

UNC SCHOOL OF GOVERNMENT

**AMERICAN  
RESCUE PLAN**

# Budgeting, Accounting, Financial Reporting, and Auditing and ARP

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## Key Fiscal Topics Related to ARP

- Budgeting
  - When does a budget have to be adopted?
  - What type of budget should be adopted?
- Accounting
  - What fund(s) may be used?
  - How do we record receipts and disbursements?
- Financial Reporting
  - How are the basic financial statements impacted?
- Auditing ARP funds

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## Budgeting

- Budgets do not have to be in place for the *receipt* of funds, but they must be in place before any disbursements may occur
- Local governments should adopt a grant project ordinance to cover the *life* of the grant resources
  - Statutes allow special revenue funds to adopt grant project ordinances
  - Segregates funds for budgeting, accounting, and reporting purposes
  - Provides an audit trail that is critical to facilitate Treasury reporting requirements
  - Budget authorization automatically carries forward into new budget years

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## Budgeting (cont.)

- All ARP funds should “flow through” a special revenue fund, regardless of their intended use
  - Once use of funds is decided, the monies may then be transferred to the appropriate fund
    - General, capital projects, and/or enterprise funds
    - Interfund transfers must be budgeted
    - The “expending” fund must also have a budget
- Funds being used solely for revenue replacement (standard allowance option) should first be accounted for in a special revenue fund and then transferred to the general fund

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## Accounting

- ARP funds are initially recorded as unearned revenue (a liability) until the governing board officially determines the use(s)
  - Unearned revenue vs. revenue classification is more of a reporting issue at fiscal year end
- Once use is determined, revenue will be recognized (would initially occur in the special revenue fund)

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## External Financial Reporting Implications

- In most cases, the ARP special revenue fund will qualify as a major fund
  - Even if is below the threshold, it would be recommended that the fund be elevated to major fund status
- Major fund reporting requires a separate column on the governmental funds' balance sheet and operating statement
- Would not be included on budget to actual in basic statements because it is a multi-year budget

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## Reporting Implications (cont.)

- Capital assets procured with ARP monies either directly from the special revenue fund, capital project fund, or general fund would only be reported at the government-wide level
  - Considered capital outlay in the fund statements
- Capital assets procured in an enterprise fund capital project fund would be reported directly in that fund

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## Reporting Implications (cont.)

- Effect of ARP monies transferred to enterprise fund for capital project on GAAP statements
  - Transfer in on the operating statement
  - Cash flows from capital and related financing activities on the statement of cash flows
- ARP monies considered restricted cash and investments on the government-wide statement of net position
- ARP monies considered program revenue (operating grants and contributions) of governmental activities on the statement of activities (government-wide level)

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## Using Standard Allowance Option for Revenue Replacement

- Entry for the ARP special revenue fund

Transfer out – general fund (revenue replacement)	\$650,000	
Cash		\$650,000

*Note: The SRF project ordinance gives the budgetary authority for the transfer through the identification of the revenues being replaced.*

- Entry for the general fund

Cash	\$650,000	
Transfer in – ARP special revenue fund (revenue replacement)		\$650,000

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## Purchase of a Fire Truck Directly from the ARP Special Revenue Fund

- Entry in the ARP special revenue fund

Capital outlay	\$1,300,000	
Cash		\$ 1,300,000

*Note: The fire truck would be reported as a capital asset in the government-wide financial statements.*

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## Using ARP Funds for Water Fund Project

- Entry in the ARP special revenue fund

Transfer out - enterprise capital project fund	\$5,500,000	
Cash		\$5,500,000

- Entry in the enterprise capital project fund

Cash	\$5,500,000	
Transfer in - ARP special revenue fund		\$5,500,000

*Note: For GAAP reporting purposes, the enterprise fund project will be reported within the enterprise fund.*

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## Using ARP Funds for Partnership Project with a Nonprofit Organization

- Entry in the ARP special revenue fund

Low Income Utility Assistance Program expenditure	\$30,000	
Cash		\$30,000

*Note: The expenditure reflects a payment to the nonprofit entity to assist in funding the program. The expenditure is in compliance with both state law and ARP guidelines.*

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## Premium Pay Previously Paid from ARP Special Revenue Fund Reclassified to General Fund

- Entries in the ARP special revenue fund

Cash	\$150,000	
Premium pay expenditures		\$150,000
Transfer out - general fund	\$150,000	
Cash		\$150,000

- Entries in the general fund

Cash	\$150,000	
Transfer in - ARP special revenue fund		\$150,000
Law enforcement premium pay expenditures	\$150,000	
Cash		\$150,000

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# Procurement of Audit Services and Other Audit-Related ARPA Challenges

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## PROCUREMENT OF AUDIT SERVICES

- **UNITS MUST** follow the procurement requirements for audit services as detailed in [§§ 200.317](#) through [200.327](#) of [subpart D of 2 CFR Part 200](#)
- Supersedes NC law regarding procurement of audit services
  - Current statutes do not require units to go through a competitive process to procure audit services in NC although it is a best practice

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## PROCUREMENT OF AUDIT SERVICES

- Units should follow most restrictive rule
- Audit services procurement requirements under UG are more restrictive than requirements in NC
- What does all this mean?
- Several steps to follow to determine what unit must do when procuring audit services

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## PROCUREMENT OF AUDIT SERVICES

Three levels of procurement requirements based on audit fee \$\$\$

- Micro-purchase threshold (MPT) - \$10,000 with some possibility to raise to \$50,000 on a unit by unit basis
- Above the MPT and below the Simplified Acquisition Threshold (SAT) – above \$10,000 but less than \$250,000
- Above the SAT of \$250,000

Virtually all local units in NC with a federal single audit will be charged a fee that falls above the micro-purchase threshold (MPT) and below the established simplified acquisition threshold (SAT)

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## PROCUREMENT OF AUDIT SERVICES

Raising the micro-purchase threshold

- 2020 revisions to the UG allow non-federal entities to set their own MPTs up to \$50,000 if certain requirements are met (scope goes beyond just audit fees)
- If unit qualifies as a low-risk auditee according to the criteria in [2 CFR 200.520](#)
- If unit completes an annual internal institutional risk assessment to identify, mitigate, and manage financial risks
- Evaluation/assessment must take place annually
- SOG Blog post: <https://canons.sog.unc.edu/2021/04/raising-the-federal-micro-purchase-threshold-self-certification-for-units-of-local-government-in-north-carolina/>

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## PROCUREMENT OF AUDIT SERVICES

Regardless of procurement threshold, several things locals **must do!**

- Make the objectives and scope of the audit clear to potential firms
- Request a copy of the auditor's peer review report
- Make affirmative efforts identified in [2 C.F.R. § 200.321\(b\)](#) to utilize small businesses, minority-owned firms, and women's business enterprises ("MWBE") to conduct the audit.
  - May contact MWBE firms directly, place these businesses on solicitation lists, and directly solicit a firm's involvement whenever it is a potential service provider. For assistance locating MWBE firms, contact the [NC HUB Office](#)

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## PROCUREMENT OF AUDIT SERVICES

- Units must follow evaluation factors and **document the process**:
  - The firms' responsiveness to the unit's requirements for audit services—including meeting the technical proposal instructions and addressing the technical evaluation criteria
  - The relevant experience of the firm or individual(s) involved
  - The availability of qualified staff to conduct the audit
  - The results of peer and external quality control reviews
  - Price
- **UNITS MUST DOCUMENT EVERYTHING!**

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## PROCUREMENT OF AUDIT SERVICES

When audit fee falls below the MPT

- Procurement is non-competitive in that unit is not required to get a certain number of proposals
- Still fall under requirements on previous two slides

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## PROCUREMENT OF AUDIT SERVICES

When audit fee falls between the MPT of \$10,000 and the SAT of \$250,000

- Must have a competitive process but full-blown RFP not required
- Can be a multi-year agreement
- Must follow previous requirements on evaluation and selection

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## PROCUREMENT OF AUDIT SERVICES

When the audit fee exceeds \$250,000

- Formal RFP process
- Includes publicization of the RFP
- Receipt of proposals from an “adequate number” of “qualified offerors” (2-3 proposals, at minimum, are recommended)
- Follow previous evaluation and documentation requirements in addition to the specifics as defined by the RFP

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## AUDIT CHALLENGES

### News from UST/OMB, April 8, 2022:

- If unit received funds directly from UST (not an NEU) and
- Unit received less than \$10 million in ARPA funds and
- ARPA expenditures are what is pushing unit into federal single audit category
- **Unit can use an “alternative audit approach” ... “intended to reduce the burden of a full Single Audit”**
- Attestation would result in an auditor’s opinion on compliance, which includes an assessment of two activities, specifically “activities allowed” and “unallowed/allowable cost.”
- <https://www.federalregister.gov/documents/2022/04/08/2022-07463/uniform-administrative-requirements-cost-principles-and-audit-requirements>

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## AUDIT CHALLENGES

### Overall compliance requirements for 2022:

- 2022 Compliance Supplement has been issued
- CSLFRF is considered “higher risk” pursuant to 2 CFR 200.519(c)(2)
- Units are required to comply with the Interim Final Rule until the Final Rule became available (4/1/2022). Units could choose to switch over to the Final Rule once it became available 1/27/2022
- Be sure to review the UST FAQs for additional information

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## AUDIT CHALLENGES

- Starting in 2022 or 2023, spending ARPA dollars will push many units into “different” audit categories than they are used to
- Category is based on **spending, not receipts**
  - Under \$100,000 spent in combined federal and state dollars, financial audit only
  - \$100,000 or more spent in **combined federal and state dollars**, financial audit plus a Yellow Book audit
  - \$500,000 or more spent in state dollars, financial audit, Yellow Book audit, and state single audit
  - \$750,000 or more spent in federal dollars, financial audit, Yellow Book audit, and federal single audit

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## AUDIT CHALLENGES

Examples:

- Town of Linusville received in the 2022 fiscal year the following state and federal funds
  - \$45,000 Powell Bill funds (state); added to their Powell Bill reserve of \$75,000
  - \$65,000 ARPA dollars as an NEU (federal)
  - \$775,000 grant award from DEQ funded by ARPA dollars (federal)
- Scenario 1 – Linusville **does not expend** any of these funds in 22 FY
  - Linusville will have a financial audit (GAAS) only
  - State and federal dollars expended = \$0

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## AUDIT CHALLENGES

- Scenario 2 – Linusville expends all of its Powell Bill funds, including its reserves, on street repairs, but expends no other state and federal funding during the year (\$45k + \$75k)
- Linusville will need a Yellow Book audit because it expended \$100,000 or more in combined state and federal grant funds
- Combined state and federal spending = \$120,000

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## AUDIT CHALLENGES

- **Scenario 3** – Linusville declares 100% of its ARPA funds to be revenue replacement funds under the standard allowance and moves all \$65,000 to the general fund to cover salaries and benefits in public safety. It also expends all of its Powell Bill funds, including reserves (\$120K total), and expends 100% of its DEQ grant of \$775k
- Linusville will need a federal single audit because it expended \$750,000 or more in federal dollars during the fiscal year
- Because the expenditure of ARPA dollars pushed Linusville over the \$750,000 single audit threshold, Linusville's auditor can take advantage of the alternative to a full-blown single audit

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## AUDIT CHALLENGES

- Scenario 3 (cont.)
- Linusville also will need a Yellow Book audit because combined federal and state funds expended exceeded \$100,000
- Total federal spending = \$840,000
- Total combined state and federal spending = \$960,000

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## AUDIT CHALLENGES

What is a Yellow Book audit?

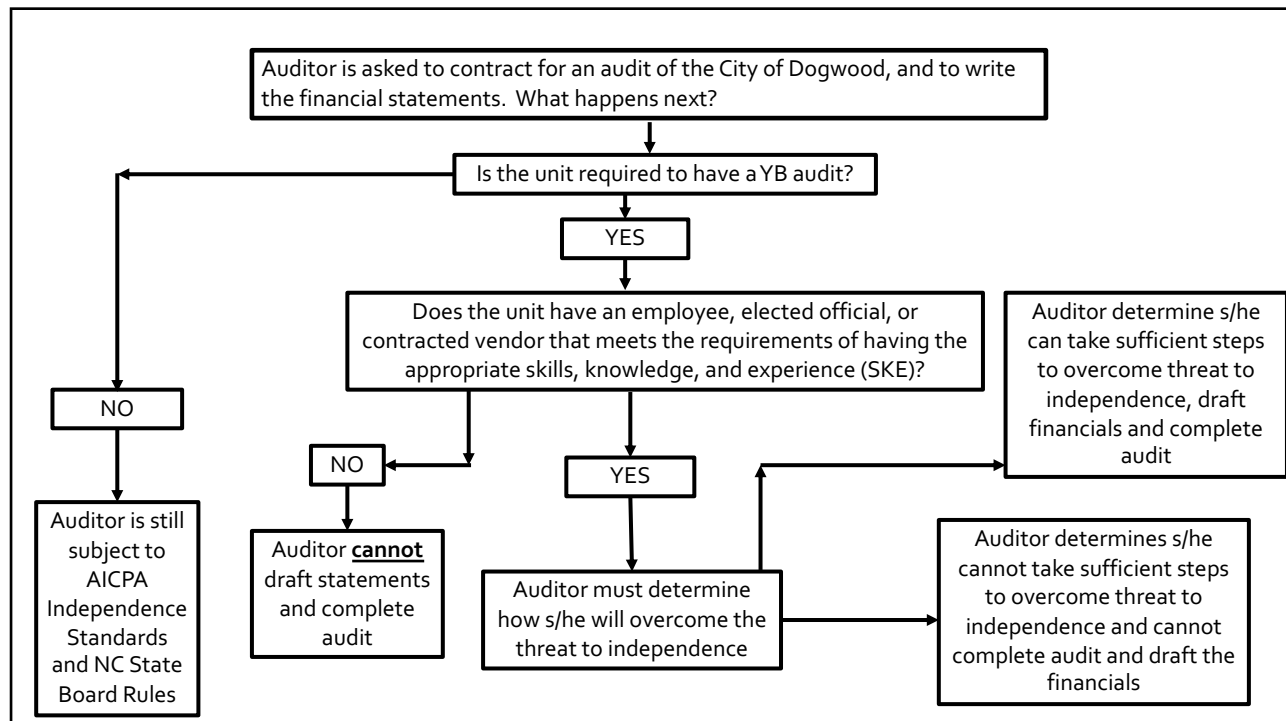
"The Yellow Book, formally the Generally Accepted Government Auditing Standards (GAGAS), is the name given to the standards promulgated by the Comptroller General (of the Government Accountability Office) for carrying out financial audits of government organizations or programs and business entities that receive financial assistance from the federal government.

- The Yellow Book provides standards for carrying out both financial and performance audits. Performance audits concern evaluating a program or project to determine whether it is meeting efficiency our [sic] outcome standards. The five standards contained in the manual include:
- Independence of the Auditor
- Due Care in Carrying Out the Audit
- Requirements for Continued Professional Education for Auditors
- Supervision of Auditors
- Quality Control Standards"

Source: [https://thebusinessprofessor.com/en\\_US/accounting-taxation-and-reporting-managerial-amp-financial-accounting-amp-reporting/yellow-book-auditing-standards-explained](https://thebusinessprofessor.com/en_US/accounting-taxation-and-reporting-managerial-amp-financial-accounting-amp-reporting/yellow-book-auditing-standards-explained)

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## AUDIT CHALLENGES

- Moving into Yellow Book category will present some challenges for small units that rely on independent auditor to write the financial report
- Significant changes to the Yellow Book standards that went into effect starting in FY 2019
- Make it more difficult if not impossible for independent auditor to draft the financial report

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## AUDIT CHALLENGES

**Preparation of draft financial statements in their entirety**, from a unit's trial balance or underlying accounting records, **creates significant threats to auditors' independence** that will require the application of safeguards to reduce the threats to an acceptable level (United States Government Accountability Office, Government Auditing Standards - 2018 Revision, p. 51) (emphasis added)

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## AUDIT CHALLENGES

- The auditor should determine that management of the unit of government has designated an individual who possesses suitable skill, knowledge, or experience (SKE) to sufficiently oversee the non-audit services
- Identified person does not have to have the SKE to perform or re-perform the services but must be able to have a sufficient understanding to oversee them
- The identified person must be able "to determine the reasonableness of the results of the non-audit services provided and to recognize a material error, omission, or misstatement in the results of the non-audit services provided." (2018 Yellow Book, 3.79)

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## AUDIT CHALLENGES

- Who can serve in the SKE role?
  - Can be a contracted vendor if unit is the contractor
  - The responsible person does not have to be the finance officer; can be another individual in the government
- The unit of government may wish to consider if the finance officer would benefit from additional training in the area or areas for which he or she does not have sufficient SKE to serve in that role.

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## AUDIT CHALLENGES

- Auditor must evaluate for SKE and must document that evaluation
  - Individual's work history, education, significant training courses

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## AUDIT CHALLENGES

- If the auditor determines that **no one at the unit has sufficient SKE** to oversee the non-audit services being provided by the auditor, then the **auditor cannot perform both the non-audit service and the audit**
- This issue should be discussed and resolved **before the audit contract is executed**

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## AUDIT CHALLENGES

- Once the SKE person has been determined, the auditor has limited options under which s/he can continue to serve as an independent auditor and draft the financial report
- This is not an exclusive list but gives you some idea of how difficult it is for the auditor to provide both audit and non-audit services

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## AUDIT CHALLENGES

Auditors can

- Not include individuals who provided the non-audit service as engagement team members
- Have another auditor, not associated with the engagement, review the engagement and non-audit work as appropriate
- Engage another audit organization to evaluate the results of the non-audit service
- Have another audit organization re-perform the non-audit service to the extent necessary to enable that other audit organization to take responsibility for the service.

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## AUDIT CHALLENGES

- What if the unit doesn't have anyone with the appropriate SKE?
  - Unit can hire a third party to serve in that role OR hire third party to write financials
- Can SKE person be an employee of the firm doing the audit if s/he is from a different team or group within the firm?
  - No
- If unit has a "lacks sufficient skills" finding in previous audits, does that automatically mean no one on staff has sufficient SKE?
  - Not exactly but definitely something to consider

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## AUDIT CHALLENGES

- Audit Contract includes language asking units and auditors to identify who is drafting the financials and who is serving in SKE role
- If audit is GAAS (financial) audit only, do not need to complete the SKE information

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## AUDIT CHALLENGES

What can units do now to plan ahead?

- Based on planned and/or historic spending, determine what type of audit you will have
- Talk with auditor now if you think you will need a Yellow Book audit and auditor has been preparing your financial statements
- If unit is not planning to expend ARPA dollars until 2023, talk with auditor as part of your 2022 audit to plan ahead for 2023; unit may need to hire a third party to draft financials

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