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and which was in use in the affected project area or areas.

[Amdt. 188, 45 FR 85702, Dec. 30, 1980, as amended by Amdt. 342, 59 FR 2733, Jan. 19, 1994]

§ 277.17 Audit requirements.

(a) *General.* This section sets forth the audit requirements for State agencies that receive FNS program funds. Audits shall be conducted on an organization-wide basis. Such audits are to determine whether:

- (1) Financial operations are conducted properly;
- (2) The financial statements are presented fairly;
- (3) The organization has complied with laws and regulations affecting the expenditure of Federal funds;
- (4) Internal procedures have been established to meet the objectives of federally assisted programs; and
- (5) Financial reports to the Federal Government contain accurate and reliable information.

Except where required by law, no additional requirements for audit will be imposed by FNS unless approved by the Office of Management and Budget (OMB). The provisions of this section do not limit the authority of FNS to make audits of State agencies, their subdivisions, and subcontracts. However, if independent audits arranged for by State agencies meet the requirements prescribed herein, FNS shall rely on them, and any additional audit work already done.

(b) *Audit standards.* (1) State agencies shall use their own procedures to arrange for independent audits, and to prescribe the scope of audits, provided that the audits comply with the requirements set forth in this section. Where contracts are awarded for audit services, the contracts shall include a reference to OMB Circular A-102, Attachment P.

(2) Audits shall be made in accordance with the General Accounting Office "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions, the Guidelines for Financial and Compliance Audits of Federally Assisted Program," and any compliance supplements approved by OMB, and generally accepted auditing standards established by the American

Institute of Certified Public Accountants.

(c) *Purpose of audit.* Audits will include, at a minimum, an examination of the systems of internal control, systems established to ensure compliance with laws and regulations affecting the expenditure of Federal funds, financial transactions and accounts, and financial statements and reports of State agencies. These examinations are to determine whether:

- (1) There is effective control over and proper accounting for revenues expenditures, assets, and liabilities.
- (2) The financial statements are presented fairly in accordance with generally accepted accounting principles.
- (3) The Federal financial reports (including Financial Status Reports, Cash Reports, and claims for advances and reimbursements) contain accurate and reliable financial data; and are presented in accordance with the terms of applicable agreements, and in accordance with Attachment H of OMB Circular A-102.
- (4) Federal funds are being expended in accordance with the terms of applicable agreements and those provisions of Federal law or regulations that could have a material effect on the financial statements or on the awards tested.

(d) *Audit coverage.* A representative number of charges to Federal funds shall be tested. The test shall be representative of:

- (1) The universe of Federal funds received, and
- (2) All cost categories that materially affect the award. The test is to determine whether the charges:
 - (i) Are necessary and reasonable for the proper administration of the program;
 - (ii) Conform to any limitations or exclusions in the award;
 - (iii) Were given consistent accounting treatments and applied uniformly to both federally assisted and other activities of the State agency;
 - (iv) Were net of applicable credits;
 - (v) Did not include costs property chargeable to other federally assisted programs;
 - (vi) Were properly recorded (i.e., correct amount, date) and supported by source documentation;

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(vii) Were approved in advance, if subject to prior approval in accordance with Financial Management Circular 74-4;

(viii) Were incurred in accordance with competitive purchasing procedures, if covered by OMB Circular A-102, Attachment O; and

(ix) Were allocated equitably to benefiting activities, including non-Federal activities.

(3) Audits usually will be made annually, but not less frequently than every two years.

(4) If the auditors become aware of irregularities in the State agency, sub-agency or subcontractor, the auditor shall promptly notify the cognizant agency and State agency management officials above the level of involvement. Irregularities include such matters as conflict of interest, falsification of records or reports, and misappropriation of funds and other assets.

(e) *Audit report.* The audit report shall include:

(1) Financial statements, including footnotes, of the State agency, sub-agency, or subcontractor organization.

(2) The auditor's comments on the financial statements which should:

(i) Identify the statements examined and the period covered.

(ii) Identify the various programs under which the organization received Federal funds, and the amounts received for each program.

(iii) State that the audit was done in accordance with paragraph (d) of this section.

(iv) Express an opinion as to whether the financial statements are fairly presented in accordance with generally accepted accounting principles. If an unqualified opinion cannot be expressed, state the nature of the qualification.

(3) The auditor's comments on compliance and internal control which should:

(i) Include comments on weaknesses in and noncompliance with the systems of internal control, separately identifying material weaknesses.

(ii) Identify the nature and impact of any noted instances of noncompliance with the terms of agreements and those provisions of Federal law or regulation that could have a material effect

on the financial statements and reports.

(iii) Contain an expression of positive assurance with respect to compliance with requirements for tested items, and negative assurance for untested items.

(4) Comments on the accuracy and completeness of financial reports and claims for advances or reimbursements to Federal agencies.

(5) Comments on corrective action taken or planned by the State agency.

(f) *Record retention.* Work paper and reports shall be retained for a minimum of three years from the date of the audit report unless the auditor is notified in writing by the cognizant agency of the need to extend the retention period. The audit workpapers shall be made available upon request to the cognizant agency or its designees and the General Accounting Office or its designees.

(g) *Cognizant agency responsibilities.* The cognizant agency shall have the following responsibilities:

(1) Obtain or make quality assessment reviews of the work of non-Federal audit organizations, and provide the results to other interested audit agencies. If a non-Federal audit organization is responsible for audits of State agencies that have different cognizant audit agencies, a single quality assessment review will be arranged.

(2) Assure that all audit reports of State agencies that affect federally assisted programs are received, reviewed, and distributed to appropriate Federal audit officials. These officials will be responsible for distributing audit reports to their program officials.

(3) Whenever significant inadequacies in an audit are disclosed, the State agency will be advised and the auditor will be called upon to take corrective action. If corrective action is not taken, the cognizant agency shall notify the State agency and Federal awarding agencies of the facts and its recommendation. Major inadequacies or repetitive substandard performance of independent auditors shall be referred to appropriate professional bodies.

(4) Assure that satisfactory audit coverage is provided in a timely manner and in accordance with the provisions of this section.

(5) Provide technical advice and act as a liaison between Federal agencies, independent auditors and State agencies.

(6) Maintain a followup system on audit findings and investigative matters to assure that audit findings are resolved.

(7) Inform other affected audit agencies of irregularities uncovered. The audit agencies, in turn, shall inform all appropriate officials in their agencies. State or local government law enforcement and prosecuting authorities shall also be informed of irregularities within their jurisdiction.

(8) Recipients shall require subrecipients that are local governments of Indian tribal governments to adopt the requirements in paragraphs (d) through (f) of this section. The recipient shall ensure that the subrecipient audit reports are received as required, and shall submit the reports to the cognizant agency. The cognizant agency will have the responsibility for those reports described in paragraph (g) of this section.

§ 277.18 Establishment of an Automated Data Processing (ADP) and Information Retrieval System.

(a) *Scope and application.* This section establishes conditions for initial and continuing authority to claim Federal financial participation (FFP) for the costs of the planning, development, acquisition, installation and implementation of ADP equipment and services used in the administration of the Food Stamp Program. Due to the nature of the procurement of ADP equipment and services, current State agency approved cost allocation plans for ongoing operational costs shall not apply to ADP system development costs under this section unless documentation required under paragraph (c) of this section is submitted to and approvals are obtained from FNS.

(b) *Definitions:*

Acceptance Documents means written evidence of satisfactory completion of an approved phase of work or contract,

and acceptance thereof by the State agency.

Advance Planning Document for Project Implementation or *Implementation APD* means a written plan of action requesting Federal financial participation (FFP) to acquire and implement ADP services and/or equipment.

Advance Planning Document for Project Planning or *Planning APD* means a brief written plan of action that requests FFP to accomplish the planning necessary for a State agency to determine the need for and plan the acquisition of ADP equipment and/or services, and to acquire information necessary to prepare an Implementation APD.

Advance Planning Document Update (APDU) means an annual self-certification by the State agency on the status of project development activities and expenditures in relation to the approved Planning APD or Implementation APD. An APDU may also be submitted as needed to request funding approval for project continuation whenever significant project changes occur or are anticipated.

Automated Data Processing or *ADP* means data processing performed by a system of electronic or electrical machines so interconnected and interacting as to minimize the need for human assistance or intervention.

Automated Data Processing Equipment or *hardware* means:

(1) Electronic digital computers, regardless of size, capacity, or price, that accept data input, store data, perform calculations, and other processing steps, and prepare information;

(2) All peripheral or auxiliary equipment used in support of electronic digital computers whether selected and acquired with the computer or separately;

(3) Data transmission or communications equipment that is selected and acquired solely or primarily for use with a configuration of ADP equipment which includes an electronic digital computer; and

(4) Data input equipment used to enter directly or indirectly into an electronic digital computer, peripheral or auxiliary equipment, or data transmission, or communication equipment.

Automated Data Processing Services means: