Final Transcript

HUD-US DEPT OF HOUSING & URBAN DEVELOPMENT: How to Read Financial Statements

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SPEAKERS

Robin Booth

PRESENTATION

Moderator Ladies and gentlemen, thank you for standing by. Welcome to the How to Read Financial Statements conference call. At this time your telephone lines are in a listen-only mode. [Operator instructions]. As a reminder, today's conference call is being recorded.

I'll now turn the conference over to your first speaker, Robin Booth. Please go ahead.

Robin Good afternoon and welcome to How to Read Financial Statements. As the moderator said, this call is being recorded, and it will be available on

HUD Exchange in the archive section, generally two to four business days after the webinar. It'll include the actual presentation, handouts and a transcript. So, if you want to refer to these materials, they will be available on archive.

As the moderator also said, the attending lines will be muted during this presentation, and the handouts for this presentation—you should have received them in advance if you registered. If not, if you look in your control panel for this webinar, you should see a PDF file and if you click on that document, it will download these materials for this webinar.

Approximately 24 to 48 hours, you will receive a thank you email indicating this is your certificate of training. This is the only certificate you'll receive there. It's not an attachment. The email itself is your certificate, so please make sure you keep that for your records.

There are multiple ways to ask questions throughout the presentation. I think based on the number of participants and thankfully, this material isn't as in depth as some other webinars. We will be able to take live questions throughout the presentation. I'll stop probably two to three times and ask if there are any live questions. If in fact you would like to ask a live question, just hit star zero. You'll be placed in the queue, and when I ask if there are any questions, the moderator will release your line so you can ask a live question. We do ask that when does occur, please make sure that you keep your phones on mute, because we may in fact hear background noise.

Another way to ask a question is we have live staff available on the webinar. In your control panel, if you go to your chat box, you can actually ask a live question. Stelba Strauther [ph] from our company will be answering those questions. If he cannot answer the question, then we'll let you know that we'll get back to you or ask you to send that question to the HUD email address which we will provide, or we may at those points where I stop and ask if there are any live questions, allow you that opportunity to ask your question.

Finally, if subsequent to this webinar, you realize you have additional questions, you can always send them to housing.counseling@hud.gov and we ask that you please put the name of this webinar, How to Read Financial Statements, in the subject line, so that it'll make it easy for HUD to actually distribute and to make sure the correct people get the question for a response.

At the completion of the webinar, you will get a brief survey. We ask that you please complete these surveys, because we use this information to plan future webinars to evaluate if the webinars are meeting your needs and expectations and hopefully to provide you with better webinars in the future. Please take a minute and complete that brief survey, and we appreciate the time you take to do that.

Onto the webinar. I've said this several times with the latest webinar, this is actually very timely, how to read financial statements. I know most of these participants on the call are either intermediaries, MSOs, State Housing Finance Authorities and/or HUD POCs who have the responsibility of reviewing financial statements to determine if an agency, a sub-recipient has the financial capability to perform on a grant.

Recognizing that you're not doing an in-depth analysis, and so to a certain extent, when they submit audit to financial statements as they're required to do, you rely on what's in those audits to give you a basis for determining the financial capability of the grantee to perform, but it is important to understand the basic types of financial statements, to be able to identify and recognize potential negative indicators or trends, even to use it as a basis to ask questions of the agencies for clarification.

Hopefully one of the goals from this webinar is that you have a better understanding and that you can use this as a resource to refer back to these materials as you're going through reviewing, especially during this grant execution time period where a lot of grants are being awarded now. As I said, this is timely.

I am Robin Booth. I am the audit principal for Booth Management Consulting. Our firm is a quality control and technical audit assistance contractor for the Office of Housing and Counseling. Most of you, or some of you may have interacted with us for action plans, or technical assistance, financial and administrative reviews and training. So, a lot of the materials we discuss here in this webinar, we also discuss via technical assistance and other ways throughout the contract.

What I hope you get out of this is one, recognizing that there are different levels of financial reporting from an external basis, meaning from those issued by certified public accountants or just accountants. All things are not equal. All reports are not equal. For this grant, the requirement is to have audited financial statements, so if in fact the agency or the sub-recipient has not submitted an audited financial statement, we want you to understand what level of financial statement they are submitting.

We'll go over the different types of audit opinions that you should see—ones that are great and ones that are not so great, and potential findings. We'll also go over some key financial reports that you should pay attention to. A lot of times, especially with this single audits, there'll be 20, 30, 40 pages. A lot of that information is not really relevant or provides value for the typed of determination you need to make. So, part of this is to kind of help you to focus in on what key information you're looking for and what can sometimes be voluminous audits.

Then, we'll speak specifically to the single-audit requirements. Thankfully, under the uniform guidance, they increased the threshold for the dollars that have been claimed or reimbursed or expended to $750,000 from $500,000. That makes a lot of difference to a lot of agencies who now are not required to have single audits. I just want to make sure you are alerted to that so that you understand that effective now, because effective after the fiscal year ended June 30th 2017, those agencies that did not expend more than $750,000 on a federal award are no longer required to have a single audit. They may be between $500,000 and $750,000, but effective now, they're no longer required to have that single audit. You can very well have an agency that submitted audits for years that in their most recent submission for grant execution, they may not have included that.

Then, as I said, we'll have questions at the end, but we'll also allow questions throughout the process. The purpose, as I said, I want to give you an understanding. We're not trying to make everybody an accountant. I hope that this material has been summarized and narrowed down to give you key buzzwords and enough understanding to identify when maybe you need additional assistance or you need additional clarification.

Just go over some analytical discussion on the fundamentals of reviewing audit reports, some red flags, some things I want you to be able to easily identify to say okay, this is potentially an issue, and then, some indicators of financial performance, both good and bad, that's the purpose of this training.

Going over the levels of report, and actually, right now, our company is doing a lot of the grant execution analysis for both the HUD POCs and for some intermediaries and MSOs and SHFAs that have sub-recipients. As we're going through these packages, we're realizing that a lot of the smaller agencies actually don't have audited financial statements, so what you may receive is a reviewed financial statement as indicated on this slide or a compiled financial statement.

There is a different level of reporting for each. The grant is written, the NOFA as written requires an audited financial statement, which is actually the highest level and the most expensive, to be quite honest with you. This is when you have to be a certified public accountant. They issue an opinion on your financial statements of whether they're in compliance or in accordance with generally accepted accounting principles.

This financial statement is just speaking to whether the financial statements are presented consistent with generally accepted accounting principles. This is not looking at any specific grant. This is not in any way the single as in single audit report. That's a different level of reporting. That's supposedly the minimal for submission with the audit with these grants. However, we've seen and some of you have probably seen financial statements where they say we have reviewed the financial statements, and generally to determine the type of financial statement it is, you have to look at the actual accountant's report. The accountant's report is the only thing that the accountant owns. Everything else, the statement of support and revenue, the statement of financial position, those other statements are actually just based on information provided by the organizations that have been adjusted or corrected to properly reflect generally accepted accounting principles.

If somebody gives you a reviewed financial statement, understand, first of all, that that's not an audit. That means that they have not determined if in fact is in compliance with generally accepted accounting principles. They are not giving you an opinion or any form of assurance. They're giving you limited assurance that they didn't become aware of any material modifications. What does that mean? That means they have not done the same level of testing of transactions, or review of documentations that they do with an audit opinion. So, they can only give you a very limited assurance unlike an audit where they are giving you an actual opinion.

Now, the lowest level of reporting is a compilation, and the audit report will say that we have compiled the financial statement. All that is—and compilations do not have to be issued by a certified public accountant. It could be a bookkeeper. It could be—I've seen all kinds of what's called compilation report. This is the lowest level. There are no assurances. Pretty much, the accountant took what the client gave them and said that it looks to be pretty much right. There's no testing. There's no analytical procedures. Basically, they're relying totally on the representations of management. Needless to say, this is the least expensive, because there's no test. There's no real testing or procedure, so it's not as time consuming, because they're really not delving deep into the transactions of the organization.

If you get a compiled financial statement or a reviewed financial statement, you can't rely on it to the same degree that you did an audit opinion. One of the things that OHC has done to assist, especially intermediaries and MSOs and SHFAs in this situation is that if in fact you have a small organization, they really can't afford to get an audit, so they're giving you compiled or reviewed financial statements.

To ensure that you've met your requirements as far as due diligence and determining whether the agency is financially capable of performing on the grant, you can request through your HUD POC a financial analysis or financial capability assessment, and that's where our firm will actually do a financial capability assessment looking at the financial statements.

We'll run ratios, we'll ask some questions about their internal controls and be able to give you a report to say yes, we believe they're financially capable of performing on this grant or no, we don't, and these are the areas of concern that need to be addressed.

That is yet some assistance that OHC is making available to you, both to the HUD POC, if you noticed it in your grant execution or to the intermediaries, MSOs, SHFAs, that if in fact you have an agency and you've gone through and reviewed their financials, they didn't give you an audit, you're looking at the review and compilation and just don't have that comfort level, you can request that assessment. It usually takes five to seven business days depending on the cooperation of the grantee for us to get that information to you.

I know, I've spent a lot of time on this slide, but that's because this kind of drives the remaining slides. When we look at an audit, what you need to know is that we have five main opinions. A good opinion is unmodified. We call it unqualified, and you'll often see it phrased as clean. Actually in the audit report, they will tell you this is unqualified, we didn't become aware of, or there were no deviations or exceptions to generally accepted accounting principles.

Now, in a modified report, generally that is a qualified opinion, meaning you're not getting the highest opinion possible and with it, it will explain to you what the areas of concern are. For instance, the common thing for a modified opinion is that certain documentation wasn't available. They can't issue an opinion on it, because it wasn't available. They'll explain that their scope was limited due to inadequate or unavailable documentation or sufficient evidential matter to be able to issue an opinion. So, modified, you always know why it's modified and that means that there were some issues.

Now, a going concern—everything else after your modified gets worse and worse and worse—a going concern is a part of an opinion where the auditor is telling you that they have some concerns about this agency, the organization's ability to continue in existence. Needless to say, that's pretty serious, because they're suggesting that there's something in their financials. Maybe it's a certain event. They could be defaulted on a mortgage or defaulted on a loan, or they lost their largest grant or funding source, or you know, unfortunately there may have been embezzlement or some kind of criminal activity that has resulted in them losing a substantial amount of their liquid assets. Whatever it is—when it's a going concern, it tells you in the audit and we'll see in the opinions that follow on the slides. It tells you we have a concern about their ability to continue. So, that's a very serious type of qualification.

A disclaimer is saying that we did not get enough to even issue an opinion. What does that mean? Unlike a modified, where they pretty much had everything that they needed but there was some areas and there were certain elements missing, but not enough to suggest that we cannot give you an opinion on what we do have, a disclaimer is basically saying we didn't get anything sufficient to be able to issue any kind of opinion on whether these financial statements conform with generally accepted accounting principles.

So, needless to say, that's not good. That usually suggests that there's inadequate documentation or they may not have maintained an accounting system or general ledger system that allows them to drill down to the details necessary to issue an opinion, or they may not have personnel there knowledgeable enough to be able to provide them with the information in order for them to issue an opinion. So, there's a lot of reasons to disclaim. Basically, we're saying we can't touch it. We don't have enough information to do it.

By far, an adverse opinion is the worst. With adverse, we're saying you gave us everything, we did all our auditing and testing procedures and pretty much, it's the exact opposite. This does not conform to generally accepted accounting principles, and whenever there's an adverse of opinion, there's a litany—they always provide you with a litany of the reasons on why that opinion is adverse. So that's, by far, the worst opinion, because it's basically saying that you gave us everything and you are totally not in compliance with generally accepted accounting principles.

Very rarely will you see an adverse opinion, because to be honest with you, a lot of times, if an organization believes they'll get an adverse opinion, they won't move forward with the audit. Because HUD mandates it to the extent that there's not some kind of exception due to the cost associated with the audit or this is a small grant and this is the only federal award, so the cost benefit doesn't make sense, requiring an audit from larger organizations becomes really, really important.

When you have a clean report, it basically says the auditor's judgment that the company's financial records and statements are fairly and appropriately presented. This is the most common type. That's the language you want to see in an unqualified report.

Here's an example of a clean and unqualified report. It'll always tell you in the first paragraph what they've audited. In this instance, they've audited all of the financial statements for the organization, because you see things like statement of financial position. A lot of us are more familiar with the term balance sheet. Then, your statements of activities and functional expenses—that's synonymous to a profit and loss statement.

The first paragraph will always tell you what statements were audited and through what period. So, you'll see there the years indicated. Then, of course, they'll tell you that it was conducted in accordance with the generally accepted standards, so they tell you what the standards what the standards are for the audit.

Then, the most important paragraph is the third paragraph—in our opinion. The paragraph that begins with our opinion—and I say that because when you have a modified report, there'll be some paragraphs before you get to the paragraph above the signature that says in our opinion, but in our opinion, the financial statements referred to above present fairly in all material respects. That is the language you need to see to know it's a clean, unqualified report.

Now, modified—two main reasons, like I said, scope limitation, we didn't get enough information, or relevant information. The second is that there's some major departure from financial reporting where they're treating certain transactions or doing some kind of accounting that's not consistent with generally accepted accounting principles. So, it's resulted in either an action or a negligence on the part of the client being audited.

If we call it a departure from GAAP—GAAP being generally accepted accounting principles, but a lot of you are probably more familiar with it when you look on the private side of things that companies like WorldCom did. They got into problems because their accounting methods that they used were a substantial departure from generally how certain transactions should have been treated. They did that because it gave them a stronger and better financial position, but that's not a normal treatment for those kind of transactions. That's exactly what the second type of qualification is—those kinds of circumstances where you can call it creative. I call it crooked, but where there's certain accounting practices that are being done that are not consistent with generally accepted accounting principles.

A going concern, and an adverse opinion is a going concern. Generally, if you have an adverse opinion, you're going to have a going concern paragraph. That's where we basically say we're not sure if the company is going to remain in business, as I talked to you about.

If you get an audit, the going concern paragraph in an audit is always after the opinion paragraph. If you look at this sample report and you go to the most important paragraph, in our opinion, the financial statements referred to above present fairly in all material respects, the financial position—notice this organization is actually doing everything right as far as their compliance, well accounting in accordance with generally accepted accounting principles, but the company financial statements have been prepared assuming that the organization will continue as a going concern.

As discussed—and they'll tell you what note it is, because you can go read more why they're saying this—the organization has suffered recurring significant reductions in grant revenues and has a net deficiency in net assets, which is synonymous to a net loss that raised substantial doubt about its ability to continue as a going concern. If you see that paragraph, we strongly recommend that you talk back to that agency and ask them one, the nature of this concern. You're going to see it in the financial statements—that note that they refer to in that will explain to you what the issue is, but they need to be able to tell you what their corrective action plan is, what their mitigating plan is, provide some evidence that there is a strategic plan to address this issue, because what you don't to do is knowingly award grant dollars to an organization that may not be in existence to perform the services. So, that paragraph is very, very, very important.

A disclaimer—we may decide that one, lack of independence—independence is a huge issue. Independence is just like we need to be independent, meaning we have no relationship, no conflict, nothing that would impair our ability to issue an objective audit opinion. The scope limitations always refer to lack of documentation or we don't have available information. That whole going concern as we said, is a disclaimer, and then, just other things involving uncertainty, like a contingent liability. If the organization is being sued, and there's a strong probability that they will lose the lawsuit, and it could impact all of their assets, then that's a matter involving uncertainty an auditor will disclaim at that point.

The adverse is just that the companies are misrepresented, misstated and do not actually reflect. So, pretty much, nothing is right when you have an adverse opinion. As you all know, with the single audit report date, under OMB, they need to be completed nine months after the end of the audit period and that these auditors are required to submit them to the clearinghouse. It's the auditor's responsibility to get them to the clearinghouse nine months after the end of the audit period.

Just a reminder about the new uniform guidance, it's now $750,000 for expenditures, and I emphasize expenditures because even if an agency has a federal award and let's say the federal award is $750,000, but it's expended over two to three years, they won't be subject to single audits for each of those years unless they expend more than $750,000. So, it's the actual amount that you expend that determines that threshold.

I said this while we were reviewing the statements, but just to give you a crosswalk, because some of us are more familiar with the for profit terminology. A statement of financial position—that's a balance sheet.

That's where most of us are used to seeing a balance sheet. Nationally, most of the time, the agencies, when they're not submitting the audited financial statements, let's say they're giving you compiled financial statements or reviews, a lot of times they don't use the proper names for the financial statements that are required from generally accepted accounting principles for non-profit organizations. That's yet another hint that maybe the financial weren't prepared by—you know, may not be able to be relied on if they're not even using the correct names required under GAAP for the actual statement.

The statement of activity is the income statement. The statement of cash flow, both of those statements, they are named the same. Then, the statement of functional expense is yet again, an income statement. What happens is generally for non-profit financial statements, they provide you with the functional activities and all of the expenses from the functional activity. So, you'll have a statement of revenue and support, and that'll have like a summary, and then you'll have the statement of functional expenses, which will then take each program area and provide you with the expenses by program area that roll up to the total expenses.

Just so you'll know, on the statement of financial position, you're looking at assets, liabilities and net assets. Now, I talk about the ratio of current assets to current liabilities and then current portion of long-term debt. When you're doing or looking at financial statements for these agencies, you want to look at their current assets to current liabilities ratio, and pretty much you're just taking the current assets divided by the current liabilities. Ideally, you want that to be a two-to-one ratio where they have twice as many assets as they have liabilities.

The worst case scenario is if the liabilities are greater than the assets. Then, there's potentially an issue of solvency suggesting that maybe they can't pay their liabilities as they become due based on the assets that they have. It's a lot to learn, and not attempting to try to make everyone into an accountant, but just so you'll know, you want to look at those.

You always want to look at assets and always want to look at liabilities even if just from a snapshot. If you look and see that the liabilities are great, especially the current liabilities and current assets, the liabilities exceed the current assets, you know that's a problem, because as I said, that means that they owe more than they're anticipating receiving. That should suggest that they will not have the ability to meet their obligations as they become due.

Statement of activities—unlike in the private sector where if you have a net loss, it's always a bad thing, that may not be true for non-profits, because one, generally a lot of times, they may be carrying over assets from prior periods. Or it might be non-cash transactions, things like depreciation, if they've written off a receivable or grants receivable that they thought they were going to get, but then they're not going to get. It's not like it's impacting their cash, but they still have to treat it as an expense.

You want to look at large fluctuations, especially decreases in support and revenue. If you see that generally financial statements, especially audits, are issued for two years at one time, and that's for comparability purposes. If you see that their revenue and support's going down, it doesn't hurt to send them an email and ask them a question—you know, what happened? Did you lose a grant? What's your plan or how do expect to recover? Now, of course, I'm going to balance that with, and this is where professional judgment comes in, if they're a larger or especially SHFA, those kinds of fluctuations won't concern you as much.

If it's a local housing authority, and they got support of $80,000 of revenue and then, the next year, they get $20,000, you're going to ask them that question. As I said, if it's an SHFA or even MSO, you may not ask that question based on fluctuations, and you have to keep that in mind when you're reviewing financial statements. The size of the organization and the type of organization is important. A lot of what I'm really discussing is more concerned with the smaller agencies with limited resources or who rely heavily on HUD grants to be able to run their programs and to run their organization.

You want to look at the leveraging fund from non-governmental sources. I just was going over a financial statement today, and I noted that the HUD grant was 80% of their total support. So, I'm looking for the leverage funds, because at this point, when you look at what their expenditures are and their expenses, this HUD grant can't carry all of the expenses associated with it, even on their budget. So what you do is you look at what their financial statements said they did in the prior year and then you're looking at these budgets you have in front of you and trying to assess does it make sense. So, then that leads to a question of, okay, what other leverage resources do you have in place to ensure that you'll be able to operate this program as you projected to meet your expenses?

The biggest thing you need to know about cash flow is that if it's negative, it's a problem. What that statement tells you is what happened with cash. So, you want it to be a positive balance at the beginning of the cash and a positive balance at the end. That's your biggest concern with cash flow. You don't need to get into the different sources of cash flow—operating, investing and financing. For you, the focus is at the end of this statement, is it going to tell me I have cash or I don't have cash? You don't ever want to see a negative cash balance. That is totally a red flag.

When you're looking at functional expenses, you want to look at the ratio of programmatic, administrative and fundraising to the total. Remember I told you, you get a statement of functional expenses and they have all their programs laid out. Well, they're also going to have a G&A, and then they're going to have fundraising. So, you want to be sure that their fundraising and G&A are not exceeding to a certain extent their program resulting in them actually being overburdened or being too top-side heavy, especially in administrative.

If you note that for their functional programs, you see that each of the programs are pretty much carrying themselves, they're getting enough support to carry their expenses, but then you have this big group of administrative and fundraising, which is the top heavy part of it, you then question about one, what happens if one of those other programs no longer gets funded? They help to feed or hope to carry the administrative and the fundraising. Two, why is it so high? Is the organization very top-heavy?

As I said, keep in mind what type of organization you're reviewing. This is more of a concern with LHCAs, less of a concern with SHFAs and MSOs.

Financial disclosures are those things called notes to financial statements, and what they do is they try to help you understand the financial statements. That's the difference between getting audited or reviewed financial statements prepared by a CPA firm. They give you those disclosures. Another hint that you may be looking at compiled or internally generated financial statements is when there's no disclosures. Generally, if there's no disclosures, they have to tell you, if it's a CPA. If it's just a bookkeeper—I just saw one packet where they tried to suggest that these were reviewed financial statements, and just by looking at the report, just by looking at the names that they called it, I don't even know—it wasn't called a statement of financial position. I forgot what it was called. It should have been called a statement of financial position or at worse, a balance sheet. You could tell it was something that was internally generated and they had somebody trying to say they do a report on it.

Just look for if they have disclosures. If you want to read all of them, you can, but some key ones you want to see, and every disclosure will always have a title. It'll always say this one is about cash, or this is about property, plant and equipment, or this is about loans. It'll always have a title, and they're always behind the actual financial statement. That's all the narrative behind the financial statement. But if you want to read the ones about debt, if they have commitments or contingencies, you want to read that. If they have any kind of legal footnotes, you want to read those, and then, if they have a footnote called subsequent event, you want to read that, because they're the ones that'll tell you if there's something going on that you need to be concerned with.

The rest of them, or most of them are required disclosures under generally accepted accounting principles, and so they're just normal disclosures that don't provide a lot of value.

This is just a reminder that under OMB 133 through June 30, 2006, and for the years thereafter, we're going to look at the types of reports, where to look for findings and how to understand findings. This is another area that gets confused. Organizations can have general financial statements that are reporting whether you're in conformance of generally accepted accounting principles. That's your basic audited financial statement. The single audit generally is a part of those, but they're actually the financial statements that come after the general audited financial statements.

Sometimes agencies may just have had an audit. They didn't have a single audit. So their audit reports will not include these additional reports or internal controls and compliance. One of the ways you know if it's single audit is that it'll say that it has a report on internal control and a report on compliance. That's another clue to let you know what type of report you're looking at, and it's all consolidated into one report.

This one, report on internal controls—and a lot of times, this is the one that people will refer to. The auditors came out and they did a report on internal controls, so that should mean we're fine. The difference is that here, they're only looking at internal controls associated with the programs that met the threshold or that were selected for audit. For instance, in larger organizations, where they may have 20 to 30 federal awards that meet the single audit threshold, they may select two or three for auditing. The rest of them, they won't do any kind of procedures including internal control.

Yes, you can rely on the fact that they do internal controls over those programs suggested. What we recommend is that if there are any findings that you at least read them to see if maybe the findings might have an impact on your HUD grant. For instance, let's say that their finding had to do for a related party. It was determined that a related party was signing disbursements for another—and they shouldn't have been doing that. Well, if the same related party also was managing all of the programs, from an internal control perspective, that might be something that could impact your HUD grant even though it was not subject to this audit. That may be something you ask a question about just for clarity and make sure it's a part of your report for that.

The next one—internal report on compliance with requirements that could have a direct and material effect on each major program—major being those programs that meet the threshold. Once again, we get the response, oh, they've done a compliance audit, and so we should be fine. Once again, the response is unless the HUD grant was included in that audit, they didn't touch any of the HUD grant. They're only talking about those program areas that they looked at and specifically, that might have impacted major program areas. If it wasn't a major program area, it wasn't included in the sample.

Where will you see findings on your OMB report? There's a schedule of findings. You can flip right through this page. You go through the whole internal control report. You go through the compliance report, and soon thereafter, you're looking for this thing called schedule of findings and questioned costs. It is required; they're all going to look like this. They're going to answer yes and no as to whether they're findings. If this tells you, they're going to tell you. If you see at the bottom, they're going to tell which grants were included in this audit that they looked at where these findings were identified. So, that can be your cheat sheet. You don’t have to go read every page in that sometimes voluminous report. You can go look for the schedule to get the information.

This is another example—just a slight variation of the format. If you notice, this is a $300,000 grant, so this was not a major federal award, but they actually did include this grant, and they looked at it because of type A and type B programs. Maybe they included in their sample looking at type B programs which didn’t meet the threshold, but once again, you’re always going to have the schedule of findings and questioned costs. You can go and read and see what the issues are and determine what if any relationship they may have to your grant.

In this one, the issue duty should be segregated to provide reasonable assurance that transactions are handled appropriately. Okay, if there’s a lack of segregation of duties, there’s a strong probability that lack of segregation also impacted your grant. So, you just want to know what have they done. So, you see if there was a recommendation here and generally, they should have a corrective action plan. They should be able to give you a corrective action plan and tell you how they’ve addressed that, because although your grant wasn’t one of those grants that was included, something like this, with that kind of internal control deficiency, would be systemic. So, there's a high probability it would in fact affect your grant.

That's just giving you examples. Some of your common findings, always lack of segregation of duties. It's tough for smaller organizations and that's why you only get a single audit if they feel like you have major funding from a federal award, because it's really tough to have ideal or optimal segregation of duties if you're a one- or two-person organization. So, thankfully you're not subject to these audits.

Lack of ability to prepare a complete set of financials, as I said, a lot of times organizations aren't maintaining their accounting systems consistent with generally accepted accounting principles, so they can't even provide auditors with a whole set of financial statements. Auditors have to assist them or rebuild certain elements of their financial statements, especially things like equipment or materials, because nobody kept track of what we call an inventory of those things. Auditors, when they come in and do the audit, they sometimes have to do an inventory count and figure out those kinds of things and then make sure that they post the correct numbers to the financials, things of that nature.

Other findings might be questioned costs. The questioned costs is where there was something charged that either one, was not consistent with the cost principles in the uniform guidance, had inadequate documentation, or was not reasonable or necessary. So, there's a question about whether it was reasonable.

When that happens, then the entire cost will get questioned, and the agency could be subject to having to repay or give back those dollars for those costs. Repeat things. You'll see that whenever there's a finding, they'll indicate until that finding is closed and it doesn't get closed until somebody follows up. Generally, the auditor that performed that audit follows up to verify that whatever the finding was, was addressed. That usually happens in the next audit report. You'll see a prior finding, and you'll see whether it's been closed or not. If that hasn't been closed or it's a repeat finding and it comes ups again, that is an issue. They should be able to provide you with a corrective action plan.

The reason why I kept this so high-level and didn't get into number crunching is because you all are just trying to make a determination of financial capability to perform. If they're giving you an audit, for the most part, you can rely on that audit. It's when they give you reviewed or compiled financials where you may need to refer or request that they have a financial capability assessment so you can put in your file that you've done the due diligence to make sure that this sub-recipient or this agency does have the financial capability to perform.

As, I said, it's not for you to become an accountant and do financial analyses, and the whole bunch of benchmarks and ratios and things of that nature, but for you to have sufficient understanding of the financial statements to determine one, if you can accept what you have and move forward with the determination that they're financially capable to perform, or to determine that hey, I need somebody to dig deeper, do a deeper delve on this, and that may be when you request a financial capability assessment through your HUD POC, who would then request that a company come do that assessment for you.

I believe I see a hand. Are there any questions in the queue?

Moderator — We have no questions in queue at this time, but if I may take a moment to remind participants. [Operator instructions].

Robin — Okay. I noticed that, did you still need me to back to slide 13? I saw that comment, but then I saw that it was addressed. If there are no other questions—I was checking the questions in the queue. Just as a reminder—

Moderator — We do have a question from the phone lines.

Robin — Okay.

Moderator — That'll be from the line of Jennifer Smith. Please, go ahead.

Jennifer — Hi, Robin. How are you? This is Jennifer, one of the POCs with HUD. I've been working with Keisha and Phyllis on reviewing the financial statements. My question is some of the grantees don't think that they have to provide anything if they don't expend less than $750,000. So, can you really tell me what it is that they are supposed to provide? Is this a financial statement? I'm just not clear about what they are supposed to provide, because I've had that question come up several times.

Robin — I'm assuming these are agencies that don't have grant awards, like they're not applying for the grant.

Jennifer No. These are like smaller agencies that received maybe not that much from HUD, but they still should be providing us with some type of financial statement. Correct?

Robin Yes.

Jennifer I just need to be clear about that they should be providing to us even if they did not expend over the $750,000.

Robin First of all, the $750,000 is just a threshold for when you need an additional audit report. Anyone receiving a federal award, should be able to provide a financial statement. That's a part of the financial management requirement. I think it's section 200.213 of the uniform guidance that says they have to maintain a financial management system to be able to report their financial activity. That's where the requirement comes from—the uniform guidance—that you have to a financial management system. It's the same one that you all require them to have in the grant execution process.

Remember they have to do that certification? I certify that I have a financial management system in compliance of 2 CFR part 200, whatever, that's what they're saying. So, when you're asking them to generate from their financial management statement, at a minimum, and I say that because a lot of times they'll have off the shelf accounting systems, QuickBooks and other things like that. So, they're not going to have the appropriate financial statement name. So, it's not going to say statement of support and revenue. It's going to say profit and loss statement and a balance sheet.

At a minimum, they should be able to from their accounting system—you know, I didn't say go to a CPA—but from just their accounting system, provide you with a balance sheet and profit and loss statement.

Jennifer Okay, that's good.

Robin Yes, and that's where you get the leverage to tell them why they have to have it. They certify they're going to have that financial management system.

Okay, so did that answer your question, Jennifer?

Jennifer Yes, you said generate a profit and loss statement and what was the other one?

Robin A balance sheet.

Jennifer A balance sheet.

Robin Yes, from their internal statement, at a minimum. They should be able to do that.

Jennifer Okay, got it. Thank you so much.

Robin You're welcome. Any other questions?

Moderator We have no one else in queue from the telephone lines.

Robin Okay, so if you have a question later, you always have the option to send it to housing.counseling@hud.gov with How to Read Financial Statements in the subject line item, and Ginger and her team will make sure that they're distributed so that we can respond accordingly.

If not, everyone please be safe, especially those in the South and hopefully everyone weathered whatever storms if you were involved, but be safe and you have a great afternoon.

Moderator: Ladies and gentlemen, that will conclude your conference call for today. Thank you for your participation and for using AT&T's Executive Teleconference Service. You may now disconnect.