

## Internal Controls and Procurement Update

Tennessee Association of Community Action

May 1, 2018

Workshop Leader: **Kay Sohl**



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## How has the Uniform Guidance changed your life?

- Easier?
- Harder?
- More confusing?
- More joyful?

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## Workshop Focus: UG Requirements for

- **Internal controls:** COSO or other framework
- **Written procurement policies & procedures**

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**No More Suspense!**

- **Procurement Deferral Ending**
- **FY beginning after 12/14/17**
- **For June 30<sup>th</sup> year ends – must have compliant policies & procedures in effect 7/1/18**

Per Federal Notice 82FR22609 published 5/7/17

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**But First...**

- **New way to think about (and streamline) Internal Controls**
- **UG and CAA Org Standards agree:**  
**It's all about RISK!**

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**Standard 4.6**

**An organization-wide, comprehensive risk assessment has been completed within the past 2 years and reported to the governing board.**

[http://cap.iescentral.com/filelibrary/oscoe\\_developed\\_standards\\_seperated.pdf](http://cap.iescentral.com/filelibrary/oscoe_developed_standards_seperated.pdf)

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**Your CAA's  
Most Significant Risks?**

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**CAA World of Risks**

- Financial Management
- Compliance
- Personnel
- Sustainability
- Service delivery
- Reputation
- Governance
- Technology
- Environmental
- Facilities
- Transportation
- ???

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Community Action Partnership  
**Risk Assessment Toolkit**

- <http://portal.nonprofitrisk.org/CAP/>
- Assessment Tools
- Risk Management Policy Templates
- Joint project with the Nonprofit Risk Management Center

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### Internal Controls

- **Systems, policies & policies** designed to prevent and detect errors and irregularities
- **Control environment:** organization wide expectations around integrity & compliance
- **Designed to manage risk**

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### Internal Controls designed to:

- **Reduce the risk** of improper actions
- Increase the likelihood that errors or wrong acts will be **detected**
- Reduce the risk that error will go **uncorrected**

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### Reality

- No perfect controls
- Controls provide **reasonable assurance**, not absolute assurance
- **Cost/benefit analysis** essential in designing, implementing, & monitoring controls

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### §200.303 Internal Controls

- Recipients or sub-recipients **must** establish **effective internal controls** over Federal awards
- **Should** use **COSO** or other comprehensive **framework for internal controls** such as Green Book

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### COSO Integrated Framework for Internal Controls

- Originally issued **1992**
- **Updated** version **May 2013**
- **Enterprise Risk Management Framework - 2017**
- <https://www.coso.org/Documents/990025P-Executive-Summary-final-may20.pdf>

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### COSO

- **Committee of Sponsoring Organizations:**

American Accounting Association  
American Institute of CPAs  
Financial Executives International  
IMA- Assoc. of Accountants & Financial Professionals in Business  
Institute of Internal Auditors

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### Use COSO Framework to

- Identify & address **risk**
- Develop **cost effective approach** to controls
- **Document** system of controls
- **Reduce** audit cost
- **Avoid** audit findings

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### COSO Framework



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### COSO Framework

1. Control environment
2. Risk assessment
3. Control activities
4. Information sharing & communication
5. Monitoring

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### **COSO Principles for the Control Environment**

- CAA commitment to integrity & ethical **values**
- **Board** is independent of management & exercises **oversight** over controls
- Management establishes effective **structures** for authority & responsibility for controls
- CAA demonstrates commitment to attract, develop, and retain **competent staff**
- CAA holds individuals **accountable** for controls

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### **Board Establishes Control Environment**

- Hires & evaluates CEO
- Establishes/reviews CEO compensation
- Participates actively in needs assessment & priority setting
- Reviews monthly financial statements
- Selects auditor & communicates with auditor without staff present

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### **Control Environment Board Role - continued**

#### **Set policies:**

- Conflict of interest
- Whistleblower
- Investment
- Annual audit
- Risk management

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*Control Environment:*  
**CEO & Management Roles**

- Identification of high risk areas
- Prioritize resources to fiscal and program management
- Analyze financial statements
- Clear delegation of authority/responsibility for compliance

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**COSO Framework**

1. Control environment
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**Risk Assessment ???**

- Materiality of exposure – \$\$\$ at risk
- Ease of misappropriation or misstatement
- Likelihood of occurrence
- Likelihood of discovery

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### Prioritization of Risk

High		
Impact	<b>Medium Risk</b> <i>Transfer Risk</i>	<b>High Risk</b> <i>Actively Control</i>
	<b>Low Risk</b> <i>Accept</i>	<b>Medium Risk</b> <i>Accept some level of risk</i>
Low	Probability	High

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### Risk Dimensions

- Financial Reporting
- Operations
- Compliance

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### 3 Kinds of Fraud

- **Misappropriation:** improper taking or use of assets
- **Misstatement:** reported assertions are false or misleading
- **Corruption:** decisions contrary to the best interest of entity

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### CAA Misappropriation Fraud Risks:

- **Phantom** employee or vendor
- **Payroll & benefits** manipulation
- **Expense reimbursement**
- **Misuse of CAA credit cards or accounts**
- **Misuse** of equipment

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### Misstatement Risks

- **Reports to funders**
  - Inaccurate financial info
  - Inaccurate assertion of compliance
- **Board financial reports**
- **Payroll tax reporting**

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### COSO Framework

1. **Control environment**
2. **Risk assessment**
3. **Control activities**
4. **Information sharing & communication**
5. **Monitoring**

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*Control Activities*

**High Level Controls:**

- Top level **review** of **accomplishments**
- **Comparison of actual to planned**, both \$\$\$ & activities
- HR management to employ **competent, high integrity staff**
- Info processing controls

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*Control Activities*

**Operational Controls**

- Physical control of assets
- Segregation of duties
- Proper execution of transactions
- Accurate/timely recording
- Access restrictions & accountability
- Documentation of transactions & controls

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*Control Activities:*

**Compliance Controls**

- Identification of compliance requirements
- Personal activity reporting to substantiate personnel related charges
- Sub-recipient monitoring
- Procurement
- Cash Management

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*Control Activities:*  
**Key Compliance Controls** -continued

- Determining allowability<sup>ksf</sup> of costs – including allocated costs
- Facilities & equipment controls

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**COSO Framework**

1. Control environment
2. Risk assessment
3. Control activities
4. Information & effective communication
5. Monitoring

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*Info & Communications*  
**Key Elements**

- Expectations, policies, procedures communicated clearly throughout organization
- Relevant, reliable, & timely access to programmatic & financial info for managers???

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**Slide 34**

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**ks1**      kaysohl, 4/16/2018

*Monitoring:*

### Identifying Control Breakdowns

- **Responsibility** for periodic testing of compliance clearly assigned with adequate time available for timely testing
- **Responsibility** for follow-up on prior findings clearly assigned with realistic timeline for resolution

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### Audit Internal Control Findings

- **Significant Deficiency**
- **Material Weakness**

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### Top CAA Control Risks

- **Compliance** breakdown
- Failure to **identify & communicate** compliance requirements
- **Training & supervision** glitches
- **Lack of time** for review & testing of financial & program data
- **Cost allocation** implementation problems

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### More CAA Control Risks:

- **Inadequate or outdated documentation** of control systems, policies, procedures
- **Control of assets** purchased with federal \$\$\$:
  - Equipment
  - Inventory

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### Reduce Likelihood of Findings

- **Improve control environment**
- **Identify compliance requirements**
- **Streamline controls**
- **Improve internal communication**
- **Internal testing** of financial & program compliance

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### Rethinking Controls

- **Document Major Processes**
  - Revenue & expense cycles
  - Payroll cycle
  - Contract management cycle
  - GL closing & reporting cycle
  - Budget cycle

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**Tools for Documentation**

- Flow charts
- Process level matrix
- Narratives

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**Identify Purpose of Control Procedures**

- Prevent error
- Detect error
- Establish accountability
- Deter fraud
- Document compliance

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**Opportunities to Streamline Controls**

- **Eliminate duplicative controls-**  
Multiple steps designed to achieve same purpose
- **Complete or eliminate incomplete controls**  
Records maintained for comparison, but no comparison made  
Authorization required but not reviewed

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### Common Ineffective Controls

- **Check-logs** never compared to GL or bank records
- **Purchase Orders** not systematically recorded, matched, investigated
- **Un-reconciled systems** for tracking accrual and use of sick & vacation time
- **Check signature requirements**

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### Procurement Update

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### Uniform Guidance §200.320 Requires

**Written policies and procedures** for purchasing goods and services with federal funds

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**Grace Period Ends  
for FY beginning after 12/26/17**

- OMB had allowed delaying implementation of **UG procurement requirements** for up to **3 years**
- During the **delay period**, CAAs required to **document** whether you are in compliance with **new or old policies & procedures** for procurement

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**CAAs with June 30th FY**

- Must adopt and implement **Procurement Policies and Procedures** required by Uniform Guidance no later than **7/1/18**
- If you previously deferred adoption, must have **documentation of your decision to defer implementation**

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**Procurement Basics**

- **Procurement** describes the policies & processes used to **purchase goods & services**
- Must **establish & follow your own** procurement policies & procedures
- Your policies & procedures must **conform to Federal standards**

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### Key Distinction

- **Procurement** Rules apply to Contactor/Vendor Agreements
- **Sub-recipient** Rules apply to agreements with sub-recipients
- **Substance not name** of agreement determines applicability

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### Grants/Awards/ & Cooperative Agreements

- Federal \$\$\$ are provided to achieve a **public benefit**
- “**Recipient**” is a governmental or nonprofit entity that receives \$\$\$ directly from a Federal Agency
- “**Sub-Recipient**” is an entity that receives federal \$\$\$ from a “**Recipient**”

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### Sub-Recipients: (Typically)

- Determine **eligibility**
- Measure **performance** against grant objectives
- Make programmatic **decisions**
- Use funds to support their programs **not to** provide goods or services to the pass-through entity

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**Sub-Recipients  
(always)**

- **Required** to adhere to federal grant rules including:
- **OMB Uniform Guidance**
- **Specific CFRs** relating to the program
- **Other program requirements**

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**Contractor/Vendor  
(typically)**

- Provide goods & services to **pass-through entity** in normal course of business
- Provide similar goods & services to other customers
- Operate in competitive environment
- **Goods/services are ancillary to federal program**

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**Contractor/Vendors Are Not**

- subject to federal assistance program rules including **OMB Uniform Guidance**
- or
- **Program CFRs**

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### Substance not Words

- **Labeling** a sub-recipient agreement as a “contract” does not make it a contract as defined in the Uniform Guidance
- Many “**contracts**” with pass-through entities are **sub-recipient agreements**

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### Procurement System Goals

- Good decisions
- Avoid purchasing unnecessary or duplicative items
- Fairness
- Appropriate balance of price and quality
- No real or perceived Conflict of Interest
- Satisfaction of your contractual requirements

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### Key Procurement Requirements

- Avoid purchasing unnecessary items
- Analyze alternatives to identify the most economical and practical procurement
- Conduct procurement solicitations properly

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### More requirements . . .

- Facilitate purchasing from small business, minority and women owned firms, and firms in labor surplus areas
- Appropriate cost and price analysis
- Use appropriate contracting methods
- Code of Conduct – to avoid actual or perceived Conflict of Interest

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### Procurement System Elements

- Written policies and procedures
- System for testing compliance
- Consequences for non-compliance
- Continuous review and revision as needed

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### Avoid Conflict of Interest

- Written code of conduct to deal with **personal** or **organizational** conflicts of interest (related entities)
- Allow **no participation** in selection, award, or administration of contract by any person with a real or apparent conflict of interest
- Consider whether in fact or appearance, your nonprofit can be **impartial** in conducting procurement with related entity

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## More Federal Requirements. . .

- Avoid contracting with debarred or suspended parties  
<https://www.dol.gov/ofccp/regs/compliance/preaward/debarlst.htm>
- Make procurement documentation available to Federal awarding agency

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## Allowable Procurement Methods § 200.320

1. Micro-purchases
2. Small purchase procedure
3. Sealed bids
4. Competitive proposals
5. Non-competitive proposal –sole source

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### Procurement "Claw" (Sections 200.317-326)



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### Current Procurement Thresholds

- Micro Purchase < \$5,000 \*
- Small Purchase < \$150,000
- Sealed Bids ≥ \$150,000
- Competitive Proposals ≥ \$150,000
- Sole Source

\* Effective October, 2015

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### 2018 Threshold Changes

- Micro Purchase < \$10,000
- Small Purchase < \$250,000\*
- Sealed Bids ≥ \$250,000
- Competitive Proposals ≥ \$250,000
- Effective Date not yet announced

\* Simplified Acquisition Threshold

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### Micro Purchase

- Supplies or services with aggregate cost of \$5,000\* or less
- \$2,000 threshold for costs covered by Davis Bacon
- Competitive quotes not required if price is reasonable

\* 2018 change to \$10,000

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### Small Purchase Procedure

- Cost **no more** than Simplified Acquisition Threshold – currently **\$150,000\***
- Set by 48 C.F.R. Subpart 2.1 (Definitions for FAR)
- Price and rate quotes **must** be obtained from adequate number of suppliers
- Rationale for selection recorded

\*2018 raised to \$250,000

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### Procurements > Simplified Acquisition Threshold

- Perform a **cost or price analysis** before receiving bids or proposals
- Negotiate **profit as a separate element** of the price in any contract in which there is no price competition
- **Must not use** cost plus a % of cost or % of construction costs methods of contracting

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### Sealed Bids

- Preferred method for **construction** projects
- Complete **specifications** required
- Firm, **fixed price contract** is anticipated
- **Price** major element in determination

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### Solicitations must include. . .

- Technical requirements – acceptable minimum standards
- “Brand name or equal” descriptions
- Preferences for environmental protection and energy efficiency
- Factors which will be used to evaluate proposals

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### Competitive Proposals

- More than one source submits offer
- Either fixed price or cost reimbursement
- Used when conditions not appropriate for use of sealed bids

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### Sole Source- Noncompetitive Proposal

- Proposal sought from only one supplier
  - Only available from one source
  - Emergency – no delay tolerated
  - Authorized in advance by Fed Agency or Pass Through Entity
- or**
- After solicitation from multiple sources, competition deemed inadequate

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### Contract Provisions

- Uniform Guidance 2CFR 200 **Appendix II Part 200** to see mandatory provisions to be included in your contracts with vendors

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### Must Use Appropriate Contracting Methods

- Determine **most appropriate instrument** – fixed price, cost reimbursable, purchase order, incentive contracts, etc.
- **Do not use** “cost-plus-a-percentage of cost” or “percentage of construction cost” instruments

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### Your Next Steps?

- COSO based **review** of your **internal controls**?
- Review of current **Procurement Policies and Procedures**?
- Evaluate procurement **thresholds**?
- Other?

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