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Professional Ethics

Most Frequent Violations of Professional Standards

Government and Not For Profit Investigations

As of June 30, 2016

Executive Summary

The AICPA Professional Ethics Division has compiled the following list of quality issues found in its investigations of government and not-for-profit entities audits during the last two years. Over that time, the division has completed 596 investigations, 145 of which were government and not-for-profit entities. In instances where reporting, disclosure, and auditing errors were noted, the practitioner often could have benefited from additional experience and specific continuing professional education in this specialized area. A quality control review of the financial statements and risk areas could also have detected the errors. When such quality issues are identified, the member is subject to remediation (for example, continuing professional education, pre-issuance reviews of select engagements by an independent third party) and in some instances sanctions that include publication and admonishment, suspension, or expulsion from AICPA membership.

Single Audit Issues

1. The auditor failed to accurately identify or 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*, section_520, “Major program determination.” The most common reasons that this occurs is as follows:
    a. Failure to combine expenditures from various funding agents having the same Catalog of Federal Domestic Assistance (CFDA) number;
    b. Improper clustering of related program CFDA numbers;
    c. Using an improper threshold;
    d. Improper low risk auditee assessment, which results in failing to obtain the correct percentage of audit coverage;
    e. Failure to consider large loans in major program assessment; and
    f. Failure to audit amounts on the Schedule of Expenditures of Federal Awards (SEFA). (An oversight.)
2. The Schedule of Findings and Questioned Costs incorrectly identified the dollar threshold used to distinguish between Type A and Type B programs**.** The single audit requirement was set at a threshold of $500,000 in 2005. Practitioners continue to be confused, using this amount as the type A major program threshold. Based on information in the Federal Audit Clearinghouse, this is not isolated to ethics cases; the problem is pervasive.
3. The auditor improperly identified the entity as a low risk auditee. The most common reasons this has occurred has been:
    a. The auditee did not file a Data Collection Form in a prior year;
    b. A qualified opinion was issued within the prior two years either over the financial statements or the SEFA;
    c. There were material weaknesses in internal controls over financial reporting or federal compliance within the last two years; and
    d. Material noncompliance on federal programs within the last two years.
4. 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, (3) the total federal expenditures for each federal program, and (4) did not include notes describing the significant accounting policies used in preparing the schedule.

Auditor’s Reporting

1. 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 redate the report. We have also seen instances; however, in which the auditor dated the report before obtaining sufficient evidence.
2. 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.
3. The auditor failed to qualify the report when there were departures from GAAP.
4. The auditor failed to opine on the prior year summarized information and failed to note that the financial statements did not disclose that the prior year summarized information did not constitute a presentation in accordance with GAAP; or, the auditor incorrectly opined on the comparative financial information when that information was presented in summarized form.
5. The auditor’s report incorrectly stated that the financial statements were issued in conformity with an Other Comprehensive Basis of Accounting based on a regulatory basis prescribed by a federal agency. Federal agencies do not prescribe a regulatory basis of accounting.
6. Auditors did not properly define in their reports the definition of deficiencies in internal control, significant deficiencies, and material weaknesses. The definition in the reports followed language in superseded guidance.
7. The auditor did not report audit findings in the Schedule of Findings and Questioned Costs with all of the required elements, the specific federal award identification including CFDA number, the name of the federal agency, or reference number or any other required component of a finding.
8. There is an inconsistency in the reporting of findings between the Summary of Audit Results, the Yellow Book, and A-133 reports being reported in one but not the other.

Audit Procedures

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

   a. Testing of compliance requirements;
   b. Use of out-of-date work programs or disclosure checklists that result in audit deficiencies;
   c. Improper use of dual purpose testing; the auditor often does not adequately design procedures to meet compliance requirements;
   d. Lack of an understanding of the difference between internal control and compliance testing; and
   e. Inappropriate or unsupported sample sizes.

2. Failure to perform or document analytical procedures in the planning and final stages of the audit.
3. Documentation of procedures performed was inadequate. This was seen in all areas.
4. The auditor failed to utilize or customize an audit program.

Financial Statement Deficiencies

1. The financial statements of not-for-profit entities omitted fair value disclosures required by the 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.
2. The financial statements did not make the subsequent events disclosures required by FASB ASC 855-10-50 (FASB Statement No. 165, *Subsequent Events*).
3. The financial statements of not-for-profit entities did not report expenses by their functional classification, such as by major classes of program services and supporting services or failed to report expenses by natural expense categories, for example, classifying expenses “indirect expenses.”
4. Inadequate post retirement disclosures for government entities.
5. Interfund and intrafund balances and transactions were not eliminated in governmental entities and, as such, the statements of financial position and activities did not focus on the organization as a whole. Also their purpose wasn't disclosed in the notes.
6. The financial statements did not disclose the nature and amount of donor-imposed restrictions related to temporarily or permanently restricted net assets in not-for-profit entities.
7. The financial statements of not-for-profit entities reported donated services that do not meet the requirements of GAAP. This is often done because the entity has a matching requirement under its grant contracts and wants to reflect this in the financial statements.
8. The Management Discussion and Analysis in governmental entities was missing required elements or was not presented as required and the auditor’s opinion was not modified.
9. The statement of revenues, expenditures, and changes in fund balances in governmental entities did not properly classify revenues by fund and source or expenditures by function or character.
10. The financial statements did not disclose terms and rates of long-term liabilities and debt service requirements for future years.
11. The basic financial statements are not prepared in conformity with the standards applicable for not-for-profit entities, for example in that they do not focus on the organization as a whole, as they are presented on a combining fund basis with a total column.

Other

1. The auditor failed to comply with the continuing professional education requirements contained in *Government Auditing Standards*.
2. The firm failed to undergo peer review as required by state board and Yellow Book requirements or by the requirements of the AICPA and state CPA society.

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