

## APPENDIX D: COMPLIANCE ACE FORM

### Assessment of the Compliance Controls' Environment

**Note: We streamlined this requirement in the December 2008 OCS. We assume auditors (including IPA's) will adequately address (and document) control environment considerations described in GAAS (especially AU 314), some of which relate directly or indirectly to compliance. Therefore, we removed points of focus auditors should have already addressed in their control environment assessments. What remains are points of focus specific to the OCS.**

#### Instructions for Using the Compliance ACE Form

- Illustrative points of focus are given for each area. The auditor should not answer 'Yes' or 'No' to the points of focus. Rather, the auditor should comment on each area, using the points of focus as further guidance where appropriate, basing comments on information available from prior years' audits, inquiries of individuals inside and outside the organization, knowledge of factors outside the government that affect its activities, observation of circumstances that are known or are understood to exist within the government, and, in some circumstances, inspection of documents.
- The areas for assessment and illustrative points of focus in the ACE are not equally relevant to all engagements, and the significance of any particular area or point of focus varies with the government. Thus, the auditor should judge the applicability and importance of each in the context of the engagement.
- In assessing the control environment, the auditor should recognize that neither the areas for assessment nor the illustrative points of focus are necessarily all-inclusive. The auditor may encounter matters affecting the control environment other than those addressed by the ACE. The auditor should document those matters and assess their effect on the control environment.
- In assessing the control environment, the auditor should look beyond the form of control measures and management actions and should concentrate on their substance. An environment may appear to be favorable but in reality may not be. For instance, a system may provide adequate reports for the governing board or senior management, but if the information is not analyzed and acted on, the system does not contribute to the control environment. Similarly, a government may establish appropriate policies; however, to be effective, they should be enforced by management. For example, although a government may have a formal code of conduct, management may have a record of condoning actions that violate it. By not reprimanding such actions, management sends a clear message undermining the code of conduct.

**Audit Implications**

- After assessing each area, the auditor should consider the audit implications of any circumstances coming to his or her attention that may affect the audit strategy and audit program, or that may represent a matter for which we can offer a recommendation for improvement.

**Application to Small and Mid-sized Entities**

- Small and mid-sized entities may implement the control environment areas differently than larger entities. For example, smaller entities might not have a written code of conduct but instead, develop a culture that emphasizes the importance of integrity and ethical behavior through oral communication and by management example. However, these conditions may not affect the auditor's assessment of control risk.

Budgetary (OCS Chapter 1)	
Area for Assessment	Comments
<p>The following factors may influence the auditor's assessment of risk of significant non-compliance with budget laws and regulations:</p> <p>Management develops strategic plans and budgets to monitor the activities of the entity. ORC 5705 codifies an annual budget process designed to prevent fund cash deficits. To be effective, these plans and budgets should be realistic, based on valid assumptions and developed by knowledgeable individuals. Management must also have sufficient reliable information on a timely basis to review and evaluate the entity's operations.</p> <p><i>Consider for example, the following points of focus:</i></p> <ul style="list-style-type: none"> <li>- <i>Existence of a budgetary monitoring system and compliance function (This is part of <b>monitoring</b> more than the control environment, but we have listed it here because of its importance and interaction with the control environment.)</i></li> <li>- <i>The effectiveness of the budget process (i.e. segregation of duties for budget preparation, adoption, execution and reporting).</i></li> <li>- <i>The level of detail (e.g. legal level of control) and informational value of plans and budgets and of financial, statistical, or other information management and those charged with governance use regarding:</i> <ul style="list-style-type: none"> <li>• <i>its relevance to the respective manager's responsibilities,</i></li> <li>• <i>its sufficiency,</i></li> <li>• <i>the frequency and timeliness with which it is received, and</i></li> <li>• <i>its reliability.</i></li> <li>• <i>Appropriate involvement of personnel, for example:</i></li> <li>• <i>both senior management and lower-level personnel,</i></li> <li>• <i>managers, for activities relating to their respective areas of responsibility, and</i></li> <li>• <i>suitably knowledgeable and experienced personnel (such as operating line management).</i></li> </ul> </li> <li>- <i>The assumptions underlying strategic plans and budgets; that is, whether they:</i> <ul style="list-style-type: none"> <li>• <i>reflect the entity's historical experience and conditions currently affecting operations, and</i></li> <li>• <i>are consistent and are communicated to the appropriate personnel.</i></li> </ul> </li> <li>- <i>The past record of the entity in meeting plans and budgets.</i></li> </ul>	

- *The effectiveness of monitoring performance with respect to:*
  - *documenting significant departures from plans (i.e. budgets), with explanation,*
  - *evaluation of explanations by the appropriate levels of management or the governing authority,*
  - *implementing corrective actions by appropriate levels of management and follow-up by senior management and those charged with governance.*
  - *timeliness of consideration of the effect of changes in the economy, industry, and competition,*
  - *indication and timeliness of corrective actions,*
- *An accounting system that integrates budgetary accounts to provide continuous information regarding available appropriations and estimated resources not yet received.*

Note: The AICPA's State & Local Government Audit Guide, 11.25 & .26 cautions the auditor to consider whether the government uses its budget to control spending or instead, uses spending to establish (i.e. amend) the budget. Many governments do the latter, in which case analytical procedures relating to the budget may not be valid support for financial position and activity statement assertions.

**Audit implications and/or management comments:**

Contracts and Expenditures (OCS Chapter 2)	
Area for Assessment	Comments
<b>Points of Focus</b> <ul style="list-style-type: none"><li>- Existence of a contract and expenditures monitoring system and compliance function (This is part of <b>monitoring</b> more than the control environment, but we have listed it here because of its importance and interaction with the control environment.)</li><li>- Legal actions brought against the entity, elected and non-elected officials related to contract compliance.</li></ul>	
<b>Audit implications and/or management comments:</b>	

Debt (OCS Chapter 3)	
Area for Assessment	Comments
<p><b>Points of Focus (Debt)</b></p> <ul style="list-style-type: none"> <li>- Existence of a debt monitoring system and compliance function (This is part of <b>monitoring</b> more than the control environment, but we have listed it here because of its importance and interaction with the control environment.)</li> <li>- Governing authority's and management's involvement in the internal control structure to assure compliance with debt laws, contracts and regulation such as covenant requirements and 17 C.F.R. § 240.15c2-12</li> <li>- Willingness to use bond counsel or other specialists (e.g. arbitrage specialists) when issuing debt.</li> <li>- Accounting system suitably designed to comply with any requirements to separately account for debt proceeds or debt service payments.</li> </ul>	
<p><b>Audit implications and/or management comments:</b></p>	

Accounting and Reporting (OCS Chapter 4)	
Area for Assessment	Comments
<b>Points of Focus</b> <ul style="list-style-type: none"><li>- Existence of a monitoring system and compliance function (This is part of <b>monitoring</b> more than the control environment, but we have listed it here because of its importance and interaction with the control environment.)</li><li>- Accounting system suitably designed to accommodate the reporting requirements in Chapter 4 applicable to the auditee.</li></ul>	
Audit implications and/or management comments:	

Deposits and Investments (Chapter 5)	
Area for Assessment	Comments
<p><b>Points of Focus</b></p> <ul style="list-style-type: none"> <li>- Existence of a deposits and investments monitoring system and compliance function (This is part of <b>monitoring</b> more than the control environment, but we have listed it here because of its importance and interaction with the control environment.)</li> <li>- Basic knowledge of laws restricting investment instruments, or a practice of referring to ORC 135 and written investment policies</li> <li>- knowledge of the features and risks of investments prior to purchasing them.</li> <li>- Sufficient cash flow planning to avoid investment losses resulting from insufficient liquidity. (For example, RC 135.14(F) requires an ability to hold an investment to maturity.) Therefore, investing all available cash in a 5 year instrument could require selling it at a loss prior to maturity if the government needs the cash before the five-year maturity, contrary to RC 135.14(F)).</li> </ul>	
<p><b>Audit implications and/or management comments:</b></p>	



Other Potentially Direct and Material Laws and Regulations (OCS Chapter 6)	
Area for Assessment	Comments
<p><b>Points of Focus</b></p> <ul style="list-style-type: none"> <li>- Existence of an appropriate monitoring system and compliance function. (This is part of <b>monitoring</b> more than the control environment, but we have listed it here because of its importance and interaction with the control environment.)</li> <li>- Accounting system suitably designed to provide information when needed, such as information related to insurance claims, landfill closure or postclosure costs.</li> <li>- Suitable systems and procedures for collecting other financially significant information reliably, such as landfill usage, student attendance statistics.</li> <li>- A commitment by school management and those charged with their governance to obtain accurate ADM student counts.</li> </ul>	
<p><b>Audit implications and/or management comments:</b></p>	