



NATIONAL ENDOWMENT FOR THE
Humanities

OFFICE OF INSPECTOR GENERAL

August 2, 2016

RETURN RECEIPT REQUESTED

Board of Directors
Arkansas Humanities Council
407 President Clinton Avenue, Suite 201
Little Rock, Arkansas 72201
Attn: [REDACTED] Chair

OIG Report Number: OIG-16-05 (DR)

Dear Board Members:

We have completed a Desk Review of the single audit report prepared by BKD, LLP, which includes the Federal assistance programs administered by the Arkansas Humanities Council (the "Council"), for the fiscal year (FY) ended October 31, 2014. The independent auditor (IPA) previously furnished a copy of their audit report dated April 10, 2015, to the Council and submitted the related reporting package to the Federal Audit Clearinghouse. The IPA issued unmodified opinions¹ regarding the financial statements and compliance with Federal requirements. Furthermore, no written findings were issued in conjunction with the single audit.

Our review was limited to an examination of the audit report, email exchanges with the Executive Director and Operations/Financial Officer of the Council, email exchanges and a teleconference with the IPA, a limited review of select IPA workpapers, and review of applicable NEH grant files and accounting records. We did not perform a comprehensive examination of the underlying audit documentation to evaluate the adequacy of the audit work performed; rather, the *Guide for Desk Reviews of OMB Circular A-133 Audit Reports (2015 Edition)*, issued by the Council of Inspectors General on Integrity and Efficiency (CIGIE), was used to determine whether the audit report meets the core reporting requirements stipulated by Office of Management and Budget (OMB) Circular A-133. Audit reports receiving a *Fail* rating require corrective action.

We assigned a rating of *Fail*² for the October 31, 2014 reporting package primarily due to the unrecognized, material deviation from generally accepted accounting principles (GAAP), which is effected by the presentation of non-accrual based "receivable" and "payable" account balances on the audited Statement of Financial Position. We also noted that the FY2014 report does not reflect

¹ An unmodified opinion represents the IPA's highest level of assurance, indicating that the audited entity's financial statement presentation (to include Federal grant activity) materially complies with applicable accounting standards and Federal requirements stipulated in OMB Circular A-133: *Audits of States, Local Governments, and Non-Profit Organizations*.

² There are three possible conclusions applicable to a single audit desk review -- Pass; Pass with Deficiencies; or Fail. The NEH-OIG has assigned a "Fail" rating to the FY2014 audit report submission since the "report contains quality deficiencies that may affect the reliability of the audit report and/or may require the auditor to conduct additional audit work to support the opinions in the report under review."

the impact of Federal financial reporting discrepancies that should have been identified during the IPA's Federal compliance testing. Accordingly, the audit report and the Data Collection Form (Form SF-SAC) must be revised and resubmitted to the Federal Audit Clearinghouse (FAC).

Material Departure from GAAP

The IPA issued an unmodified opinion³ that the Council's FY2014 financial statements present fairly, in all material respects, the financial position of the Council as of October 31, 2014, and the changes in its net assets and its cash flows for the year then ended, in accordance with accounting principles generally accepted in the United States of America. However, we determined that the Council deviated materially from GAAP by presenting "receivable" and "payable" account balances on the Statement of Financial Position which were established through implementation of unconventional accounting procedures. Neither the IPA nor the Council were able to provide a compelling reason for this deviation.

According to accrual basis accounting (which conforms to GAAP), revenue is recorded when earned, and expenses are recorded when incurred. When revenue is recorded, a corresponding asset is recorded in a "receivables" account. This receivable remains until payment is received from the appropriate funding source. When an entity receives goods or services before payment, an expense is recorded and a corresponding liability is recognized through a "payables" account. In accrual accounting, receivables and payables are created to reflect the lag between when a revenue or expense is recorded and when a payment is received or disbursement made by an entity.

The Council uses cash basis accounting for daily operations because it is an easier way to track revenue and expenses, in comparison to the more complex accrual basis. Under the cash basis of accounting, transactions are only recorded when there is a related change in cash. Since the Council uses cash basis accounting, there is no lag between payments (i.e., disbursements or receipts) and the recording of expenses or revenues. Accordingly, the creation of "receivable" or "payable" accounts is not necessary.

We were informed by the Council and the IPA that, despite operating on a cash basis of accounting, the Council uses "receivable" and "payable" accounts to track regrants. However, these receivables and payables are not created to correspond with the recording of revenues or expenses. Regrant expenses are recorded when a payment is disbursed by the Council and revenue is recorded when the Council receives a payment from a funding source. On a monthly basis, the Council adjusts the "Regrants payable" account to reflect the cumulative total of regrant funds awarded, from all funding sources, but not yet paid to the recipient. A corresponding adjustment is also recorded to a "Grants receivable" account.

According to the Council's Operations/Financial Officer, the bookkeeping at the Council has been done the same way for many years. The Council only uses the "Regrants payable" and "Grants receivable" accounts to track total funds obligated for regrants. This practice does not conform to generally accepted accounting principles. The nature of the respective accounts would best be described as budgetary accounts, and budgetary accounts should not be included on the Statement of Financial Position.

³ OMB Circular A-133 (Audits of States, Local Governments and Non-Profit Organizations) states that the IPA should provide "an opinion (or disclaimer of opinion) as to whether the financial statements are presented fairly in all material respects in conformity with generally accepted accounting principles and an opinion (or disclaimer of opinion) as to whether the schedule of expenditures of Federal awards is presented fairly in all material respects in relation to the financial statements taken as a whole." (OMB A-133; Subpart E – Auditors; §____.505).

The unconventional use of the “Regrants payable” and “Grants receivable” accounts by the Council and presentation of the respective account balances on the Statement of Financial Position result in a material deviation from GAAP. Since the IPA issued an unmodified opinion that the Council’s financial statements present fairly, in all material respects, the financial position of the Council and the changes in its net assets and its cash flows in accordance with accounting principles generally accepted in the United States of America, the IPA’s opinion is misleading. Such opinion facilitates the assumption by a reasonable person that the account balances on the Statement of Financial Position were determined in conformance with the accrual basis of accounting; and, the receivable and payable account balances are reflected in the expense and revenue totals provided in the Statement of Activities. This belief may be further reinforced by the following note to the financial statements:

The Council certifies the application and requests the grant funds from the National Endowment for the Humanities, the Winthrop Rockefeller Foundation, the Arkansas History Commission and other grantors, creating a receivable equal to the regrants payable to subrecipients for expenses incurred. Additionally, the Council is reimbursed under its grant agreements for costs incurred for administration and service to the field.⁴

This note implies a relationship between the “Grants receivable” account balance and “regrants payable to subrecipients for expenses incurred.” When in fact, the “Grants receivable” account balance does not reflect regrant expenses, only outstanding regrant obligations. The process of recognizing regrant expenses in the Council’s accounting system takes place independently from the monthly adjustments to the “Regrants payable” and “Grants receivable” account balances; and changes to the “Regrants payable” and “Grants receivable” account balances have no effect on expense or revenue accounts.

Arkansas Humanities Council’s Compliance with Federal Reporting Requirements

In addition to determining whether the Council’s financial statements are presented fairly in all material respects, in accordance with generally accepted accounting principles, OMB Circular A-133 also requires the IPA to determine whether the Council has complied with Federal statutes, regulations, and the terms and conditions of Federal awards that may have a direct and material effect on each of its major programs. Compliance testing must include tests of transactions and other auditing procedures necessary to support the IPA’s opinion on compliance.

The Council is required by the NEH *General Terms and Conditions for General Support Grants to State Humanities Councils* to submit to the NEH an annual and Final Federal Financial Report, SF425 (FFR) within 90 days after the completion date of the respective reporting period. The FFR is used as a standardized format to report expenditures as well as Federal cash status. OMB Circular A-110 requires such reporting to be substantiated by the Council’s accounting records.

We ascertained the IPA’s testing procedures related to Federal financial reporting. According to the IPA, the FFRs submitted to the NEH on January 29, 2015⁵ were “compared to the client’s FSRs⁶ included as supplemental information in the back of the client’s audited financial statements.” The IPA agreed the FSRs to worksheets prepared by the Council. The IPA further asserted, and we

⁴ Note 2: Grants Receivable (Page 8 of the FY2014 Financial Statements)

⁵ The annual FFRs covered the reporting period ending October 31, 2014.

⁶ Financial Status Reports (FSRs) covered the period November 1, 2013 to October 31, 2014.

verified, that the Federal share of net outlays identified in the supplemental FSRs matches Federal expenditures reflected in the FY 2014 SEFA⁷.

On the contrary, during the course of our desk review, we noted discrepancies in FY2014 Federal expenditure amounts certified in the FFRs submitted to the NEH on January 29, 2015, as compared to the audited FY 2014 SEFA and the supplemental FSRs, (see chart below).

CFDA No.	Grant Number	FY 2014 Expenditures		Variance
		Per SF 425	Per Audited SEFA/FSRs	
		(a)	(b)	(a – b)
45.129	SO-50404-11	\$143,112 *	\$88,462	\$54,650
45.129	SO-50582-14	\$545,817	\$553,135	(\$7,318)

* The SF 425s submitted to the NEH reflect Federal Share of Expenditures on a cumulative basis. Therefore, Federal Share of Expenditures reported for FY 2014 were calculated by subtracting Federal Share of Expenditures reported via the SF425 for the period ended October 31, 2013 (\$1,635,522) from Federal Share of Expenditures reported via the SF425 for the period ended October 31, 2014 (\$1,778,634).

The IPA issued an unmodified opinion concerning the Council’s compliance with the requirements described in the OMB Circular A-133 *Compliance Supplement* that could have a direct and material effect on its major Federal program for the year ended October 31, 2014, and no written findings were issued. It is not clear whether the impact of the discrepancies identified during or desk review is properly represented in the FY2014 OMB Circular A-133 reporting package, as issued by the IPA.

As the Council’s oversight agency, NEH will not accept this single audit report submission until the above deficiencies are addressed and corrective action taken to include the resubmission of the single audit reporting package to the FAC. Please contact FAC support staff for assistance with the single audit resubmission process since special procedures must be followed, (800-253-0696 or govvs.fac@census.gov).

The material deviation from GAAP, as effected by the presentation of non-accrual based “receivable” and “payable” account balances on the Statement of Financial Position, and the unidentified reporting discrepancies are troubling. Accordingly, we expect the IPA to strengthen their audit testing procedures to ensure that all elements of the Council’s single audit reporting package submitted to the FAC are in compliance with all OMB Circular A-133 requirements. To document this process, we expect Council management to provide the OIG with a written corrective action plan regarding the noted deficiencies within 30 days of receipt of this letter.

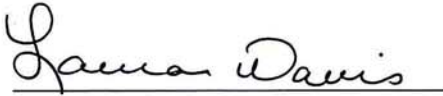
Please be advised that we are sending a copy of this letter to the Director at BKD, LLP to inform him of the results of our review.

⁷ The IPA asserts in the FY2014 OMB Circular A-133 reporting package that information presented in the SEFA compares and reconciles directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves. Accordingly, the IPA concluded and issued an opinion that the SEFA is fairly stated in all material respects in relation to the basic financial statements as a whole.

Letter to the Board of Directors
August 2, 2016
Page 5

If you have any questions concerning this letter or need accounting assistance, please contact Mr. Daniel M. Gelfand at (202) 606-8353 or via email at dgelfand@neh.gov.

Sincerely,



Laura Davis
Inspector General

Distribution List:

Auditor:

██████████, Director
BKD, LLP
Certified Public Accountants & Advisors
400 West Capitol Avenue, Suite 2500
Little Rock, AR 72203