

Analyzing Financial Statements and Risk Assessment Updates

November 10, 2016

Florida Grants Consortium Workgroup



Objectives

To help answer questions submitted for

- Financial statement reviews / processing
- Federal or state requirements for risk assessments

To share questions and draft tools

To identify other topics of interest and future training opportunities



Agenda

Overview

- Financial Statements
 - Why they are important
 - Sample (draft) review tool
- Entity Risk Assessments
 - What's needed – the basics
 - Sample (draft) review tool
- Open Forum – Q&A



Overview – Financial Statements

Financial Statements

- Background
- Types of statements
- Breakdown of different sections
- Tasks / To Do List to complete analysis
- Red Flags and other tips



Financial Statements

What are they?

- A snapshot of an entity's operations
- Notes and additional explanations
- Group of tables/statements that show you the money
 - Where the money came from (income)
 - Where the money went (expenses)
 - Where the money is now (assets/equity)



Financial Statements

Who is responsible for processing them?

- Assignments vary across agencies
 - Many OIG retain primary responsibility
 - Contracts Administration Team
- Duties for Project/Contract Managers
 - Will vary in scope across agencies
 - To assess stability and experience of potential Contractors/Sub-grantees for agency



Financial Statements

Why do I need to review them?

- To judge a potential Contractor's ability to
 - Provide services as scoped and on timely basis
 - Communicate with agency staff
 - Support/help meet grant program goals, objectives and performance measures
- To document the review process used and results obtained



Financial Statements

When should the review(s) be done?

- During procurement phase for competitive procurements
- During pre-award phase for non-compete agreements
- Before execution of contract/award
- Post-award on a periodic basis



Financial Statements

Where do I find the data I need?

How do I search for the data I need?

How do I judge the data I find?

- Key items are shown in different sections of the statements, notes and reports
- Look for certain disclosures and/or perform analytic calculations
- Use a tool or other form to document your results



Financial Statements

Types of financial statements issued

- Audited
 - Offer most reliability; are prepared by CPAs
- Reviewed
 - CPAs/accountants prepare from entity's books and perform limited inquiry/analytical tests
- Compiled
 - Prepared from entity books with no tests done
- Other presentations – will vary



Financial Statements

Financial statements/schedules (cont'd)

1. Balance Sheets

- Include assets, liabilities and S/H equity
 - Show what the entity has of value
 - Show money/debts entity owes to others
 - Show equity, fund balances or working capital
- Reminder - the titles/labels used will vary with each entity (for-profit companies, governments, non-profits)
 - See workshop handouts for specific examples



Financial Statements

Financial statements/schedules (cont'd)

2. Income Statements

- Show revenue earned for specific time period
 - Show related costs and expenses
 - Show gain or net loss for the period
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- Reminder - the titles/labels used will vary with each entity (for-profit companies, governments, non-profits)
 - See workshop handouts for specific examples



Financial Statements

Financial statements/schedules (cont'd)

3. Cash Flow Statements

- Show cash inflows/outflows for specific time period
 - Show operating, investing and financing activities
 - Help you see if entity generated cash
- Reminder - the titles/labels used will vary with each entity (for-profit companies, governments, non-profits)
 - See workshop handouts for specific examples



Financial Statements

Financial statements/schedules (cont'd)

4. Schedule of Expenditures of Federal Awards (SEFA)

- Prepared by entity/auditee
 - Shows individual federal programs by #/agency
 - Shows total awards expended for each program, including non-cash assistance, insurance and loans/loan guarantees
 - May include note disclosures
- Note – this schedule is required for entities subject to federal and/or state Single Audit Act
 - See workshop handouts for specific examples



Financial Statements

Financial statements/schedules (cont'd)

5. Schedule of Findings and Questioned Costs

- Shows summary of auditor's results
 - Shows financial statement findings
 - Shows federal award findings/questioned costs
 - Shows state award findings/questioned costs
 - Other useful disclosures – see examples
- Note – this schedule is required for entities subject to federal and/or state Single Audit Act
 - *See workshop handouts for specific examples*



Financial Statements

How to review financial statements

- Know type of financial statements received
- Look at balance sheet
- Look at income statement
- Look at cash flow statement
- Look at the note disclosures
- Look at supplemental information (if any)

– *See workshop handouts for specific examples*



Financial Statements

Analyzing Operating Performance

- Tips for reviewing data for one year only
 - Look for completeness of filings/forms
 - Look for related note disclosures
 - Look for potential red flags
- Tips for reviewing data for multiple years
 - Consider using ratio analytics
 - Look for potential red flags



Financial Statements

Ratio Analytics – four main categories

1. Liquidity ratios

- Used to determine how quickly an entity can convert assets to cash if needed

2. Profitability ratios

3. Activity ratios

- Show how well resources are managed

4. Leverage/Equity ratios

- Show how much an entity relies on debt



Financial Statements

Potential “red flags” for operations

1. Rising debt-to-equity ratio
2. Several years of revenue trending down
3. Large “other” expenses
4. Unsteady cash flow
5. Rising accounts receivable or inventory in relation to total sales
6. Rising outstanding share count
7. Consistently higher liabilities than assets
8. Decreasing gross profit margin



Financial Statements

Review other disclosures

- Look at the notes to the financial statements
 - Data items
 - Red flag notes
- Look at other supplemental information
 - MD&A
 - Management representations letter
 - *See workshop handouts for specific examples*



Financial Statements

Audit reports and other schedules

1. FS report
2. Program report
3. Internal Controls (IC) report
4. SEFA
5. Schedule of findings/questioned costs
6. Auditor management letter
 - *See workshop handouts for specific examples*



Financial Statements

Closing thoughts

- You (or your team) can do this!
- Missing files/forms also tell you about risk
- Remember
 - Each set of financial statements typically follows a pattern of disclosures
 - Use the examples provided to shorten your search time
 - Document your review results



BREAK



Overview - Risk Assessments

Risk Assessments

- Background
 - Federal instructions
 - State instructions
 - Recap of pass-through entity requirements
- Evaluating risks
 - What's needed – the basics
 - Sample (draft) review tool



Risk Assessments

What are they?

Risk – the chance that something will happen that will adversely impact the success of achieving expected results

Risk assessments - a thoughtful process designed to identify and evaluate operating conditions for an entity



Risk Assessments

Who is responsible for these tasks?

- Assignments vary across agencies
 - Contracts Administration Team
- Duties for Project/Contract Managers
 - Will vary in scope across agencies
 - To assess stability and experience of potential Contractors/Sub-grantees for agency



Risk Assessments

Why are they important?

- Required by OMB and state guidance
- Risk assessments help each agency
 - Provide oversight for contracted federal and state funds for all administered programs
 - Identify the program/fiscal areas that represent the most risk/chance of errors
 - Identify potential “red flags” or serious problems on a timely basis
 - identify and arrange for subsequent technical assistance required by Contractors/Sub-grantees
 - Prioritize efforts and “target” scarce staff resources



Risk Assessments

When should the review(s) be done?

- During procurement phase for competitive procurements
- During pre-award phase for non-compete agreements
- Before execution of contract/award
- Post-award on a periodic basis



Financial Statements

Where do I find the data I need?

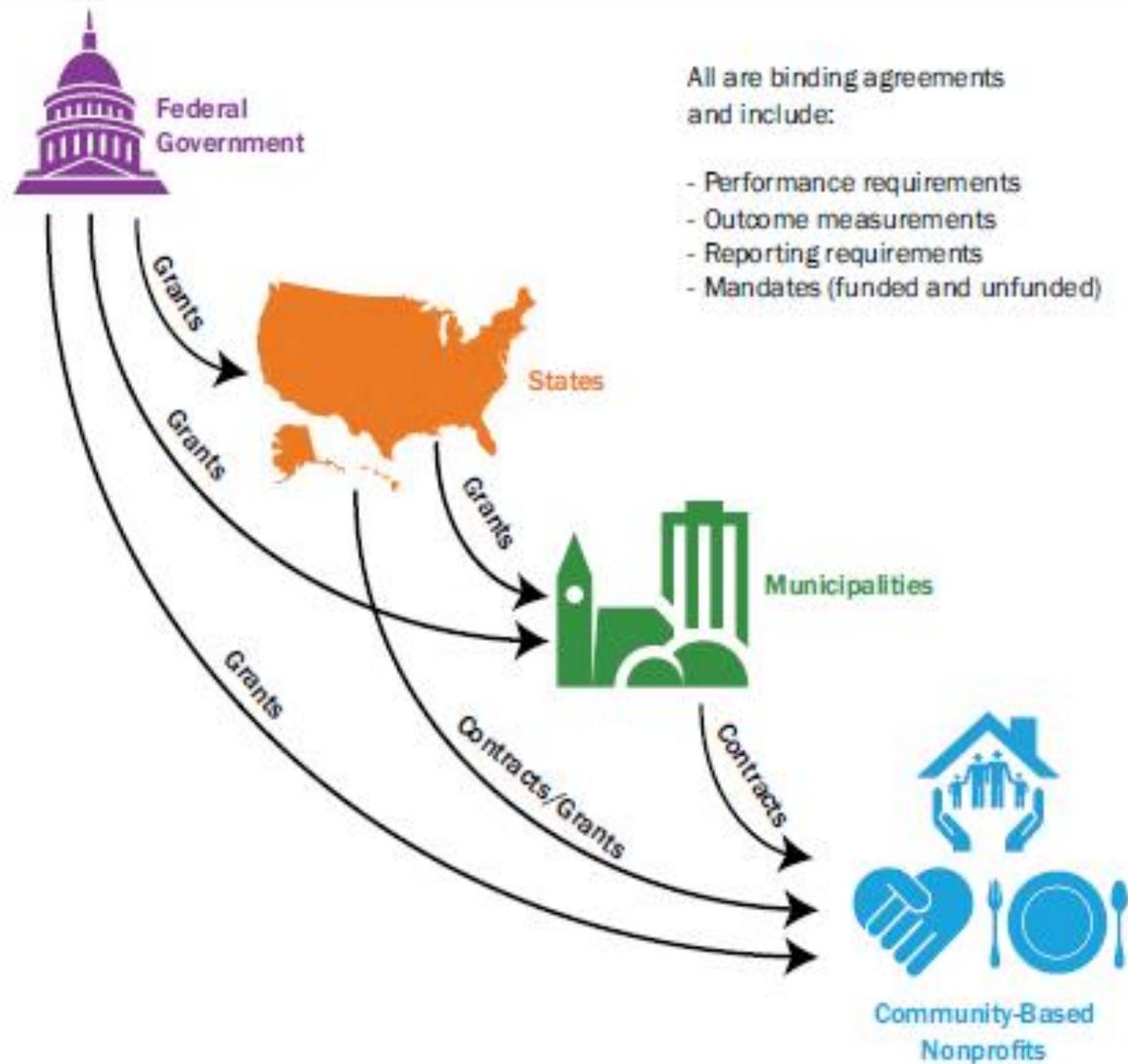
How do I search for the data I need?

How do I judge the data I find?

- Requested from/submitted by each entity
- Criteria used or operating areas analyzed may vary slightly based on the agency and/or the individual contract or award
- Look for certain disclosures and/or perform analytic calculations
- Use a tool or other form to document your results
 - *See workshop handouts for specific examples*



Background – Federal Requirements



Source: FGC UG Guidance Updates, October 2015

Background – Federal Requirements

Public Laws

Passed by Congress and signed by President to become part of the United States Code.

Federal Regulations

From Federal Departments to implement the laws (programs) are found in the Code of Federal Regulations.

Uniform Guidance, 2 CFR Part 200

From the Office of Management and Budget is incorporated (codified) into administrative regulations from each Federal Department.

Specific Requirements

Applicable to a recipient would be incorporated into a grant condition.

Additional guidance from Federal agencies could be program instructions, information memorandums, technical assistance guides, etc.



Source: Wipfli Uniform Guidance Update, 2014

Background – Federal Requirements

Subpart C – Pre Award Requirements

§ 200.205 New framework for risk

Awarding agency review of risk posed by applicants



- Risk factors may include
 - Financial stability
 - Quality of management systems
 - History of performance
 - Reports and findings from audits
 - Ability to effectively implement requirements



Source: FGC UG Guidance Updates, October 2015

Background – Federal Requirements

Subpart D – Post Award Requirements

§ 200.331 Pass-through entity requirements

- Oversight and monitoring requirements

The pass-through entity must

- Consider operating factors for each sub-award to complete a **risk assessment** to determine appropriate level of sub-recipient monitoring
 - Risk of noncompliance
 - Sub-recipient’s prior experience with the award
 - Results of previous audits or federal monitoring
 - Whether the sub has new personnel or systems



Source: FGC UG Guidance Updates, October 2015

Background – Federal Requirements

Subpart D – Post Award Requirements

§ 200.331 the pass-through entity must

- Verify sub-recipients have audits as needed*
 - *Reminder - this is not the only monitoring task
- Consider actions required to address any instances of sub-recipient noncompliance
- Follow-up to ensure sub-recipient takes appropriate action on all deficiencies related to the sub-award identified through audits, onsite review or other monitoring tasks
- Issue a management decision for audit findings related to sub-award(s) made by the PTE



Source: FGC UG Guidance Updates, October 2015

Background – Federal Requirements

“Consider actions” may = Special conditions

Results may trigger special conditions for an award that includes, but is not limited to the following

- Require reimbursement
- Withhold funds until evidence of acceptable performance
- More detailed reporting
- Additional monitoring
- Require sub-grantee/sub-recipient to obtain technical or management assistance or
- Establish additional prior approvals



Background – State Requirements

CFO Memo No. 06 (2011-12)

Contract Monitoring and Documenting Contractor Performance

- Agencies must have a formal contract monitoring process that includes
 - Risk Assessment
 - Monitoring Plan
 - Monitoring Procedures and Criteria
 - Evidence to support results obtained
 - Corrective Action Plan (CAP), if required
 - Agency follow-up on CAP, if required



Risk Assessments

Recap of requirements

- Identify high-risk areas by considering
 - Stability (or lack) in entity's management
 - Efficiency (or lack) in controls and processes
 - Coverage (or gaps) in expected/actual results
 - Past history/experience
- Assign risk levels based on results
- Develop appropriate monitoring plan
 - *See workshop handouts for specific examples*



Risk Assessments

What's needed – the basics

Testing tasks/process – by entity/award

1. Determine/identify your agency's current criteria (aka risk factors)
2. Determine/identify any additional risk factors that may apply based on specific scoped tasks or other program requirements
3. Ensure the entity's data can be reviewed/tested to provide results for all the listed risk factors
4. Request/obtain entity data* (*before award is issued*)



Risk Assessments

What's needed – the basics (cont'd)

Testing tasks/process – by entity/award

5. Review entity data to evaluate against your agency's current criteria (aka risk factors)
6. Compile all risk factor answers to calculate one combined score
7. Repeat process for all contract/awards
 - Individual scores will help evaluate all agency activities and current levels of risk
 - Data can be used to “target” staff resources and tasks
 - See workshop handouts for specific examples



Risk Assessments

Risk Assessment Factors

- Dollar size
 - Age and complexity of activity
 - Nature of recipients
 - Operating model for entity (centralized or not)
 - Human capital
 - Historical data
 - Quality of fiscal/payment controls
 - Quality of monitoring/oversight controls
- *See workshop handouts for specific examples*



Risk Assessments

What could a low-risk entity look like?

- No significant Single Audit or agency-specific site visit findings (no major questioned costs)
- Responsive to agency staff inquiries
- Timely submission of reports that are complete and have no errors
- Spends all awarded funds on allowable activities
- Does not have to de-obligate or return a high amount of awarded funds (more than 10%)
 - See workshop handouts for specific examples



Risk Assessments

What could a medium risk entity look like?

- No *significant* Single Audit or agency-specific site visit findings (no major questioned costs)
- Generally responsive to agency staff inquiries
- Timely submission of reports that are mostly complete and have few/minor errors
- Spends all awarded funds on allowable activities
- Does not consistently de-obligate or return a high amount of awarded funds (less than 15%)
 - *See workshop handouts for specific examples*



Risk Assessments

What could a high risk entity look like?

- *Significant* Single Audit or agency-specific site visit findings (material weakness(es) and/or major questioned costs)
- Generally not responsive to agency staff inquiries
- Delayed submissions of reports that are not complete and with multiple errors
- Spends awarded funds on unallowable activities
- Consistently de-obligates or return a high amount of awarded funds (over 20%)
 - *See workshop handouts for specific examples*



Risk Assessments

Closing thoughts

- Be sure to understand processes already in place for your agency
 - Make sure your processes align
 - Ask questions or get help if you don't know
- Missing files/forms also tell you about risk
- Remember
 - There is no “one size fits all” for testing risks
 - Document your review results



Open Forum - Q&A



Contact us with your questions

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