

**MEMORANDUM REPORT ON REVIEW OF  
BIG SANDY TELECOMMUTING SERVICES, INC.  
PIKEVILLE, KENTUCKY**

**Big Sandy Telecommunications Center  
Phase I**

**ARC Grant No.: KY-12014-95-I-302-0327**

**January 1, 1995 through December 31, 1997**

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**Report Number: 98-41(H)**

**Date: April 17, 1998**

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Prepared By:  
Tichenor & Associates  
Certified Public Accountants  
Woodbridge, Virginia

Under Contract Number J-9-G-5-0010 with the  
U.S. Department of Labor  
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Office of Audit

# TICHENOR & ASSOCIATES

CERTIFIED PUBLIC ACCOUNTANTS and MANAGEMENT CONSULTANTS

WASHINGTON OFFICE  
12531 CLIPPER DRIVE SUITE 202  
WOODBIDGE VA 22192

PARTNERS

WILLIAM R. TICHENOR  
JONATHAN D. CROWDER  
JAMES M. ANDERSON

BUSINESS: (703) 490-1004  
METRO: (703) 352-1417  
FAX: (703) 491-9426  
E-MAIL: TICHASSOC@AOL.COM

TO: Appalachian Regional Commission (ARC)  
Office of Inspector General (OIG)

FROM: Tichenor & Associates  
Woodbridge, Virginia

REPORT FOR: The Federal Co-Chairman  
ARC Executive Director  
OIG Report No. 98-41(H)

SUBJECT: Memorandum Review Report on Big Sandy Telecommuting Services,  
Inc., Pikeville, Kentucky. Grant No.: KY-12014-95-I-302-0327; ARC  
Contract No. 95-105.

PURPOSE: The purpose of our review was to determine if (a) the total funds claimed for reimbursement by the Big Sandy Telecommuting Services, Inc., for the Big Sandy Telecommunications Center, Phase I, were expended in accordance with the ARC-approved grant budget and did not violate any restrictions imposed by the terms and conditions of the grant; (b) the accounting, reporting and internal control systems provided for disclosure of pertinent financial and operating information; and, (c) the objectives of the grant had been met.

BACKGROUND: ARC awarded Grant Number KY-12014-95-I-302-0327 to the Big Sandy Telecommuting Services, Inc. (the Grantee) for the period January 1, 1995 through December 31, 1996. Total project costs were estimated at \$174,114, of which total ARC funding was not to exceed \$100,000, or 57 percent of actual, reasonable and eligible project cost, whichever was less. ARC required that the grant be matched with \$74,114, or 43 percent in cash, contributed services, or in-kind contributions, as approved by ARC. On January 2, 1997, the grant was amended, extending the period through December 31, 1997, and increasing the total project costs to \$487,714, of which total ARC funding was not to exceed \$300,000, or 62 percent of actual, reasonable, and eligible project cost, whichever was less. ARC required that

the grant be matched with \$187,714 or 38 percent in cash, contributed services, or in-kind contributions as approved by ARC. ARC made payments to the Grantee, as follows:

Payment Date	Payment Amount
01/31/96	\$ 29,616.80
04/05/96	17,578.08
06/13/96	22,715.56
09/16/96	19,126.07
09/26/96	10,963.49
01/08/97	100,000.00
05/19/97	50,000.00
12/09/97	30,000.00
01/06/98	15,000.00
Total	\$295,000.00

The funds from this grant were to provide support to establish and equip a telecommunications center in Pikeville, Kentucky to provide telecommunications services, including but not limited to, training in computer applications, conducting demonstration programs, establishing a community bulletin board, and providing technical support to businesses and individuals.

SCOPE: We performed a program review of the grant project as described in the Purpose, above. Our reviewed covered the time period of January 1, 1995 through December 31, 1997. We based our review on the terms of the grant agreement and on the application of certain agreed-upon procedures previously discussed with the ARC OIG. Specifically, we determined if the specific tasks listed above had been performed, if the accountability over ARC funds was sufficient as required by the applicable Office of Management and Budget (OMB) Circulars, and if the Grantee had complied with the requirements of the grant agreement. In addition, we discussed the program objectives and performance with the Grantee. Our results and recommendations are based on those procedures.

RESULTS: The following results were based on our review performed at the Grantee's offices in Pikeville, Kentucky on April 16 through 17, 1998.

**A. Incurred Costs**

The Grantee reported program costs of \$646,718, of which they claimed direct reimbursable costs from January 1, 1995 through December 31, 1997 of \$300,000 and in-kind costs of \$187,714. We reviewed the direct and in-kind costs reported and determined that \$228,989 of the incurred costs were not allowable or unsupported in accordance with the terms of the grant and applicable OMB Circulars. These costs are discussed below.

1. Program Income Was Not Offset Against Expenses

The Grantee collected program income of \$210,647 from Internet access fees (\$205,594), skills training classes (\$4,641) and video conferencing (\$412). This income, generated from the use of equipment and services purchased under the grant, was not used to offset ARC program expenses.

ARC General Contract Provisions, Article G4, Contract Related Income states:

“Pursuant to Section 18-7.3 of the ARC Code, contract-related income must be used to reduce the ARC grant amount unless the ARC specifically approves the expenditure of such contract-related income to expand project services”

RECOMMENDATION:

We recommend that the ARC require the Grantee to offset total expenditures by the program income and recalculate ARC’s portion of the total grant funding. If ARC approves the use of program income to further the project, the Grantee should document and support the use of funds.

2. Unallowable Entertainment Expenses

The Grantee held a grand opening to celebrate the opening of the communications center. They incurred \$736 for food and other supplies related to this event. These expenses are not necessary for the accomplishment of the grant objectives and are unallowable.

OMB Circular A-122, Attachment B, Paragraph 12, Entertainment Costs states:

“Costs of amusement, diversion, social activities, ceremonials, and costs relating thereto, such as meals, lodging, rentals, transportation and gratuities are unallowable.”

### 3. Unsupported Expenses

The Grantee had unsupported expenditures totaling \$11,922, as follows:

- \$4,460 to Waltrip & Associates, a consulting firm that assisted the Grantee in establishing business plan.
- \$7,462 on the corporate credit card.

The Grantee could not supply an invoice to support the payment to Waltrip & Associates. They also could not supply sufficient documentation for the credit card purchases in order to enable us to determine the allowability of the expenses.

OMB Circular A-122, Attachment A, Section A, Paragraph 2, Factors affecting allowability of costs states:

“To be allowable under an award, costs must meet the following criteria:

- b. Conform to any limitations or exclusions set forth in these principles or in the award as to types or amounts of costs items
- g. Be adequately documented.”

### 4. Interest Expense Included in Total Costs

The Grantee included, as part of total project costs, payments to Pikeville National Bank and Community Trust Bank. These payments were interest payments on loans used to establish the corporation. Interest expense identified totalled \$684.

OMB Circular A-122, Attachment B, Paragraph 19, Interest, fund raising, and investment management costs, states:

“a. Costs incurred for interest on borrowed capital or temporary use of endowment funds, however represented, are not allowable”

### 5. Principal Payment on a Loan Included in Total Costs

The Grantee included, as part of the total project costs, a \$5,000 payment to the Pikeville National Bank. This payment was a principal payment on a loan used to establish the corporation.

OMB Circular A-122, Attachment A, Composition of total costs states:

“The total cost of an award is the sum of the allowable direct and allocable indirect costs less any applicable credits.”

RECOMMENDATION:

We recommend that the above-mentioned unallowable and unsupported costs be removed from the total allowable costs and that the Grantee recalculate its total ARC funding

**B. Internal Controls**

We determined that the Grantee had the following internal control weaknesses which affected the accountability of costs or compliance with the terms of the grant. These weaknesses were such that the accounting system is inadequate to properly account for complete use of grant funds.

1. Insufficient Controls Over Reasonableness, Allocability and Allowability of Costs.

The Grantee did not have written procedures to determine reasonableness, allowability, or allocability of costs to a project in accordance with the applicable Federal cost principles and the conditions of the award. The Grantee maintains a manual general ledger. However, this ledger was only complete for the period ending June 1996. Accounting information for the last two quarters of 1996 to support the amounts claimed was not available. In addition, costs claimed in 1997 were claimed based on the cash advance amounts.

Although the Grantee was able to provide some support that expenditures were made under the grant (checks and county payroll records), these costs did not support the amounts claimed for reimbursement and included many unallowable costs.

In addition, the Grantee does not have written policies and procedures covering personnel or travel issues or the accounting function.

OMB Circular A-110, Section .21, Standards for financial management systems, paragraph (b) (6), states:

“Recipients’ financial management systems shall provide for the following.

- (6) Written procedures for determining the reasonableness, allocability and allowability of costs in accordance with the provisions of the applicable Federal cost principles and the terms and conditions”

RECOMMENDATION:

We recommend that the Grantee establish and implement policies to determine the allowability of expenses and to maintain documentation in sufficient detail to support those determinations.

2. Inability to Identify the Source and Use of Federal Funds

The Grantee did not maintain records that segregated Federal funds from other funds. When a report was submitted, the Grantee attempted to identify the expenditures relating to the federal award, however, the information was not maintained in sufficient detail as to allow clear determination as to which expenses on their general ledger related to the grant. Only after an employee identified individual expenses that they thought belonged to the grant could an estimate of the actual grant expenses be made.

OMB Circular A-110, Section .21, Standards for financial management systems, paragraph (b) (2) states:

“Recipients’ financial management systems shall provide for the following:

- (2) Records that identify adequately the source and application of funds for federally-sponsored activities. These records shall contain information pertinent to Federal awards, authorizations, obligations, unobligated balances, assets, outlays, income and interest.”

RECOMMENDATION:

We recommend develop and implement procedures to clearly that the Grantee maintain funds from Federal sources separate from its other operating funds.

3. No Comparisons of Budget to Actual

The expenditure information that the Grantee maintained was a listing of expenditures by payee. From this information, the type of expense (such as supplies or travel) could not always be determined. Because they could not identify expenditures by budget category, the Grantee could not perform budget to actual comparisons to determine that the grant was



being expended in accordance with the approved ARC budget.

OMB Circular A-110, Section .21, Standards for financial management systems, paragraph (b) (4), states:

“Recipients’ financial management systems shall provide for the following...

(4) Comparison of outlays with budget amounts for each award.:

RECOMMENDATION:

We recommend that the Grantee establish an accounting system to allow them to summarize expenditures by category and to compare these expenditures to budgeted amounts.

4. Incomplete Equipment Inventory

The equipment inventory maintained by the Grantee for equipment purchased using Federal funds was incomplete. The list supplied included a description of the equipment, the serial and model numbers, but did not include items such as acquisition date, unit acquisition cost, source of funding for the equipment, or condition of the equipment.

OMB Circular A-110, Section .34, Equipment, paragraph (f) (1), states:

“Equipment records shall be maintained accurately and shall include the following information...

(iii) Source of the equipment, including the award number.

(v) Acquisition date and cost.

(vii) Location and condition of the equipment and the date the information was reported

(viii) Unit acquisition costs.”

RECOMMENDATION:

We recommend that the Grantee update its inventory to include missing information.

5. Final Report Not Prepared and Submitted

The Grantee has not yet prepared a final financial or progress report for submission to the ARC. As such, the ARC is withholding the final payment until the reports are submitted.

Grant Agreement 95-105, Article 2, Section 10.1, Final Reports states:

“Within one (1) month after the period of performance, Grantee shall prepare and submit to the ARC Project Coordinator for approval, three copies of a draft final report of all work accomplished under this agreement including recommendations and conclusions based on the experience and results obtained.”

RECOMMENDATION:

We recommend that the Grantee prepare and submit the final report to the ARC.

**C. Program Results**


The Grantee has achieved all of the specific tasks and objectives identified in the grant, as summarized above.

DISCUSSION:

We discussed these issues with the Grantee's management during an exit conference held on April 17, 1998. Management generally agreed with the findings and recommendations.

OTHER:

We provided the Grantee with a copy of the draft review report on August 10, 1998. The Grantee did not provide any written or oral comments to the findings and recommendations contained in the report. Therefore, no changes to the findings or recommendations have been made subsequent to the draft report.

  
TICHENOR & ASSOCIATES  
Woodbridge, Virginia