Professional Ethics

Most Frequent Violations of Professional Standards

Government and Not For Profit Investigations

As of December 31, 2012
Executive Summary

The AICPA Professional Ethics Division has compiled the following list of deficiencies frequently found in its investigations of audits of government and not-for-profit entities over the last 2 years. Over that time, the division has conducted a total of 498 investigations, 226 of which were of such entities. Most often, these errors have occurred as a result of a lack of experience and specific continuing professional education in these areas and could have been detected by a quality control review of the financial statements and risk areas.
Single Audit Issues

Failure To Accurately Identify and Test All Major Programs

The auditor failed to accurately identify and test all major programs in accordance with the Office of Management and Budget Circular A-133, Audits of States, Local Governments and Non-Profit Organizations, §.520, “Major program determination.” This is still our most pervasive problem found. The most common reasons that this occurs follow:

1. Failure to combine Catalog of Federal Domestic Assistance (CFDA) programs
2. Improper clustering
3. Using an improper threshold either because of the problems identified below or making a preliminary assessment without making adjustments for items’ final balances
4. Improper low risk assessment with resulting percentage of coverage missed
5. Failure to consider loans in major program assessment
6. Failure to audit amounts on the Schedule of Expenditures of Federal Awards (SEFA)

Incorrect Dollar Threshold Used

The Schedule of Findings & Questioned Costs incorrectly identified the dollar threshold used to distinguish between Type A and Type B programs. There continues to be a lack of education about this threshold; many practitioners believe the threshold for determining a major program is $500,000 confusing it with the single audit requirement. Based on information in the Federal Audit Clearinghouse, this is not isolated to ethics cases; the problem is pervasive.

Improper Risk Assessment

The auditor improperly identified the entity as a low risk auditee. Recently, we have seen that the auditor performed a single audit in a prior year when no Data Collection Form was due (for example, the auditee did not meet the single audit threshold) and believed this did not disqualify a low risk assessment. Similarly, if the auditee did not file a Data Collection Form in a prior year when it was required, the auditor did not consider this in his or her risk assessment.

Missing Information In the SEFA

The SEFA had missing information such as (1) the CFDA number (or other identifying number when the CFDA information is not available), (2) name of the federal agency or the name of pass-through entity and identifying number assigned by the pass-through entity, and/or (3) the total federal expenditures for each federal program, or (4) it did not include notes describing the significant accounting policies used in preparing the schedule.
Auditor’s Reporting

Improper Audit Report Date
The auditor did not properly date the audit report. This usually occurs because the auditor reissued the report as a result of additional disclosures or audit procedures but did not dual date or re-date the report. However, we have also seen instances in which the auditor dated the report before obtaining sufficient evidence.

Character of Examination and Degree of Responsibility
The auditors' report did not contain an appropriate indication of the character of the examination and the degree of responsibility taken with respect to the required supplementary information or supplementary information accompanying the basic financial statements other than with respect to the SEFA.

Summarized Information
The auditor failed to opine on the prior year’s summarized information and failed to note that the financial statements did not disclose that the prior year’s summarized information did not constitute a presentation in accordance with generally accepted accounting principles (GAAP).

SAS No. 115
The auditor did not comply with Statement on Auditing Standards (SAS) No. 115, Communicating Internal Control-Related Matters Identified in an Audit, in wording their reports. The definitions of control deficiencies, significant deficiencies, and material weaknesses followed language in superseded guidance. This problem is frequent despite the age of the SAS.

Opinion Units and Departures Not Specified
The Yellow Book (Government Auditing Standards) report lacked specification of opinion units in the first paragraph and did not indicate the departures from the standard audit report.

Omitted Required Opinion and Report Wording
The auditors’ opinions, including the reports required under the Yellow Book and the Single Audit Act of 1984, omitted wording particular to government engagements. It is particularly prevalent in the paragraph in the report on the financial statements referring to the Yellow Book report.
Audit Procedures

Allocation of Indirect Expenses

The auditee allocated indirect expenses using rates in the grant agreement and failed to determine whether this was a systematic or rational basis.

Failure to Obtain Sufficient Competent Evidential Matter

The auditor did not obtain sufficient competent evidential matter to support the opinion on the financial statements. Although we see this in all areas of the audit, the most frequently seen problems concern the following:

1. Testing of compliance requirements; sometimes the work papers include the matrix in the compliance supplement with some checkmarks next to it.
2. Use of out-of-date work programs or disclosure checklists that result in audit deficiencies.
3. Improper use of dual purpose testing; the auditor often does not adequately design procedures to meet compliance requirements.
4. Lack of an understanding of the difference between internal control and compliance testing.

Inadequate Documentation

Documentation of procedures performed was inadequate. This is seen in all areas of the audit.

Audit Program

The auditor failed to utilize or customize an audit program.
Financial Statement Deficiencies

Reporting Expenses

1. The financial statements did not report expenses by their functional classification, such as major classes of program services and supporting services.

2. The financial statements did not allocate indirect expenses on a systematic or rational basis or by natural expense category. Often there is a line titled “Indirect costs” or “Allocated expenses” in the statement of functional expenses.

Donated Services

The financial statements reported donated services that do not meet the requirements of GAAP. This is often done because the entity has a matching requirement under the grant contract and wants to reflect this in the financial statements.

Nature and Amount of Donor-Imposed Restrictions Not Disclosed

The financial statements did not disclose the nature and amount of donor-imposed restrictions related to temporarily or permanently restricted net assets.

Fair Value Disclosure

The financial statements omitted fair value disclosures required by Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820 (FASB Statement No. 157, Fair Value Measurements) or made errors in the disclosure, such as the level of investment. Right now, this is our most frequently seen disclosure problem.

Management Discussion and Analysis

The Management Discussion and Analysis (MD&A) was missing required elements or was not presented as required and the auditor's did not modify the opinion.

Revenues Not Properly Classified

The Combined Statement of Revenues, Expenditures, and Changes in Fund Balances did not properly classify revenues by fund and source or expenditures by function or character.

Unreserved Fund Balance

On the fund balance sheet, the financial statements did not disclose the unreserved fund balance related to non-major governmental funds by fund type in the Balance Sheet-Governmental funds.

Interfund Balances
1. On the fund balance sheet, the interfund receivables and payables with respect to the discretely presented component unit do not balance in the combined balance sheet and were not disclosed in the notes.
2. The auditor did not eliminate interfund and intrafund balances and transactions or disclose their purpose.

Disclosure of Prior Period Adjustments
When there were prior period adjustments, the disclosures did not include nature, reason, or amount and may not have been properly presented within the net income and the like of the prior year comparative financial statements.

Disclosure Concerning Liabilities and Debt Service
The financial statements did not disclose terms and rates of long-term liabilities and debt service requirements for future years.

Subsequent Events
The financial statements did not make the subsequent events disclosures recently required by FASB ASC 855-10-50 (FASB Statement No. 165, Subsequent Events).
Other

Continuing Professional Educational Requirements

The auditor failed to comply with the continuing professional education requirements contained in Government Auditing Standards.