

# Imagine

*what we can do together*

## Accounting Newsletter for Arizona School Districts

### The Ethical Climate: Sunny and Mild, or Overcast and Foggy?

by Cherie R. Wright, CPA, CFE, CGFM, Partner

“Tone at the top” refers to a district’s general ethical climate, which is established by its governing body members, audit committee and upper management. Having a strong tone at the top is the foundation of the internal control structure and can help to prevent fraud and other unethical practices.



The governing board members have the responsibility for creating codes of conduct and living by them. The hypocrisy of “do as I say, not as I do” has been proven time and time again to be an ineffective approach. It generates a lack of respect for the internal controls set in place and the individuals who designed them.

A good organizational tone can be supported through policies, codes of ethics, a commitment to hiring competent employees and the development of reward structures that promote good internal controls and effective governance.

Instances of financial fraud are commonly associated with weaknesses in the tone at the top. Poor tone at the top may include instances of the following: a disparagement of internal controls, an overemphasis on other objectives such as fund balances or achievement of certain projects at the expense of ethics, a belief that compliance with the letter of the law is sufficient for appropriate ethical behavior, accommodations of some stakeholders but not others, blaming higher-ups or colleagues for unethical practices and conflicts of interest.

*(Continued on P.3)*

### Changes to Federal Financial Management and Audit Requirements

by Michael A. Hoerig, CPA, Partner

The Office of Management and Budget (OMB) was tasked by the President in 2009 to seek out potential reforms that would help increase the effectiveness and efficiency of Federal financial management. This directive led to the creation of the Council on Financial Assistance Reform (COFAR). COFAR membership consists of the OMB, eight of the largest federal granting agencies, and one other federal agency. The over-arching goals of the COFAR are to identify more efficient financial management practices through standardization of business processes, data standards and information technology; as well as to eliminate regulatory overburden and inconsistencies. In February 2012 the COFAR and OMB published their initial proposed guidance in the Federal Register for public comment. Over 300 comments were received from various agencies, organizations, and practitioners. This feedback prompted several changes and ultimately led to the final guidance issued in December 2013.

*(Continued on P.2)*

#### Also in This Issue

Applying Ratios to Your Financial Statements	P.2
HMU Events	P.5
H&M News	P.5
Tips on FLSA Compliance	P.5
Upcoming Deadlines	P.6



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## Changes to Federal Requirements

*(cont'd from P.1)*

One of the largest accomplishments achieved by the COFAR in the final guidance includes the elimination of duplicative OMB Circulars to one centralized guidance document. In particular, the following OMB Circulars have been consolidated:

- A-21, Cost Principles for Educational Institutions
- A-87, Cost Principles for State, Local, and Indian Tribal Governments
- A-89, Federal Domestic Assistance Program Information
- A-102, Awards and Cooperative Agreements with State and Local Governments
- A-110, Uniform Administrative Requirements for Awards and Other Agreements with Institutions of Higher Education, Hospitals, and Other Nonprofit Organizations
- A-122, Cost Principles for Non-Profit Organizations
- A-133, Audits of States, Local Governments and Non-Profit Organizations
- A-50, Audit Follow-Up, related to Single Audits

This accomplishment, along with a current study to consolidate and standardize key data elements and language, intends to reduce duplicative and inconsistent applications of the required guidance.

Other changes focus on performance achievements and outcomes, rather than prescribed practices and requirements. One example cited by OMB relates to the time and effort requirements. The new guidance focuses more on the importance and necessity for time and effort tracking rather than specific examples of how to track time and effort. The intention is to place more emphasis on the grantees' responsibilities to develop and maintain strong internal control environments to ensure

*(Continued on P.4)*

## Applying Ratios to Your Financial Statements

*by Neil S. Galassi, CPA, Audit Manager*

Ratios are an effective way to compare financial performance and resource utilization over a period of time. They can provide a great amount of information that can be used to assess the position of your district moving forward and to identify trends that may affect future fiscal years as annual budgets and projections are developed. They can be applied to virtually any balance sheet or income statement reporting category. Some ratios that may prove useful to your district include:

### Balance Sheet Ratios

can be used to determine the amount of leverage that a government has to finance its assets. They typically compare liabilities to total and current assets. A high ratio of total liabilities to total assets is indicative of your district depending on debt to finance its assets. These ratios can also be applied to specific balance sheet categories. For example, a ratio comparing outstanding debt to total assets can provide measure of solvency. Debt can also be compared to current assets to demonstrate the ability to your district to satisfy debt with more liquid assets (e.g., cash and investments). In this instance, a ratio greater than one indicates a high amount of leverage. The ideal ratio for your district is dependent on long and near-term financing needs as well as the ability to generate resources on an annual basis to satisfy debt payment obligations on an annual basis.



**Revenue and Expenditure Ratios** provide information on how a government's financial position has changed from year to year and what resources are available moving forward. One such ratio compares fund balance as a percentage of expenditures. This ratio is an indicator of the level of fund balance that can be used to pay for future obligations. This ratio is most meaningful when

*(Continued on P.3)*

## Ethical Climate

*(cont'd from P.1)*

Defining the ethical standards for a district can be difficult. Codes of conduct are typically written with legal requirements in mind for disciplinary use and cannot realistically address every scenario that may arise, but we generally set our own ethical standards at a higher level. In addition, everyone tends to have opinions on various ethical and moral questions, but rarely do they agree. Ethical dilemmas frequently occur in politics, science, medicine, religion – everywhere that more than one human being interacts with another. Ideally, we base our ethical decisions on a conviction that it is important to do our best to distinguish between right and wrong and that we always try to do what is right.



The bottom line is ensuring our decisions are based on the best interest of the district and the students and community served. Conflicts of interest can get in the way of conducting ourselves in this manner. Competing interests can include outside financial relationships, the desire for professional advancement and the desire to do favors for family and friends. Officials and employees with these competing interests should recuse themselves from the decision-making process and allow those who are free from the conflict of interest to choose what is the best decision for the district.

If conducting operations in the best interest of the district and the students and community served is not enough motivation for ensuring a strong tone at the top, how about preventing fraud and the loss of the district's resources? The Association of Certified Fraud Examiners (ACFE) conducts a study on fraud every two years.

*(Continued on P.4)*

## Applying Ratios

*(cont'd from P.2)*

expenditures are compared to unrestricted fund balance as this category represents the most available and liquid element of fund balance. A ratio of one indicates the government has fund balance equal to one fiscal year of expenditures. The optimal ratio for your government will depend on budget and fiscal policies, regulations, and practices in place at your government.

**Comparisons to Prior Fiscal Years** A beneficial characteristic of governmental financial statements is that they are typically comparable from year to year. Large fluctuations and noticeable trends in your district's financial statements will typically be a factor of a specific event. Some comparisons may include:

- Comparing changes in net position or fund balance by category
- Comparing assets and liabilities by category
- Comparing revenues by type to prior fiscal years
- Comparing expenditures by function to prior fiscal years

Such comparisons are most meaningful when taken over a period of time (e.g., three fiscal years) and can be useful tools for forecasting and budgeting as well as provide some basis for future decisions.

Overall, ratios can be applied to virtually any financial statement or disclosure in your financial report and provide a wealth of information to assist you in when making decisions regarding your district. ■

## Changes to Federal Requirements

(cont'd from P.2)

compliance with financial management requirements.

The most significant change in audit requirements is the increase in the Single Audit threshold to \$750,000 from the current level of \$500,000. According to OMB research, increasing this threshold will eliminate the need for approximately 5,000 Single Audits while still maintaining audit coverage for 99% of the federal grants awarded. Increasing the threshold will reduce the burden on smaller non-federal entities while also reducing the sub-recipient monitoring duties of larger granting agencies. In addition to the Single Audit threshold, the guidance also increases the Type A threshold for major federal programs to \$750,000 from the current level of \$300,000. Other changes in audit requirements affect the determination of the amount of Federal awards to be audited. Specifically, the minimum amount of awards that must be audited for low-risk auditees will decrease from 25% to 20% of annual federal expenditures while audit coverage for high-risk auditees will decrease from 50% to 40% of annual federal expenditures.

All of these changes will require a significant amount of effort at each Federal agency to incorporate the new guidance into their respective granting and oversight processes, as well as their grant literature and forms. As such, the implementation date for Federal agencies is immediate; however the implementation date for non-federal entities is the fiscal year *beginning* on or after January 1, 2015.

Visit the COFAR website (<https://cfo.gov/cofar/>) for more information and guidance to occur over the next year, as well as links to video webinars held in December 2013 and January 2014. The finalized guidance is available at <https://federalregister.gov/a/2013-30465> ■

## Ethical Climate

(cont'd from P.3)

Based on this study, the ACFE estimates the typical organization loses 5 percent of its revenues to fraud each year. Based on the U.S. gross national product (GNP), this represents a nationwide loss of \$755 billion every year! In comparison, the 2012 gross cost for the U.S. Department of Defense was \$782 billion (the world's largest employer with 3.2 million employees).



The evaluation of the control environment and a district's general ethical climate is a key element in conducting an entity-wide risk assessment. An entity-wide risk assessment identifies the highest risks so that resources are dedicated to the highest priorities for the protection of the district's assets and resources. These are typically prepared by the internal auditors or contracted out.

To demonstrate a commitment to an ethical environment, some of the things that districts can do include: (1) regular trainings on ethics and the expectations of conduct provided to all officials and employees, (2) adoption of a code of conduct or code of ethics and provided to all officials and employees; (3) potential conflicts of interest disclosed and updated on a regular basis; and (4) a process for monitoring potential conflicts of interest.

**Questions or need help?** Contact Cherie Wright at (602) 277-9449 or [cheriew@heinfeldmeech.com](mailto:cheriew@heinfeldmeech.com). ■

## Puzzler

Decipher the hidden meaning: (Answer on p. 6)  
**KJUSTK**

## HMU Events

Details and links to online registration can be found at [www.heinfeldmeech.com/hmu](http://www.heinfeldmeech.com/hmu). For more help, contact Susan at 520-742-2611, x107 or [hmu@heinfeldmeech.com](mailto:hmu@heinfeldmeech.com).



### Understanding Reporting of School District Capital Assets

**Location:** Mesa, AZ (Mesa Convention Center)

**Date:** Monday, March 3

**Registration Ends:** 2/20/14

### Arizona School Board Members Lunch Workshop

**Location:** Phoenix, AZ (Arizona School Board Assn.)

**Date:** Friday, April 4

**Early Bird Pricing Ends:** 3/20/14

**Registration Ends:** 3/27/14

### Accounting Skills for Governments and Non-Profits (a 2-day workshop)

**Locations:** Mesa, AZ and Vail, AZ (Tucson area)

**Dates:** Thursday and Friday, May 8-9

*Details and registration available by mid-March!*

## H&M News

*Karin M. Smith, MBA, SFO*, was recently promoted to Partner. Karin has been a member of the firm's consulting division since 2011 and also has more than 14 years of experience working in the public sector in Arizona. For more information on Karin, visit [her page on our website](#).

We are also happy to announce these other recent promotions: *Kara Jungbluth, CPA*, and *James Shankland* to Senior Associate; and *Katlin M. Bryant, CPA*, *Jordan King*, and *Joseph Wagner* to Staff Associate II.

## Tips on FLSA Compliance

*by CW Payne, CPA, Partner*

The following items were a few of the areas reviewed during our firm's most recent workshops on Fair Labor Standards Act (FLSA) Compliance. For current FLSA guidance, visit <http://www.dol.gov/whd/flsa/>.

**Travel Time/Travel Away from Home:** According to the Wage & Hour Division, "travel away from home" is defined as travel that keeps an employee away from home overnight. Travel away from home is clearly identified as work time when it cuts across the employee's workday. Travel time not only includes hours worked during normal working hours on regular working days, but also during corresponding hours on nonworking days. However, the Division does not consider travel time as a passenger in a transport vehicle (away from home and outside of regular working hours) to be work time.

**On-Call Time:** When employees are on-call it can be difficult to determine what is worked time vs non-worked time. Here is a link to help with those questions: [www.dol.gov/elaws/esa/flsa/hoursworked/screenER80.asp](http://www.dol.gov/elaws/esa/flsa/hoursworked/screenER80.asp)

**Docking Time:** Employers can only dock exempt employees by the day; exempt employees' pay cannot be docked for partial days. Employers do have the ability to reduce employees leave balance for partial day absences. Additional guidance about disciplinary deductions can be found at: [www.dol.gov/elaws/esa/flsa/overtime/cr5.htm](http://www.dol.gov/elaws/esa/flsa/overtime/cr5.htm) ■

*Legal and Tax Advice Disclaimer:* The information presented in this newsletter does not constitute legal advice or tax advice. Heinfeld, Meech & Co., P.C. makes no claims about its accuracy, completeness, or currency of information presented, including any external references provided. Please consult legal counsel for advice pertaining to your specific organization.

### Upcoming School District Deadlines

<u>Due Date</u>	<u>Item</u>
Feb. 15	Special Education Census should be submitted to ADE English Language Learners (ELL) report due to ADE
Feb. 28	For paper filing, Form 1096, Annual Summary and Transmittal of U.S. Information Returns, along with Copy A of all Forms 1099, must be filed with the IRS.  Form A-1R, Annual Withholding Tax Return, must be filed with the Arizona Department of Revenue. (A.R.S. 43-412)  Form W-3, Transmittal of Wage & Tax Statements, along with Copy A of all Forms W-2, must be filed with the Social Security Administration.
March 31	Annual and biennial audits due to AG, ADE and Federal Clearinghouse (if applicable)  For electronic filings, Form 1096 and Copy A of all Forms 1099 due to IRS. (Organizations with more than 250 returns must file electronically.)
April 1	Deadline to submit an amendment for all grants ending on June 30
Before May 15	Final budget revision must be approved by the Board
May 18	Final budget revision must be uploaded to ADE

### About H&M

Heinfeld, Meech & Co., P.C., CPAs and Business Consultants, has offices in Tucson, Phoenix and Flagstaff, Arizona. With more than 27 years of experience, we are the recognized leaders in the State of Arizona in the field of school district accounting and auditing.

Our active involvement with national and state associations keep us up-to-date about emerging issues affecting your school district. We offer this free newsletter as part of our commitment to providing resources and training to school district business personnel.

For more about our firm, please visit our web site at [www.heinfeldmeech.com](http://www.heinfeldmeech.com).



Answer to Puzzler (Page 4): "Just in case"