

Audit Best Practices: How to Prepare for Financial and Compliance Audits

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Internal Controls and Documentation

- What is an Internal Control?
- Why are Internal Controls important?
- How do Internal Controls affect my audit?

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What is an Internal Control?

- Policies and procedures
- Communication
- Monitoring and oversight
- Overall control environment – “Tone at the Top”

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Why are Internal Controls Important?

- Strong controls lead to commitment to integrity and ethical values
- Reduce incentives and temptations for fraudulent or unethical activities
- Ensure management and governing board are made aware of day to day issues and that approved policies are being implemented

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How do Internal Controls affect my audit?

- Risk assessments
- Amount of testing performed
- Areas of testing and supplemental testing
- Streamlining of financial reporting process

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Basic Internal Controls/Control Environment

- Establish code of conduct and/or ethics policies
- Communicate policies to employees
- Implement procedures to communicate changes in policies
- Set realistic expectations for goals to be achieved and allow for feedback
- Incorporate changes and updates to policies as necessary

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Specific Controls

- Should be documented and consistent
- Allow for little or no management override
- Specific to the needs of your entity and operations
- Narratives/walkthroughs

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Payroll/HR Controls

- New hire packet documentation
- Approval of supervisors for timesheets, leave requests, etc.
- Employee evaluations performed on a regular basis
- Cross training of employees and mandatory vacations
- Clearly communicated responsibilities/segregation of duties

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Payroll/HR Controls – Audit Preparation

- Employee files are up to date, accurate and available for all employees paid during the audit period
- Support for paychecks is available and organized (pay date, individual, etc.)
- Narrative/walkthrough is available to auditors
- All implemented and approved internal controls are documented

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Disbursement/Procurement Controls

- Policies clearly dictate procedures for purchasing:
 - Micro-purchases
 - General purchasing
 - Competitive bidding

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Disbursement/Procurement Controls

- Internal documentation (voucher):
 - Requisitions/purchase orders
 - Invoices
 - Approvals
 - Bill of lading or similar
 - Payment and review

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Disbursement/Procurement Controls – Audit Preparation

- Written policies and recently approved updates to policies are available to auditors and approved in governing board minutes
- Voucher packets are complete and organized
- Narrative/walkthrough is available to auditors
- All implemented and approved internal controls are documented

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Budgetary Controls

- Estimated receipts
- Actual disbursements and encumbrances
- 5 year forecast
- Capital requirements, debt requirements and cash flows

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Budgetary Controls – Audit Preparation

- Documentation of estimated receipts
- End of year balance(s)
- Grant awards
- Approved appropriations/budget
- Supplemental appropriations and approvals
- Outstanding encumbrances and liabilities
- Narrative

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Revenue/Cash Receipts Controls

- Documentation of cash collection points and procedures for differing types
- Physical control over cash collections and reconciliation of deposits
- Monitoring of cash collections and spot-checking for accuracy
- Incentives to encourage accurate accounting
- Pre-numbered receipt documentation and point of sale systems

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Revenue/Cash Receipts Controls – Audit Preparation

- Support for revenue is available and organized
- Property taxes are accounted for at gross receipts
- Grant receipts are properly documented
- Point of sale reports are reconciled and documented
- Accounts receivable aging schedule is available to auditors
- Narrative/walkthrough is available to auditors
- All implemented and approved internal controls are documented

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Cash Controls

- Monthly cash reconciliation
- Review and approval of monthly cash reconciliation
- Investigation of all reconciling items and documentation of support
- Cross training of employees
- Segregation of duties
- Investment policies

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Cash Controls – Audit Preparation

- Monthly cash reconciliations are properly documented and available
- Reconciling items are supported and documented
- Online access to bank accounts and Ohio Pooled Collateral System (OPCS)
- List of bank contact information and bank accounts
- Support for investments

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Capital Asset/Inventory Controls

- Maintenance of capital asset listing
 - Additions
 - Disposals
 - Salvage valuations
 - Useful life/asset classification
 - Method of depreciation/depreciation calculations
- Asset valuation by third party

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Capital Asset/Inventory Controls

- Physical control over inventory
- Procedures for processing purchases and usage of inventory
- Communication to employees regarding inventory policies
- Spot checks and interim inventory counts and reconciliations
- Inventory counts and reconciliation
- Financial accounting methods

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Capital Asset/Inventory Controls – Audit Preparation

- Complete and accurate capital asset listing
- Written policies and procedures for updating capital asset listing and capitalization thresholds
- Written policies and procedures for inventory control and reconciliation
- Documentation of depreciation calculations and postings
- Documentation of inventory reconciliation and postings
- Notify auditor of when and where inventory counts are being performed

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Debt Controls

- Adherence to all debt covenants and lease agreements
- Approval of all debt agreements by governing board
- Reconciliation of liabilities with amortization schedules
- Allocation of current and long-term portion of liabilities

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Debt Controls – Audit Preparation

- All debt documentation is available – particularly amortization schedules
- Debt schedule of outstanding liabilities is available
- Listing of entities holding debt instruments

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Miscellaneous Controls

- Allowance for doubtful accounts/write off of uncollectible amounts
- Obsolete inventory

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Miscellaneous Controls – Audit Preparation

- Written policies are available to auditors
- Approval of write offs is documented
- Obsolete inventory is documented and supported
- Calculation of estimates is supported by underlying data

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Financial Statement Controls

- Complete and accurate – GAAP requires:
 - Management's Discussion & Analysis
 - Statement of Net Position
 - Statement of Revenues, Expenses and Changes in Net Position
 - Statement of Cash Flows
 - Notes to the Financial Statements
 - Required Supplementary Information (GASB 68 & GASB 75)

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Financial Statement Controls

- Federal granting agencies require:
 - Schedule of Expenditures of Federal Awards (SEFA)
 - Notes to the Schedule of Expenditures of Federal Awards
 - Certification of SEFA on Federal Data Clearinghouse website
- Ohio Auditor of State requires:
 - Schedule of Prior Audit Findings
 - Audit Recipient Spreadsheet (generally prepared by auditor)

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Financial Statement Controls

- Trial balance is complete and accurate with support for all items
- Calculation of investment in capital assets and restricted net position is updated and supported
- Calculation for cash flows is available and all amounts are supported
- Use of a knowledgeable third party for all or part of the compilation and review
- Review by individual(s) with the knowledge to correct mistakes and assess accuracy and completeness

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Financial Statement Controls

- Accurate and complete accounting of federal grants
- SEFA should include:
 - Granting agency and any pass-through entities
 - Catalog of Federal Domestic Assistance (CFDA) number
 - Pass-through grant number (if any)
 - Subrecipient information (if any)

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Financial Statement Controls

- Notes to the SEFA should include:
 - Summary of significant accounting policies specific to federal awards
 - Election of 10% de minimis cost rate
 - Approved carryover of any federal awards

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Financial Statement Controls – Audit Preparation

- Use newest version of SEFA template and SEFA note template available on Auditor of State website: www.ohioauditor.gov
- Use newest version of Schedule of Prior Audit Findings template available on Auditor of State website – complete on letterhead, if possible
- SEFA, Notes to SEFA, and Schedule of Prior Audit Findings should be provided to auditor at start of fieldwork or earlier

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Financial Statement Controls – Audit Preparation

- All support for federal expenditures and accruals (if applicable) should be available
- Inventory of capital assets purchased with federal funds should be available
- Approval and support for carryover federal awards should be available

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Compliance Controls

- Integrated with controls over financial reporting
- Exceptions:
 - Continuing education requirements
 - Public records training and policy and records retention policy and schedule
 - Bonding requirements, if applicable
 - Fraud, conflicts of interest, ethics policies

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Compliance Controls

- Significant integrated controls:
 - Annual financial statement reporting (HINKLE)
 - Issuance of revenue bonds
 - Health care/liability self-insurance requirements
 - Investment requirements
 - Mandated accounting records
 - Allocation of audit costs
 - Deposits of public money
 - Withholding of payroll deductions/contributions to retirement plans

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Compliance Controls – Audit Preparation

- All policies should be available
- All minutes should be available
- Certificates for education requirements should be available
- Ask your auditor for a list of items necessary

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Single Audit Controls

- Written policies are required for:
 - Cash management
 - Determining allowable costs
 - Evaluation and selection of procurement by competitive proposals
 - Time and effort

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Questions?

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