
Betty Montgomery Auditor of State

Bulletin 2006-007

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TO: All Public Offices
Independent Public Accountants

FROM: Betty Montgomery
Ohio Auditor of State

SUBJECT: Public Contracting/Required Financial Reviews (Sections 9.23, 9.231, 9.232, 9.233, 9.234, 9.235, 9.236, 9.237, 9.238, 9.239, R.C.)

Overview

Recently enacted House Bill 66, the State's biennial budget bill, contains a series of provisions which affect the process for public offices that contract with private entities.¹ This Bulletin is intended to notify public offices about a form for financial reviews which the Auditor of State is required to create and make available. Please note that this Bulletin is not intended to be a comprehensive explanation of the public contracting provisions included in House Bill 66. Public offices should consult with their legal counsel about the requirements of the bill, and the Auditor of State will defer to the well reasoned opinions of legal counsel on interpretations of the law.

Background

The Revised Code sections identified above, all of which were enacted in House Bill 66 (effective January 1, 2006), include specific requirements for contracts between public offices (on both the State and local level) and private entities, in excess of \$25,000. Exceptions to these requirements are described in R.C. § 9.231. These statutes include specific requirements that must be addressed in those contracts, such as the minimum percentage of money that must be expended on direct costs, records that must be maintained, and allowable dispositions of money received in excess of the allowable amount. The bill requires annual reporting by the private entities, addresses the manner in which misspent money may be recovered, and gives the contracting public offices access to the records of the private entity related to the contract.

¹ Includes both nonprofit and for-profit entities.

Financial Review Forms (Sections 9.234, 9.238, R.C.)

House Bill 66 also requires in R.C. § 9.234 (B), annual audits or financial reviews, depending on the amount of money received by the private entity, conducted by independent public accounting firms. It is the responsibility of the public office to identify the contractors to whom this applies and to ensure that the annual audits or financial reviews are completed. It should be noted that R.C. § 9.234 includes language which clarifies that these audit and financial review requirements do not limit the authority of the Auditor of State to conduct audits authorized elsewhere in the Revised Code. Further, if the contracted private entity receives an audit conducted in accordance with generally accepted auditing standards or if the audit is conducted pursuant to the federal “Single Audit Act of 1984,” the private entity is not required to undergo either the financial review or the annual audit required per House Bill 66.

Relative to these requirements, R.C. § 9.238 requires the Auditor of State to prescribe a single form independent accountants must use for the financial reviews required of private entities receiving between \$100,000 and \$500,000 of public money. In compliance with this requirement the Auditor of State has developed a financial review form, which is attached to this Bulletin and which shall be used to comply with R.C. § 9.234 (B). The financial review form may also be obtained from the Auditor of State website at www.auditor.state.oh.us.

The contracted private entity must provide the public agency with the completed financial review or audit report for each year in which it meets the thresholds described in R.C. § 9.234. Please note that copies do not need to be submitted to the Auditor of State’s Office.

Questions

Questions regarding the financial review form should be addressed to the Accounting & Auditing Support Group of the Auditor of State’s Office at 1-800-282-0370. Any questions with regard to the public contracting provisions of House Bill 66 should be directed to your legal counsel.



Betty Montgomery
Ohio Auditor of State

1. SAMPLE REVIEW REPORT ON CONTRACTOR'S SCHEDULE

Independent Accountant's Report

Contractor Name
Contractor Address

We have reviewed the accompanying Schedule of Revenues and Expenses of [*Contractor*] for the fiscal year ended [Date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants and the requirements of the Auditor of State of Ohio. All information included in this Schedule is the representation of the management of [*Contractor*].

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the Schedule taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying Schedule in order for it to be in conformity with generally accepted accounting principles and the provisions of section 9.232 of the Ohio Revised Code.

[*Signature of Accountant*]

[Date]

2. FORMAT FOR THE CONTRACTOR'S SCHEDULE OF CONTRACTED REVENUES AND EXPENSES

Major categories of contract revenues [detailed]

Major Categories of Contract Expenses [detailed]

Direct

Allocable Nondirect

Notes to the Schedule

Significant Accounting Policies

Methodology for computing direct and non-direct costs as defined in the
ORC\OAC
Other

Supplementary Information: Summary of Activities for which the contractor used the
contracted money

3. OPTIONAL PRACTICE AIDS

REVIEW ENGAGEMENT LETTER

[*Contractor/Client Name*]

[*Contractor Address*]

Dear [*Client*]:

This letter is to confirm our understanding of the terms and objectives of our engagement and the nature and the limitations of the services we will provide.

We will perform the following services:

We will review the Schedule of Revenues and Expenses of the [*Contractor*] for the fiscal year ended [Date] in accordance with Statement on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants and the requirements of the Auditor of State of Ohio.

Our review will consist primarily of inquiries of company personnel and analytical procedures applied to financial data, and we will require a representation letter from management. A review does not contemplate obtaining an understanding of the internal control structure or assessing control risk, tests of accounting records, and responses to inquiries by obtaining corroborating evidential matter, and certain other procedures ordinarily performed during an audit. Thus, a review does not provide assurance that we will become aware of all significant matters that would be disclosed in an audit. Our engagement cannot be relied upon to disclose errors, fraud, or illegal acts that may exist. However, we will inform the appropriate level of management of any material errors that come to our attention and any fraud or illegal acts that come to our attention, unless they are clearly inconsequential.¹ We will not perform an audit of such Schedule, the objective of which is the expression of an opinion regarding the Schedule taken as a whole, and accordingly, we will not express such an opinion on it.

¹ Paragraph 5.20 of *Government Auditing Standards* (2003 Revised) indicates that quantitative and qualitative factors determine whether a non-compliance item is: “clearly inconsequential.” The Auditor of State’s *Ohio Compliance Supplement* classifies audit findings with an impact of \$100 or less as “clearly inconsequential.”

Our review report on the Schedule of [Contractor] is currently expected to read as follows:

We have reviewed the accompanying Schedule of Revenues and Expenses of [Contractor] for the fiscal year ended [Date], in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants and the requirements of the Auditor of State of Ohio. All information included in this Schedule is the representation of the management of [Contractor].

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an audit in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the Schedule taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying Schedule in order for it to be in conformity with generally accepted accounting principles and the provisions of section 9.232 of the Ohio Revised Code.

If, for any reason, we are unable to complete the review of your Schedule, we will not issue a review report on such Schedule as a result of this engagement.

Our fee for these services will be based on the number of hours required by the staff assigned to complete the engagement. In accordance with our recent discussion, we believe that the engagement fee will not exceed \$. However, if we encounter unexpected circumstances that require us to devote more staff hours to the engagement than estimated, we will discuss the matter with you.

We look forward to a continued relationship with your company, and we are available to discuss the contents of this letter or other professional services you may desire.

If the foregoing is in accordance with your understanding, please sign the copy of this letter in the space provided and return it to us.

Sincerely,

[Signature of Accountant]

ACKNOWLEDGED:

[Contractor]

[Date]

REVIEW PROGRAM

Use the following procedures as a guide for performing a continuing review engagement. The review program is only a guide, and professional judgment should be exercised to determine how the procedures should be modified by revising procedures listed or adding procedures to the review program.

Initial and date each procedure as it is completed. If the procedure is not relevant to this particular review engagement, place "N/A" (not applicable) in the space provided for an initial.

Client Name: _____

Date of Schedule: _____

Date of Fieldwork: _____

	<u>Initials</u>	<u>Date</u>	<u>Workpaper Reference</u>
1. Acquire an adequate understanding of accounting principles and practices of the client's industry and methods of applying them.	_____	_____	_____
2. Develop an understanding of the client's organization.	_____	_____	_____
3. Develop an understanding of the client's operating characteristics.	_____	_____	_____
4. Develop an understanding of the nature of the client's assets, liabilities, revenues, and expenses.	_____	_____	_____
5. Make inquiries concerning the client's accounting principles, practices, and methods, including computing direct costs as defined in Ohio Administrative Code section ..	_____	_____	_____
6. Make inquiries concerning the client's procedures for recording, classifying, and summarizing transactions and accumulating information for disclosure in the Schedule, including the direct and indirect cost methodologies.	_____	_____	_____

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| 7. Make inquiries concerning actions taken by the contractor's governing authority at meetings of stockholders, board of directors, or other meetings that may affect the Schedule. | | | |
| 8. Make inquiries concerning the consistent application of GAAP. | | | |
| 9. Make inquiries concerning changes in the client's business activities or accounting principles and the implication for Schedule. | | | |
| 10. Make inquiries concerning occurrence of subsequent events that may have a material effect on the Schedule. | | | |
| 11. Make inquiries regarding the extent of unusual or complex situations that might exist and that have a material effect on the Schedule. | | | |
| 12. Make inquiries about whether significant transactions occurred or were recognized in the last several days of the reporting period. | | | |
| 13. Inquire about the status of uncorrected misstatements identified in prior engagements. | | | |
| 14. Inquire regarding whether management has any knowledge of fraud or suspected fraud affecting the entity that might involve management or others that could materially misstate the Schedule. | | | |
| 15. Make inquiries concerning the types of significant journal entries or other adjustments that exist. | | | |
| 16. Inquire regarding whether the client has received communications from regulatory or contracting agencies. | | | |
| 17. Apply analytical procedures to identify relationships and individual items that appear to be unusual. | | | |

18. Consider whether other professional services are needed before starting the review engagement.

19. If appropriate, obtain reports from other accountants.

20. Consider whether other review procedures should be performed on the basis of the results of performing the minimum review procedures.

21. Read the Schedule to consider if it conforms with GAAP.

22. Obtain a client representation letter.

23. Other review procedures:

Reviewed By:

Date: _____

REVIEW CHECKLIST

Use the following checklist as a guide for performing review procedures in a continuing engagement. The checklist is only a guide, and professional judgment should be exercised to determine how the checklist should be modified by revising questions listed or adding questions to the checklist where appropriate.

Initial and date each question as it is considered. If the question is not relevant to this particular review engagement, place "N/A" (not applicable) in the space provided for an initial. If the answer to the question is "no" or if additional explanation is needed with respect to a question, provide a proper cross-reference to another workpaper.

Client Name: _____

Date of Schedule: _____

	<i>Initials</i>	<i>Date</i>	<i>Workpaper Reference</i>
1. Have we acquired an adequate understanding of specialized accounting principles and practices of the client's industry by			
• Reviewing relevant AICPA Accounting/Audit Guides?	_____	_____	_____
• Reviewing Schedules of other entities in the same industry?	_____	_____	_____
• Consulting with other individuals familiar with accounting practices in the specialized industry?	_____	_____	_____
• Reading periodicals, textbooks, and other publications?	_____	_____	_____
• Performing other procedures?	_____	_____	_____
2. Have we developed an understanding of the client's organization, including			
• The form of business organization?	_____	_____	_____
• The history of the client?	_____	_____	_____
• The principals involved in the organizational chart or similar	_____	_____	_____
• Other relevant matters?	_____	_____	_____
3. Have we developed an understanding of the client's operating characteristics, including			
• An understanding of the client's products and services?	_____	_____	_____
• Identification of operating locations?	_____	_____	_____
• Other operating characteristics?	_____	_____	_____

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|--|--|--|
| <p>4. Have we developed an understanding of the nature of the client’s assets, liabilities, revenues, and expenses by</p> <ul style="list-style-type: none"> • Reviewing the client’s chart of accounts? • Reviewing the previous year’s Schedule? • Considering the relationships between specific accounts and the nature of the client’s business? • Performing other procedures? | <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> | <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> |
| <p>5. Have we made inquiries concerning accounting principles, practices, and methods?</p> | <p>_____</p> | <p>_____</p> |
| <p>6. Have we made inquiries concerning the accounting procedures used by the client, including</p> <ul style="list-style-type: none"> • Recording transactions? • Classifying transactions? • Summarizing transactions? • Accumulating information for making disclosures in the Schedule? • Other accounting procedures? | <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> | <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> |
| <p>7. Have we made inquiries concerning the effect on the Schedule due to actions taken at meetings of the contractor’s governing authority</p> <ul style="list-style-type: none"> • Stockholders? • The board of directors? • Other committees? | <p>_____</p> <p>_____</p> <p>_____</p> | <p>_____</p> <p>_____</p> <p>_____</p> |

8. If there were changes in the application of accounting principles
- Did the change in accounting principle include the adoption of another acceptable accounting principle? _____
 - Was the change properly justified? _____
 - Were the effects of the change presented in the Schedule, including adequate disclosure, in a manner consistent with APB-20? _____
 - Were there other matters that we took into consideration? _____
9. Have we made inquiries concerning changes in the client's business activities that may require the adoption of different accounting principles, and have we considered the implication of this change for the Schedule? _____
10. Have we made inquiries concerning the occurrence of events subsequent to the date of the Schedule that may require
- Adjustments to the Schedule? _____
 - Disclosures in the Schedule? _____
11. Have we made inquiries regarding the extent of unusual or complex situations that might exist and that have a material effect on the Schedule? _____
12. Have we made inquiries about whether significant transactions occurred or were recognized in the last several days of the reporting period? _____
13. Have we inquired about the status of uncorrected misstatements identified in prior engagements? _____

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|---|-------|-------|-------|
| 14. Have we inquired regarding whether management has any knowledge of fraud or suspected fraud affecting the entity that might involve management or others that could materially misstate the Schedule? | _____ | _____ | _____ |
| 15. Have we made inquiries concerning the types of significant journal entries or other adjustments that exist? | _____ | _____ | _____ |
| 16. Have we inquired regarding whether the client has received communications from regulatory or contracting agencies? | _____ | _____ | _____ |
| 17. Have we performed analytical procedures, including | | | |
| • Comparing current Schedule with comparable prior period(s)? | _____ | _____ | _____ |
| • Comparing current Schedule with anticipated results? | _____ | _____ | _____ |
| • Studying financial statement elements and expected relationships? | _____ | _____ | _____ |
| • Other analytical procedures? | _____ | _____ | _____ |
| 18. Have we considered whether other professional services are needed in order to complete the review engagement, including | | | |
| • Preparing a working trial balance? | _____ | _____ | _____ |
| • Preparing adjusting journal entries? | _____ | _____ | _____ |
| • Consulting matters fundamental to the preparation of acceptable Schedule? | _____ | _____ | _____ |
| • Providing bookkeeping or data processing services that do not include the generation of Schedule? | _____ | _____ | _____ |
| • Considering other services that may be necessary before a review can be performed? | _____ | _____ | _____ |

- 19. Have we obtained reports from other CPA(s) who reported components of the client-reporting entity? _____
- 20. Have we read the Schedule to determine whether it appears to be in accordance with GAAP based on the information that has come to our attention? _____
- 21. Have we obtained a client representation letter? _____
- 22. Have we used other procedures to resolve questions during the review arrangement? _____

Reviewed By: _____

Date: _____

CLIENT REPRESENTATION LETTER

[Date (no earlier than the date of the accountant's report)]

[Auditor Name]

[Address]

Dear [Auditor]:

In connection with your review of the Schedule of Revenues and Expenses of [Contractor] for the year ended [Date], for the purpose of expressing limited assurance that there are no material modifications that should be made to the statements in order for them to be in conformity with generally accepted accounting principles, we confirm, to the best of our knowledge and belief, the following representations made to you during your review.

- 1. The Schedule referred to above presents the revenues and expenses of [Contractor] related to contracts entered into pursuant to section 9.231 of the Ohio Revised Code in conformity with generally accepted accounting principles. In that connection, we specifically confirm that:
 - a. The company's accounting principles, and the practices and methods followed in applying them are as disclosed in the Schedule.

- b. There have been no changes during the year ended [Date] in the company's accounting principles and practices.
 - c. There are no material transactions that have not been properly reflected in the Schedule.
 - d. There are no violations or possible violations of laws or regulations whose effects should be considered for disclosure in the Schedule or as a basis for recording a loss contingency, and there are no other material liabilities or gain or loss contingencies that are required to be accrued or disclosed. Also, there are no unasserted claims or assessments that our lawyer has advised us are probable of assertion that must be disclosed in accordance with Financial Accounting Standards Board (FASB) Statement No. 5 (CT C59), Accounting for Contingencies.
 - e. There are no related-party transactions, including sales, purchases, loans, transfers, leasing arrangements, and guarantees, and amounts receivable from or payable to related parties that have not been properly disclosed in the Schedule.
 - f. We have complied with all aspects of contractual agreements that would have a material effect on the financial statement in the event of noncompliance.
 - g. To the best of our knowledge and belief, no events have occurred subsequent to [[fiscal year end date] and through the date of this letter that would require adjustment to our disclosures in the Schedule.
 - h. Management has identified all significant estimates used in the preparation of the Schedule.
2. We have advised you of all actions taken by our governing authority at meetings of [stockholders, the board of directors, and committees of the board of directors] (or other similar bodies, as applicable) that may affect the Schedule.
 3. We have responded fully and truthfully to all inquiries made to us by you during your review.
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