Cognizant Agencies of the Single Audit

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The Single Audit Act of 1984 is the result of nearly twenty years of controversy. A need for single audits arose primarily because of the steep increase in the number of federal grants, an increase of approximately ninety billion dollars over the twenty years. The Comptroller General of the United States reported that audits were not performed on a surprising eighty percent of the federal grant funds spent from 1974-1977. Furthermore, some recipients were not audited even one time, while others reported being audited more than fifty times (Brown and Burnaby 47).

On October 19, 1984, President Reagan signed the Single Audit Act into law. The signature brought into practice a new auditing approach on federal grant monies given to state and local governmental units. The Act allows for an organization-wide audit of these federal grants, rather than the grant-by-grant approach previously used. The major purpose of the new system was to make audits less costly and less duplicative.

An important aspect of the single audit involves cognizant agencies which are assigned to provide guidance to the audited governmental units and review the audit reports. This paper examines the implementation of the cognizant agency concept within the single audit. Some of the problems concerning this implementation will be discussed, and solutions will be proposed to increase the effectiveness of cognizant agencies in practice.
REVIEW OF THE SINGLE AUDIT ACT OF 1984

In 1979, Circular A-102 (Attachment P) was issued by the Office of Management and Budget (OMB). This administrative directive called for single audits, but implementation of the single audit concept was slow and limited. Legislative action was necessary for full-scale implementation to be effective, and this action came with Public Law Number 98-502, better known as the Single Audit Act.

Section 1(b) of the Act states its objectives:

1. to improve the financial management of State and local governments with respect to Federal financial assistance programs;

2. to establish uniform requirements for audits of Federal financial assistance provided to State and local governments;

3. to promote the efficient and effective use of audit resources; and

4. to ensure that Federal departments and agencies, to the maximum extent practicable, rely upon and use audit work done pursuant to chapter 75 of title 31, United States Code (as added by this Act).

The effective date of the Act is fiscal years beginning after December 31, 1984.

The Act also set down guidelines for determining the requirement for a single audit of a governmental unit. Governmental units that receive $100,000 or more per year in federal assistance are required to have annual, independent audits on financial statements, internal controls, and compliance regarding each major program. Those who receive $25,000 to $100,000 annually have an option; they may elect to have a
single audit or comply with the previous requirements under the applicable federal program. Lastly, those units that obtain less than $25,000 per year are only required to maintain adequate accounting records, including documentation concerning grants received; they generally do not have to have an audit performed on the grant monies. These monetary standards include assistance received directly from federal grant agencies, as well as money received indirectly through another state or local governmental unit. The recipients of assistance in the latter situation are referred to as subrecipients.

At least three different audit reports are required with a single audit. (1) A standard report is issued giving an opinion on the financial statements of the unit. (2) A report on an evaluation of internal controls must include the controls examined, controls not examined and why, and identified weaknesses. (3) Finally, a report on an audit test of compliance pertaining to each major program must be compiled. To determine compliance, a listing of federal funds is supplied by the governmental unit. The auditor then examines a specified number of transactions from each major program. The report includes a positive statement of assurance for items tested, negative assurance for items not tested, a summary of instances of noncompliance, and a final report of amounts questioned, if any.

The issued reports are submitted to: the audited unit, those who arranged for the audit, all applicable federal granting
agencies, and the original recipient of funds in the case a subrecipient is audited. Reports must be submitted within thirty days of the completion of the audit. The federal agencies use these reports to determine whether additional auditing is necessary.

HISTORY OF THE COGNIZANT AGENCY

A cognizant agency is "the Federal agency that is assigned audit responsibility for a particular recipient organization by the Office of Management and Budget (Attachment P)." All major recipients of grants are assigned a cognizant agency, which is simply one of the federal grant agencies providing money to the governmental unit.

Attachment P not only requires a cognizant agency, but also sets down its responsibilities. Cognizant agencies are responsible for:

1. reviewing the auditors' work and providing information concerning the audit to other applicable granting agencies,

2. ensuring that audits are performed completely and timely,

3. seeing that corrective action is taken if warranted,

4. acting as a liaison among the various federal agencies, and

5. informing these other agencies if irregularities exist.

After the enactment of the Single Audit Act, the OMB began assigning cognizant agencies. This Act reasserts the responsibilities of the cognizant agency as set down in
Attachment P of Circular A-102. Presently, cognizant agencies have been assigned to 1800 units requiring a single audit out of the over 80,000 units of state and local government. The units assigned a cognizant agency include all states, major counties, and major cities.

IMPLEMENTATION OF THE COGNIZANT AGENCY

Implementation of the cognizant agency concept was extremely slow despite efforts of the General Accounting Office (GAO) and the OMB to establish guidelines. One major reason for the delay in full implementation was that no penalties existed for not having a single audit performed under Attachment P (Cronin, personal interview). Additionally, many recipients of federal grant monies did not believe that the granting agencies serving as cognizant agencies were knowledgeable enough to perform their role in the single audit adequately (Steinberg, Miller, and Menzel 58). Many people believed that the Single Audit Act was needed to ensure acceptance of the single audit concept.

Adoption of the Single Audit Act was the largest factor in implementation of the single audit concept and in the appointment of cognizant agencies. A factor which enabled cognizant agencies to be effective was the variety of education made available to them. This education came in the form of publications by several agencies, most notably "Cognizant Agency Guidelines" published by the Joint Financial Management Improvement Program.
IMPACT OF THE COGNIZANT AGENCY IN THE SINGLE AUDIT

If the cognizant agencies do not perform their duties as assigned, the single audit's effectiveness is decreased. Therefore, cognizant agency performance in actual practice should be examined. Interviews conducted with 1) CPAs working in the public sector, 2) a State Board of Accounts auditor in Indiana, and 3) the director of GAO's Quality Task Force in Washington, D.C., provided data to gain insight concerning the effectiveness of the cognizant agency in practice. A sampling of these questions follows:

1. Who determines the cognizant agency?

One CPA reported that the auditee can usually identify its cognizant agency. This situation occurs because CPAs in Indiana who audit governmental entities audit only large units. These units are among the 1800 which have had cognizant agencies assigned to them by the OMB. Units which do not have a cognizant agency designated for them are placed in a general oversight category. These units, which come under the scope of the Indiana State Board of Accounts, receive single audit guidance from the primary grantor of funds to them for the year under audit. In this case, the units must determine each year who to contact for assistance and where to send the audit report. Governmental units in the general oversight category may send their audit report to different grant agencies each year. This can
result in unsubstantial review by the agencies because they may not be responsible for the unit's audit next year.

2. What do the cognizant agencies do with the reports sent to them?

Several auditors believe that the reports are simply filed away. One CPA stated that it depends on the agency and the size of the unit. On the other hand, a State Board of Accounts auditor discussed one case in which the cognizant agency was able to identify the cause of a discovered shortage which resulted in the payment of a charge by the party responsible.

3. What causes the cognizant agencies to be effective or ineffective in their role in the single audit?

One of the auditors interviewed claimed that the cognizant agencies are indecisive when problems arise, stating that he had been in situations in which the cognizant agency was quick to solve small problems, yet avoided large ones. He also believes a high turnover of employees within granting agencies exists and results in a lower level of competence. He said that oftentimes he will call a cognizant agency and ask for the person he talked to last year only to learn that the person no longer works for the agency. Both of these situations decrease the effectiveness of the cognizant agency.
4. What changes would you like to see concerning the role of cognizant agencies in the single audit? This question was asked of an official from the General Accounting Office who is involved with audit quality. He stated that he would like to see the aforementioned general oversight category given more defined responsibilities. He stated that a review of 2300 single audits performed in 1986 resulted in 34 percent requiring some degree of modification. Most of these substandard reports were audits of smaller governmental units which fall under this general oversight category. When asked if he would like to see cognizant agencies assigned to these general oversight units, he replied that the measure would result in too great a task for the federal agencies. On the other hand, he believes a level between general oversight and cognizant agency assignment involving increased review and testing would greatly improve the quality of single audit reports by identifying more of the errors that occur in the reports.

The cognizant agency concept does not appear to be working as well in practice as the framers hoped it would. One major reason for this may be that not all units requiring a single audit are assigned a cognizant agency. Therefore, the federal granting agencies see their responsibilities to the single audit from two very distinct sides.
First, the granting agencies serve as cognizant agencies to some units. They work with these units yearly, becoming familiar with them, and the granting agencies are provided with very definite responsibilities to these units. Second, they have a varying group of units each year to which they provide general oversight. They may not have been involved with several of these units' audits in the previous year and may not be required to assist them next year. Their responsibilities to these units are not as well defined. Therefore, these units may not be given much priority and are more likely to have their reports overlooked and routinely filed away.

PROPOSED IMPROVEMENTS

The general oversight category should be revamped. Considering that all federal grant agencies provide general oversight to units each year, it seems reasonable that they could provide this general oversight to the same units each year. If these units are assigned to the same granting agency each year, communication among the auditor, auditee, and granting agency would have the benefit of history and could be improved. This improved communication is an important factor in increasing coordination among the parties involved in the single audit, which is vital for the cognizant agency to be effective in its role.

Improved communication can be attained by performing two important steps in the audit process. The auditor should contact
the cognizant agency in order to establish a representative within the agency for the audit. Establishing one contact person from the cognizant agency is very important. The representative can more accurately provide answers to questions because he can become more closely involved with the audit. This situation also reduces the risk of the auditor or unit receiving inconsistent information from varying sources within the cognizant agency.

Also, prior to beginning the field work, the auditor can conduct a planning meeting between the auditor, a representative from the governmental unit, and the designated representative from the cognizant agency. The planning meeting can accomplish several goals, the most important being the initial exchange of information between the parties. This exchange is vital because it enables the auditor to resolve differences before commencing field work. The topics addressed should include: the scope of the audit, the audit reports to be issued, compliance requirements, and sampling plan (Steinberg, Miller, and Menzel 61-62). In discussing the audit reports, the format and the number of reports to be issued should be determined.

Reviewing and testing of the audit reports of these general oversight units should be increased. Materiality would cause this increase to remain below the level attained for units assigned a cognizant agency, but the quality of the reports could still be improved.
CONCLUSION

The cognizant agency concept of the single audit is a promising idea. Cognizant agencies must educate themselves concerning the processes of state and local governmental units. With increased understanding of these grantees, the agencies will possess greater ability to assist in the single audit. Increased coordination among the auditor, governmental unit, and cognizant agency is vital for the success of the single audit (Broadus and Comtois 63). This coordination can be improved most effectively in the planning stage of the audit.

Additionally, the general oversight category of the single audit must be examined. Studies have shown that the majority of single audit reports requiring modification has involved reports within this category. Increased review and testing of these reports by the federal agencies can reduce errors while improving audit quality.
BIBLIOGRAPHY


