit under this part is not expected to test relatively small Federal programs. Therefore, except to meet the 50 percent rule discussed in paragraph (f) of this section, the auditor is only required to perform risk assessments on Type B programs that exceed the larger of:

(i) $100,000 or three-tenths of one percent (.003) of total Federal expenditures when the auditee has less than or equal to $100 million in total Federal expenditures.

(ii) $300,000 or three-hundredths of one percent (.0003) of total Federal expenditures when the auditee has more than $100 million in total Federal expenditures.

(e) *Step 4.* At a minimum, the auditor shall audit all of the following as major programs:

(1) All Type A programs, except the auditor may exclude any Type A programs identified as low-risk under Step 2 (paragraph (c)(1) of this section);

(2) At least one half of the Type B programs identified as high-risk under Step 3 (paragraph (d) of this section), except this paragraph (e)(2) does not require the auditor to audit more high-risk Type B programs than the number of low-risk Type A programs identified as low-risk under Step 2; and

(3) Such additional programs as may be necessary to comply with the 50 percent rule discussed in paragraph (f) of this section. This paragraph (e)(3) may require the auditor to audit more programs as major than the number of Type A programs.

(f) *50 percent rule.* The auditor shall audit as major programs Federal programs with expenditures that, in the aggregate, encompass at least 50 percent of total Federal expenditures. If the auditee meets the criteria in § _____.530 for a low-risk auditee, the auditor need only audit as major programs Federal programs with expenditures that, in the aggregate, encompass at least 25 percent of total Federal expenditures.

(g) *Documentation of risk.* The auditor shall document in the working papers the risk analysis process used in determining major programs.

(h) *Auditor's judgment.* When the major program determination was performed and documented in accordance with this part, the auditor's

judgment in applying the risk-based approach to determine major programs shall be presumed correct. Challenges by Federal agencies and pass-through entities shall only be for clearly improper use of the guidance in this part. However, Federal agencies and pass-through entities may provide auditors guidance about the risk of a particular Federal program and the auditor shall consider this guidance in determining major programs in audits not yet completed.

(i) *Deviation from use of risk criteria.* For first-year audits, the auditor may elect to determine major programs as all Type A programs plus any Type B programs as necessary to meet the 50 percent rule discussed in paragraph (f) of this section. Under this option, the auditor would not be required to perform the procedures discussed in paragraphs (c), (d), and (e) of this section.

(1) A first-year audit is the first year the entity is audited under this part or the first year of a change of auditors.

(2) To ensure that a frequent change of auditors would not preclude audit of high risk Type B programs, this election for first-year audits may not be used by an auditee more than once in every three years.

**§ _____.525 Criteria for Federal program risk.**

(a) *General.* The auditor's determination should be based on an overall evaluation of the risk of noncompliance occurring which could be material to the Federal program. The auditor shall use auditor judgment and consider criteria, such as described in paragraphs (b), (c), and (d) of this section, to identify risk in Federal programs. Also, as part of the risk analysis, the auditor may wish to discuss a particular Federal program with auditee management and the Federal agency or passthrough entity.

(b) *Current and prior audit experience.* (1) Weaknesses in internal control over Federal programs would indicate higher risk. Consideration should be given to the control environment over Federal programs and such factors as the expectation of management's adherence to applicable laws and regulations and the provisions of contracts and grant agreements and the competence and experience of personnel who administer the Federal programs.

(i) A Federal program administered under multiple internal control structures may have higher risk. When assessing risk in a large single audit, the auditor shall consider whether weaknesses are isolated in a single operating unit (e.g., one college campus) or pervasive throughout the entity.

(ii) When significant parts of a Federal program are passed through to subrecipients, a weak system for monitoring subrecipients would indicate higher risk.

(iii) The extent to which computer processing is used to administer Federal programs, as well as the complexity of that processing, should be considered by the auditor in assessing risk. New and recently modified computer systems may also indicate risk.

(2) Prior audit findings would indicate higher risk, particularly when the situations identified in the audit findings could have a significant impact on a Federal program or have not been corrected.

(3) Federal programs not recently audited as major programs may be of higher risk than Federal programs recently audited as major programs without audit findings.

(c) *Oversight exercised by Federal agencies and pass-through entities.* (1) Oversight exercised by Federal agencies or pass-through entities could indicate risk. For example, recent monitoring or other reviews performed by an oversight entity which disclosed no significant problems would indicate lower risk. However, monitoring which disclosed significant problems would indicate higher risk.

(2) Federal agencies, with the concurrence of OMB, may identify Federal programs which are higher risk. OMB plans to provide this identification in the compliance supplements.

(d) *Inherent risk of the Federal program.* (1) The nature of a Federal program may indicate risk. Consideration should be given to the complexity of the program and the extent to which the Federal program contracts for goods and services. For example, Federal programs that disburse funds through third party contracts or have eligibility criteria may be of higher risk. Federal programs primarily involving staff payroll costs may have a high-risk for time and effort reporting, but otherwise be at low-risk.

(2) The phase of a Federal program in its life cycle at the Federal agency may indicate risk. For example, a new Federal program with new or interim regulations may have higher risk than an established program with time-tested regulations. Also, significant changes in Federal programs, laws, regulations, or the provisions of contracts or grant agreements may increase risk.

(3) The phase of a Federal program in its life cycle at the auditee may indicate risk. For example, during the first and last years that an auditee participates in a Federal program, the risk may be higher due to start-up or closeout of program activities and staff.

(4) Type B programs with larger expenditures would be of higher risk than programs with substantially smaller expenditures.

**§ _____.530 Criteria for a low-risk auditee.**

An auditee which meets all of the following conditions for each of the preceding two years shall qualify as a low-risk auditee and be eligible for reduced audit coverage in accordance with § _____.520(f):

(a) The audits were performed in accordance with the provisions of this part.

(b) The auditor's opinions on the financial statements and the schedule of expenditures of Federal awards were unqualified. However, the cognizant or oversight agency for audit may judge that an opinion qualification does not affect the management of Federal awards and provide a waiver.

(c) There were no deficiencies in internal control which were identified as material weaknesses under the requirements of GAGAS. However, the cognizant or oversight agency for audit may judge that the material weaknesses do not affect the management of Federal awards and provide a waiver.

(d) None of the Type A programs, as defined in § _____.520(b), had audit findings from any of the following:

(1) Internal control deficiencies which were identified as material weaknesses;

(2) Noncompliance with the provisions of laws, regulations, contracts, or grant agreements which have a material effect on the Type A program; or

(3) Known or likely questioned costs that exceed five percent of the total expenditures for a Type A program during the year.

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