



# OFFICE OF INSPECTOR GENERAL

## U.S. ENVIRONMENTAL PROTECTION AGENCY

CUSTOMER SERVICE ★ INTEGRITY ★ ACCOUNTABILITY

### *Compliance with the law*

## The EPA Was Not Compliant with the Payment Integrity Information Act for Fiscal Year 2021

Report No. 22-P-0050

June 27, 2022

FY 2021 reporting



Allowability of costs



Improper grant payments



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**Abbreviations:**

AFR	Agency Financial Report
C.F.R.	Code of Federal Regulations
EPA	U.S. Environmental Protection Agency
FY	Fiscal Year
OCFO	Office of the Chief Financial Officer
OIG	Office of Inspector General
OMB	Office of Management and Budget
PIIA	Payment Integrity Information Act of 2019
SOP	Standard Operating Procedure

**Key Definitions:** Please see Appendix A for key definitions.

**Cover Image:** Payments for unallowable expenses are improper payment dollars.  
(EPA OIG image)

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# Office of Inspector General U.S. Environmental Protection Agency **At a Glance**

22-P-0050  
June 27, 2022

## Why We Did This Audit

The Office of Inspector General conducted this audit to determine whether the U.S. Environmental Protection Agency met the requirements of the Payment Integrity Information Act of 2019 as they relate to the formulation and inclusion of payment integrity information in the *Fiscal Year 2021 Agency Financial Report* and accompanying materials.

The Payment Integrity Information Act of 2019 requires inspectors general to determine and report their agencies' compliance with the Act every fiscal year. The Act also requires the heads of each agency to periodically review and identify all programs and activities with costs exceeding the \$10-million statutory threshold that may be susceptible to significant improper payments. Prior to fiscal year 2021, the EPA had designated its grants payments as susceptible to significant improper payments.

### This audit supports EPA mission-related efforts:

- *Compliance with the law.*
- *Operating efficiently and effectively.*

### This audit addresses a top EPA management challenge:

- *Managing infrastructure funding and business operations.*

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[List of OIG reports.](#)

## ***The EPA Was Not Compliant with the Payment Integrity Information Act for Fiscal Year 2021***

### What We Found

The EPA was not compliant with the Payment Integrity Information Act of 2019 because the Agency did not adhere to all of the Office of Management and Budget improper payment reporting requirements for fiscal year 2021. Specifically, the EPA did not adequately conclude whether its programs with annual outlays greater than \$10 million were likely to make improper payments above or below the statutory threshold.

**The EPA needs to implement appropriate control measures to better identify and reduce the risk of its improper payments.**

The EPA divides its expenditures into ten payment streams, eight of which have annual outlays greater than \$10 million. In fiscal year 2021, with respect to the grants payment stream, while the Agency reviewed payments to determine the error rate and estimate the value of improper payments, it did not incorporate the cost-allowance principles set forth in 2 C.F.R. part 200, subpart E. This oversight occurred because the Office of the Chief Financial Officer's *Standard Operating Procedure Grants Improper Payment Review*, which was updated in September 2021, was not completed in time to use for the fiscal year 2021 risk assessment. The standard operating procedure is intended to be used to review the allowability of grant payments. For the remaining seven payment streams with outlays greater than \$10 million, the EPA did not establish an adequate methodology for determining risk-assessment attributes and results.

The Agency may not have reported approximately \$10.3 million in improper payments—of which approximately \$8.6 million may be subject to recovery—because it did not apply the cost-allowance principles in the Agency's review of grants payments. Further, because the EPA has not established an adequate methodology for risk assessments, the Agency's risk-assessment process does not provide reasonable assurance that payment streams are not susceptible to improper and unknown payments above the statutory threshold or, in other words, are susceptible to significant improper payments.

### Recommendations and Planned Agency Corrective Actions

We make four recommendations to the chief financial officer, which address reviewing the OIG-identified questioned costs, determining the payment allowability, recovering costs and recalculating the error rate, conducting an off-cycle risk assessment, updating applicable standard operating procedures, and training Agency personnel on the application of cost principles. The EPA agreed with our recommendations and provided an acceptable corrective action for one recommendation. However, it did not provide acceptable corrective actions for the remaining three recommendations. Recommendation 3 is resolved with corrective actions pending. Recommendations 1, 2, and 4 remain unresolved.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY  
WASHINGTON, D.C. 20460

THE INSPECTOR GENERAL

June 27, 2022

**MEMORANDUM**

**SUBJECT:** The EPA Was Not Compliant with the Payment Integrity Information Act  
for Fiscal Year 2021  
Report No. 22-P-0050

**FROM:** Sean W. O'Donnell

A handwritten signature in blue ink, reading "Sean W O'Donnell", is placed next to the "FROM:" field.

**TO:** Faisal Amin, Chief Financial Officer

This is our report on the subject audit conducted by the Office of Inspector General of the U.S. Environmental Protection Agency. The project number for this audit was [OA-FY22-0028](#). This report contains findings that describe the problems the OIG has identified and corrective actions the OIG recommends. Final determinations on matters in this report will be made by EPA managers in accordance with established audit resolution procedures.

The Office of the Chief Financial Officer is responsible for the issues discussed in this report. In accordance with EPA Manual 2750, your office provided an acceptable planned corrective action and estimated milestone date for Recommendation 3. This recommendation is resolved. A final response pertaining to this recommendation is not required; however, if you submit a response, it will be posted on the OIG's website, along with our memorandum commenting on your response.

**Action Required**

Recommendations 1, 2, and 4 are unresolved. EPA Manual 2750 requires that recommendations be resolved promptly. Therefore, we request that the EPA provide us within 60 days its responses concerning specific actions in process or alternative corrective actions proposed on the recommendations. Your response will be posted on the OIG's website, along with our memorandum commenting on your response. Your response should be provided as an Adobe PDF file that complies with the accessibility requirements of Section 508 of the Rehabilitation Act of 1973, as amended. The final response should not contain data that you do not want to be released to the public; if your response contains such data, you should identify the data for redaction or removal along with corresponding justification. The Inspector General Act of 1978, as amended, requires that we report in our semiannual reports to Congress on each audit or evaluation report for which we receive no Agency response within 60 calendar days.

We will post this report to our website at [www.epa.gov/oig](http://www.epa.gov/oig).

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# Chapter 1

## Introduction

### Purpose

The U.S. Environmental Protection Agency’s Office of Inspector General [initiated](#) this audit to determine whether the EPA met the requirements of the Payment Integrity Information Act of 2019, or PIIA, as they relate to the formulation and inclusion of payment integrity information in the *Fiscal Year 2021 Agency Financial Report*, or AFR, and accompanying materials.

#### Top Management Challenge Addressed

This audit addresses the following top management challenge for the Agency, as identified in OIG Report No. [22-N-0004](#), *EPA’s Fiscal Year 2022 Top Management Challenges*, issued November 12, 2021:

- Managing infrastructure funding and business operations.

### Background

To improve efforts to identify and reduce governmentwide improper payments, Congress enacted the PIIA on March 2, 2020. The PIIA repealed and replaced several related acts, including the:

- Improper Payments Information Act of 2002.
- Improper Payments Elimination and Recovery Act of 2010.
- Improper Payments Elimination and Recovery Act of 2012.
- Fraud Reduction and Data Analytics Act of 2015.

As noted in the PIIA, agencies must implement the Act’s requirements in accordance with the guidance that the Office of Management and Budget, or OMB, set forth and provided in Appendix C to OMB Circular A-123, *Management’s Responsibility for Internal Control*, which is also titled OMB Memorandum M-21-19, *Requirements for Payment Integrity Improvement*. The March 2021 revision of Appendix C outlined ten specific requirements related to the PIIA that agencies had to implement in fiscal year 2021 to be in compliance with the Act. We detail these ten requirements in the “PIIA Compliance Table” section later in this chapter.

The PIIA directs the head of each executive agency to periodically review all agency-administered programs and activities—hereafter referred to collectively as “programs”—with annual outlays greater than \$10 million, which is the statutory threshold set forth in the PIIA, and to identify those programs that may be susceptible to significant improper payments. Agency heads must conduct these periodic reviews, generally referred to as “risk assessments,” not less than once every three years. As described in Appendix C to OMB Circular A-123, these risk assessments can be either qualitative or quantitative but must reasonably determine whether a program is susceptible to

#### Improper and Unknown Payments

The PIIA defines an **improper payment** as “any payment that should not have been made or that was made in an incorrect amount, including an overpayment or underpayment, under a statutory, contractual, administrative, or other legally applicable requirement.”

An **unknown payment** is a payment that cannot be determined either proper or improper because of insufficient or lack of documentation.

significant improper payments. A quantitative risk-assessment reviews disbursements to formulate the overall estimated improper payment rate. A qualitative risk assessment may use questionnaire responses or other forms of data to identify the risk of improper payments.

Appendix C to OMB Circular A-123 states that a program is susceptible to significant improper payments if the total improper and unknown payment amount exceeds the statutory threshold. The statutory threshold for a program is either (1) both 1.5 percent of program outlays and \$10 million of all program payments made during the fiscal year or (2) \$100 million of estimated improper payments.

### ***Requirements for Programs Susceptible to Significant Improper Payments***

For programs that are deemed susceptible to significant improper payments, the OMB requires agencies to conduct statistically valid sampling-and-estimation quantitative risk assessments. The OMB further requires agencies to publish both improper and unknown payment estimates for these programs in the accompanying materials of the AFR. For agencies to achieve compliance, they must submit a *Sampling and Estimation Methodology Plan* to the OMB in the fiscal year following the one in which the program in question was deemed likely to be susceptible to improper payments.

To be compliant with the PIIA, agencies must report an improper and unknown payment estimate of less than 10 percent for each program for which an estimate was published in the accompanying materials of the AFR. Each program with an improper or unknown payment estimate above 10 percent is considered noncompliant with the PIIA.

### ***The EPA's Improper Payment Reporting***

The EPA has divided its programs into ten payment streams. Eight of the EPA's ten payment streams exceed \$10 million in annual outlays and are thus required to undergo risk assessments at least once every three years.

Beginning in its FY 2016 AFR, the Agency reported that one of those eight payment streams—the grants payment stream—was susceptible to significant improper payments. Since making that determination, the EPA annually conducted a sampling-and-estimation quantitative risk assessment for the grants payment stream to determine an error rate for and to estimate the total dollar value of improper and unknown payments.

In FY 2021, the EPA conducted the required sampling-and-estimation quantitative risk assessment for the grants payment stream, as well as a combination of quantitative and qualitative risk assessments for the seven other payment streams with outlays of over \$10 million. Based on these risk assessments, the EPA determined and subsequently reported in its FY 2021 [AFR](#) that none of the Agency's payment streams were susceptible to significant improper payments (Table 1). Accordingly, the EPA stated that it would not conduct any risk assessments again for three years, which would be in FY 2024.

Despite this determination, the EPA still reported information regarding the grants payment stream improper payments in its FY 2021 AFR. The AFR noted that the EPA gathered and finalized this improper payment information before determining that the grants payment stream was no longer susceptible to significant improper payments. Specifically, the Agency reported grants payment stream outlays of \$1.63 billion, grants payment stream improper payments of \$8.18 million, and grants payment stream unknown payments of \$8.15 million. Although the grants payment stream had total improper and unknown payments exceeding \$10 million, the grants payment stream was not deemed subject to



significant improper payments because it did not meet the additional statutory threshold of 1.5 percent of annual outlays.

**Table 1: EPA FY 2021 assessment of improper payment susceptibility**

Payment stream	Exceeds \$10 million in annual outlays?	Is susceptible to significant improper payments?
Commodities	Yes	No
Contracts	Yes	No
Clean Water State Revolving Fund	Yes	No
Drinking Water State Revolving Fund	Yes	No
Grants	Yes	No
Hurricane Sandy	Yes	No
Payroll	Yes	No
Purchase Cards	Yes	No
Travel	No	Not applicable
2018 Disaster Relief	No	Not applicable

Source: OIG analysis of data from the FY 2021 AFR. (EPA OIG table)

## The OIG's Payment Integrity Requirements

The PIIA requires each agency's inspector general to annually determine the agency's compliance with the PIIA and issue a report on that determination. Furthermore, Appendix C to OMB Circular A-123 requires that:

- Inspectors general evaluate the accuracy and completeness of their agencies' improper payments reporting.
- Agencies publish risk assessments at least once every three years for programs with outlays above \$10 million.
- OIGs evaluate the risk assessments to determine if they adequately conclude whether the program is likely to make improper and unknown payments above or below the statutory threshold.
- If an OIG determines that a risk assessment incorrectly identified whether a program or activity was likely to make improper and unknown payments above or below the statutory threshold, the OIG recommend changes to the agency's improper payment risk-assessment methodology. Such recommendations may include that the agency conduct an off-cycle risk assessment.

Appendix C also states that an agency, at its own discretion, may determine that it should undertake an off-cycle risk assessment for various reasons, including a significant increase in the funding level of a program.<sup>1</sup>

## Responsible Offices

The Office of the Chief Financial Officer, or OCFO, formulates the EPA's *Annual Budget and Performance Plan*; coordinates the EPA's strategic-planning efforts; develops the EPA's *Annual Performance Report*

<sup>1</sup> The Agency, because of an influx of appropriations from the Infrastructure Investment and Jobs Act, which was enacted November 15, 2021, will see a significant increase in funding for grant programs.



and AFR; implements the Government Performance and Results Act; provides financial services for the EPA; and makes payments to grant recipients, contractors, and other vendors. The OCFO is responsible for creating policies for, issuing reports on, and providing oversight of the EPA's financial operations. The Office of the Controller develops, manages, and supports the Agency's financial management by interpreting fiscal legislation, maintaining fiscal operations, and implementing governmentwide external reporting reforms.

## Scope and Methodology

We conducted this performance audit from November 2021 to May 2022 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We assessed the internal controls necessary to satisfy our audit objective.<sup>2</sup> In particular, we assessed the internal control components—as outlined in the U.S. Government Accountability Office's *Standards for Internal Control in the Federal Government*—significant to our audit objective. Any internal control deficiencies we found are discussed in this report. Because our audit was limited to the internal control components deemed significant to our audit objective, it may not have disclosed all internal control deficiencies that may have existed at the time of the audit. We assessed the control environment and risk assessments. Additionally, we assessed the Agency's activity against the OMB Circular A-123 Appendix C requirement that programs proactively manage their payment integrity risk to prevent improper and unknown payments. In combatting payment integrity risk, it is important to assess the Agency's controls and the control environment.

To determine whether the EPA complied with the PIIA, we reviewed the EPA's FY 2021 AFR and its accompanying materials. We also reviewed the Agency's Federal Managers' Financial Integrity Act assurance letters; standard operating procedures, or SOPs; and risk-assessment methodologies. We interviewed OCFO staff at EPA headquarters to obtain an understanding of the processes, procedures, and controls used for improper payment detection and reporting across the EPA. To test transactions, we used the Council of Inspectors General on Integrity and Efficiency's *Guidance for Payment Integrity Information Act Compliance Reviews*, dated October 2021.

In accordance with Appendix C to OMB Circular A-123, OIGs are required to evaluate and report whether their agencies are compliant with the PIIA. In FY 2021, the Agency conducted risk assessments for eight payment streams that exceeded outlays of \$10 million, as described in Table 1. While the EPA reported in its FY 2021 AFR that the grants payment stream was no longer susceptible to significant improper payments, the Agency still performed a quantitative risk assessment of the grants payment stream. Therefore, the OIG was required to evaluate that risk assessment to verify the Agency's determination that the grants payment stream was not susceptible to significant improper payments.

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<sup>2</sup> An entity designs, implements, and operates internal controls to achieve its objectives related to operations, reporting, and compliance. The U.S. Government Accountability Office sets internal control standards for federal entities in GAO-14-704G, *Standards for Internal Control in the Federal Government*, issued September 10, 2014. These standards are the foundation for establishing and maintaining internal control, as well as for identifying and addressing significant management challenges and areas at the greatest risk for fraud, waste, abuse, and mismanagement.

To evaluate this, we judgmentally selected 25 (roughly 10 percent) of the 240 grant payments that the EPA used to complete its risk assessment. We selected these 25 payments, which were made from October 2019 through March 2021, based on their inherent risk and dollar value. The 240 grant payments totaled \$24,362,536, and the 25 grant payments we reviewed totaled \$11,987,085—almost one-half of the value of the grants that the Agency reviewed. We reviewed these 25 payments and supporting documentation to identify any payment that that the Agency should not have made.

For the other seven payment streams with outlays over \$10 million, we measured the content of the completed assessments against the criteria for qualitative and quantitative assessments in Appendix C to OMB Circular A-123.

## Prior Reports

From 2019 to 2021, the OIG issued three reports—EPA OIG Report No. [21-P-0135](#), Report No. [19-P-0163](#), and Report No. [20-P-0167](#)—pertaining to the EPA’s compliance with the PIIA. In all three of those reports, we noted a significant deficiency in applying the cost principles to the Agency’s review process. Also, in OIG Report No. 21-P-0135, we recommended that the EPA revise the OCFO’s SOP for grants improper payment reviews, titled *Standard Operating Procedure Grants Improper Payment Review*, to include the cost-allowance principles set forth in 2 C.F.R. part 200, subpart E, in the EPA’s improper payment estimates for the grants payment stream and to provide training to staff on the updated SOP. The Agency agreed with our recommendations and proposed to (1) limit the cost-allowance principles to 2 C.F.R. §§ 200.402–200.411 and not the entirety of subpart E and (2) apply those C.F.R. provisions for risk assessments only when a program was designated susceptible to improper payments. The OIG concurred with the proposed corrective actions. According to the EPA, the OCFO revised the *Standard Operating Procedure Grants Improper Payment Review*, in September 2021, which was after the Agency conducted the FY 2021 improper payment risk assessments. Therefore, we did not evaluate the completeness of the corrective actions while reviewing the Agency’s FY 2021 compliance with the PIIA. As such, we did not determine whether the corrective action adequately included all cost principles that federally funded grantees must follow.

## PIIA Compliance Table

Appendix C to OMB Circular A-123 requires that each OIG report pertaining to PIIA compliance include a high-level summary that clearly states the agency’s overall compliance status. We determined that the EPA did not comply with the requirement to adequately conclude whether programs with annual outlays greater than \$10 million were likely to make improper and unknown payments above or below the statutory threshold. We determined that the EPA complied with five of the PIIA’s other nine requirements and that the other four requirements were not applicable. Table 2 summarizes our findings on PIIA compliance.

**Table 2: FY 2021 EPA PIIA compliance reporting table**

Compliance element	Payment stream							
	Commodities	Contracts	Clean Water SRF	Drinking Water SRF	Grants	Hurricane Sandy	Payroll	Purchase Card
1a. Published payment integrity information with the annual financial statement	✓	✓	✓	✓	✓	✓	✓	✓
1b. Posted the annual financial statement and accompanying materials on the agency website	✓	✓	✓	✓	✓	✓	✓	✓
2a. Conducted improper payment risk assessments for each program with annual outlays greater than \$10 million at least once in the last three years	✓	✓	✓	✓	✓	✓	✓	✓
2b. Adequately concluded whether the program is likely to make improper and unknown payments above or below the statutory threshold*	✗	✗	✗	✗	✗	✗	✗	✗
3. Published improper and unknown payments estimates for programs susceptible to significant improper payments in the accompanying materials to the annual financial statement	✓	✓	✓	✓	✓	✓	✓	✓
4. Published corrective action plans for each program for which an estimate above the statutory threshold was published in the accompanying materials to the annual financial statement	*	*	*	*	*	*	*	*
5a. Published improper and unknown payment reduction target for each program for which an estimate above the statutory threshold was published in the accompanying materials to the annual financial statement	*	*	*	*	*	*	*	*
5b. Demonstrated improvements to payment integrity or reached a tolerable improper and unknown payment rate	*	*	*	*	*	*	*	*
5c. Developed a plan to meet the improper and unknown payment reduction target	*	*	*	*	*	*	*	*
6. Reported an improper and unknown payment estimate of less than 10 percent for each program for which an estimate was published in the accompanying materials to the annual financial statement	✓	✓	✓	✓	✓	✓	✓	✓

Source: EPA FY 2021 AFR. (EPA OIG table)

\* Because the Purchase Card and Hurricane Sandy payment streams have significantly lower annual outlays, we acknowledge that the probability that improper and unknown payments are above the threshold for these streams is low. However, based on the Agency's inadequate methodologies, we cannot support the Agency's conclusions.

Legend:

✓ Complaint

✗ Noncompliant

\* Not Applicable

SRF State Revolving Fund

## **Chapter 2**

### **The EPA Needs to Improve Risk Assessments to Adequately Conclude Whether Program Improper and Unknown Payments Exceed the Compliance Threshold**

In FY 2021, the EPA was not compliant with one of the ten PIIA requirements under Appendix C to OMB Circular A-123; therefore, the Agency was not compliant with the PIIA. Specifically, we found that the EPA did not adequately conclude whether the EPA's eight payment streams with annual outlays greater than \$10 million were likely to make improper and unknown payments above or below the statutory threshold, as follows:

- For the grants payment stream, the Agency's improper payment procedures did not require the use of the cost-allowance principles in 2 C.F.R. part 200, subpart E, when determining whether a payment was improper.
- For the remaining seven payment streams, the EPA's risk assessments were insufficient because the EPA had not established an adequate methodology for determining risk-assessment attributes and results.

Because the Agency did not apply the cost-allowance principles when reviewing the allowability of payments for the grants payment stream, the Agency, which only reported \$89,000 in improper grant payments, should have potentially reported more than \$10.3 million in improper grant payments. This would mean that the Agency, which reported the improper payment rate to be 0.5 percent in its FY 2021 AFR, should have potentially reported that rate to be 21 percent. The Agency has recovered approximately \$1.7 million of these improper payments, leaving \$8.6 million that is potentially subject to recovery. Further, by not establishing an adequate methodology for both qualitative and quantitative risk assessments, the Agency cannot provide reasonable assurance that payment streams are not susceptible to significant improper payments.

### **The PIIA Requires Agencies to Conduct Risk Assessments to Determine Whether Payments Exceed Statutory Threshold**

In accordance with Appendix C to OMB Circular A-123, each agency should develop an improper payment risk-assessment methodology for programs with outlays greater than \$10 million to ensure that the results of the agency's risk assessments reasonably support whether the programs are likely to make improper and unknown payments above or below the statutory threshold or, in other words, are susceptible to significant improper payments. Agencies may choose to conduct a qualitative or quantitative assessment. If a qualitative risk assessment is performed, the agency should develop and apply a risk-scoring methodology to determine whether payment streams exceed the statutory threshold. It is the agency's responsibility to determine the risk factors and the associated weighting methodology for each program and risk. A quantitative assessment uses numerical data to determine whether a payment stream exceeds the statutory threshold. This type of assessment must include support to verify the calculated error rate or estimated improper payment dollars.

In FY 2021, the EPA conducted qualitative and quantitative risk assessments for the eight payment streams that had expenditures over \$10 million to determine whether the payment streams were susceptible to significant improper payments. The risk assessments included reviews of payment data and associated risks that covered multiple time periods ranging from July 2018 to June 2021.

Because the EPA reported in its FY 2020 AFR that the grants payment stream was susceptible to significant improper payments, the Agency was required by Appendix C to OMB Circular A-123 to provide an improper payment rate estimate for the program in the following fiscal year. The Agency prepared this estimate using a statistical sampling methodology that incorporated a review of 240 selected grant payments. When the Agency identifies any questioned costs in such an estimate, the OCFO submits those questioned costs to the Grants Management Office to determine whether the payments were improper.

The OIG is responsible for evaluating the completeness and accuracy of the EPA's risk-assessment methodology to determine whether the Agency is in compliance with the PIIA. Appendix C to OMB Circular A-123 states that agencies should be mindful that OIGs must consider the adequacy of the risk-assessment methodology used to evaluate compliance. OIG compliance evaluations will determine whether the audits, examinations, and legal actions indicate a higher risk of improper payments. Therefore, when developing a risk-assessment methodology, the OMB encourages agencies to review the results of audits and to consider whether the results affect the risk of improper payments.

For the seven EPA payment streams (other than the grants payment stream) that the EPA did not previously identify as being subject to significant improper payments and that the EPA conducts risk assessments for every three years, we evaluated the:

- Risk assessments conducted.
- Methodology that the Agency used to determine if the risk assessments adequately concluded whether the programs were likely to make improper and unknown payments above or below the statutory threshold.
- Accuracy of the improper and unknown payment estimates and whether the *Sampling and Estimation Methodology Plan* that the Agency used was appropriate given the programs' characteristics.
- Improper payment risk-assessment methodology of the programs, including whether:
  - Audits, examinations, and legal actions indicated a higher risk of improper payments.
  - Actual improper payments were included in the improper payment risk assessments.
- Agency and program efforts to prevent and reduce improper and unknown payments.

In addition, we determined whether the Agency had published the results of risk assessments in the Agency's AFR.

For the Agency's grants payment stream, we assessed the methodology for the EPA's review of the 240 grant payments. We applied the "questioned-cost" criteria defined in Appendix C to OMB Circular A-123, which requires that we classify a cost as questionable if it:

- Resulted from a violation or possible violation of a statute, a regulation, or the terms and conditions of a federal award, including those for funds used to match federal funds.

- Was not supported by adequate documentation.
- Appeared unreasonable and did not reflect the actions a prudent person would take in the circumstances.

## The EPA Did Not Test Grant Payments for Cost Principles

The Agency used the *Standard Operating Procedure Grants Improper Payment Review* to determine the method for selecting and testing grant payments for improper payments in FY 2021. The *Standard Operating Procedure Grants Improper Payment Review* did not incorporate the cost-allowance principles prescribed in 2 C.F.R. part 200, subpart E, and all its subsections. In response to OIG Report No. [21-P-0135](#), the Agency agreed to a proposed corrective action to incorporate the limited cost principles in 2 C.F.R. part 200, subpart E, into an updated grant payment SOP. While the Agency stated that it issued an updated SOP in September 2021 for future reviews that included the cost principles in 2 C.F.R. part 200, subpart E, and all its subsections, the updated SOP was not completed in time to be implemented for the FY 2021 AFR risk assessments. Because the Agency used the old SOP for these assessments, the Agency did not apply the cost principles.

In 16 (64 percent) of the 25 grants that the OIG reviewed, there was insufficient documentation to support the costs or payments that were actual or possible violations of a statute, regulation, or grant terms; therefore, grant recipients were paid for unallowable costs. Table 3 shows the results of the OIG's review of payments and the OIG's identified questioned costs.

**Table 3: Results of OIG-selected grants and areas of noncompliance**

No.	Award number	Draw amount	Improper payments reported by the EPA	Questioned costs identified by the OIG	Potential or actual violation of statute, regulation, or grant terms	Insufficient documentation
1	BG00A00355	\$51,686.00	\$0	\$48,106.36		X
2	I96891001	80,496.00	0	45,938.62		X
3	PA00J99101	95,178.41	0	95,164.51		X
4	BG99T90420	150,000.00	0	119,280.99		X
5	GA99T78501	112,242.97	0	112,242.97	X	
6	GA99T78501	130,323.00	0	130,323.00	X	
7	DE01F24301	1,363,078.00	0	1,363,078.00	X	
8	CB-96331101-7	371,904.51	0	371,904.51		X
9	BF00A005190	297,430.30	0	0		
10	83587301	137,580.92	0	53,650.62		X
11	BF00E02375	77,530.92	0	15,676.14		X
12	00E02060	620,964.00	0	620,964.00	X	X
13	01J12201	1,851,776.62	0	1,851,776.62	X	
14	00615819-2	410,429.86	0	410,429.86		X
15	99T29201	1,769,375.69	0	1,769,375.69	X	
16	00905519	509,825.00	0	0		
17	00E01523	1,573,164.61	0	1,573,164.61	X	X
18	BG98542816	1,103,020.00	0	805,216.91	X	X
19	C6-00E99209-3	168,877.75	0	58,617.75		X
20	L00640514-2	397,047.00	0	397,047.00		X
21	BG99T52020-1	161,178.73	40,462.24	0		
22	83938701	360,135.31	4,164.57	355,970.74		X
23	A00408120	133,462.87	9,686.21	123,776.66		X

No.	Award number	Draw amount	Improper payments reported by the EPA	Questioned costs identified by the OIG	Potential or actual violation of statute, regulation, or grant terms	Insufficient documentation
24	A98055711-0	22,596.25	22,596.25	0		
25	GA01J22401	37,780.51	12,398.06	25,382.45		X
<b>Total</b>		<b>\$11,987,085.23</b>	<b>\$89,307.33</b>	<b>\$10,347,088.01</b>	<b>8</b>	<b>16</b>

Source: OIG analysis of gathered data (EPA OIG table)

Legend:

X Noncompliant

We questioned costs for 21 (approximately 84 percent) of the 25 grants we reviewed because there was insufficient documentation to support the costs that the grant recipients claimed. For example, the Agency reimbursed a grant recipient without receiving an invoice or other supporting documentation. If requested, recipients are required, per grant terms and conditions, to provide supporting documentation for reimbursement of costs. In addition, 2 C.F.R. § 200.403(g) requires that costs be “adequately documented” to be allowable. According to Appendix C to OMB Circular A-123, when an agency’s review is unable to determine whether a payment was proper because of insufficient or missing documentation, the payment must be considered an unknown payment.

For eight (approximately 32 percent) of the 25 grants we reviewed, we questioned costs for violations or potential violations of a statute, regulation, or grant terms. For example, the Agency reimbursed a recipient for a tax expense of \$171,234.12 that may have been subject to a tax exemption. Pursuant to 2 C.F.R. § 400.470, the payment of taxes is not allowable if the taxes are subject to an exemption afforded the federal government. Although 2 C.F.R. § 400.470 was not one of the cost-allowance principles that the Agency agreed to apply in its corrective action, the OIG, in undertaking its own review, applied all applicable regulations during the OIG’s PIIA auditing.

There were also instances in which the Agency already identified and recovered improper payments but did not report them in the FY 2021 AFR. For example, a recipient erroneously withdrew and subsequently returned funds on two occasions; however, the EPA did not report these transactions as improper payments because the recipient returned the funds. Although the funds were recovered, the grant withdrawals were improper payments at the time that they occurred. They are considered improper payments that the Agency should report, even though there are no amounts that would be subject to recovery. From the 25 grant files we reviewed, we identified approximately \$1.7 million that the Agency recovered because the funds were improperly paid; however, the Agency did not report the funds as improper payments.

The EPA reported \$89,307 in improper payments. In contrast, the OIG identified a total of \$10,347,088 in questioned costs. Since these questioned costs resulted from an analysis of only 25 (approximately 10 percent) of the 240 grants that the Agency reviewed, there is a high probability that additional improper and unknown payments exist within the remaining 215 grants. Based on our analysis, the Agency may have underreported its improper and unknown payments by \$10,256,781. If the Office of Grants and Debarment determines these payments to be improper, the Agency’s reported error rate could increase from 0.50 percent to 21.88 percent—a recalculation that would indicate that the grants payment stream exceeded the statutory threshold. Of the \$10.3 million in payments the OIG identified, the Agency has recovered approximately \$1.7 million that needed to be reported, leaving approximately \$8.6 million as potentially recoverable.



## The Grant SOP Used Does Not Require an Analysis of Cost Principles

The Agency's January 2020 version of *Standard Operating Procedure Grants Improper Payment Review*, which the Agency used as guidance for the FY 2021 improper payment reviews, does not require OCFO reviewers to analyze the allowability of costs according to 2 C.F.R. part 200, subpart E. As such, the OCFO's review of grant payments was limited to examining supporting documentation for the following three components:

- Purpose: there was an authorized need or intent for the cost.
- Time: the cost was incurred within the time frame of the grant.
- Amount: the cost was within the limits of the grant budget.

The *Standard Operating Procedure Grants Improper Payment Review* requires that any OCFO payment reviewer who has questions about a particular cost refer the matter to the EPA's Office of Grants and Debarment for further review. We concluded that the OCFO review did not fully apply cost principles, which led to underreporting at least \$10 million in questioned costs to the Office of Grants and Debarment. Of the 25 grant payments, totaling \$11,987,085.23, that we selected for review, OCFO grant reviewers referred \$89,307.33, or less than 1 percent, to the Office of Grants and Debarment for examination of cost allowability. The other grant payments were never reviewed for cost allowability beyond the limited analysis of purpose, time, and amount.

OCFO officials previously took the position that improper payment legislation does not require the inclusion of the 2 C.F.R. part 200 requirement in reviews subject to significant improper payments. Rather, OCFO management and staff interpreted the cost principles in 2 C.F.R. part 200, subpart E, as pertaining to grant compliance reviews, which the OCFO does not perform. Additionally, OCFO reviewers told us that their main priority was to follow the *Standard Operating Procedure Grants Improper Payment Review*, which does not require the application of the C.F.R. cost-allowance principles. OCFO reviewers could not provide sufficient evidence to support that the amounts paid met the cost principles. However, Appendix C to OMB Circular A-123 advises agencies to be mindful that, when evaluating compliance, inspectors general must consider the adequacy of the risk assessment and methodology used.

In EPA OIG Report No. 20-P-0167, we noted the Agency's lack of inclusion of cost-allowance principles in the Agency's review of grant payments and recommended that the Agency include the criteria in the *Standard Operating Procedure Grants Improper Payment Review*. The Agency agreed to the corrective action, but the updated *Standard Operating Procedure Grants Improper Payment Review* was issued in September 2021 and was, therefore, not updated in time for the FY 2021 review. The Agency's planned corrective action was to apply limited cost-allowance principles (that is, 200 C.F.R. §§ 400.402–400.411) only when a program was identified as being susceptible to significant improper payments. Because the Agency was unable to implement the updated *Standard Operating Procedure Grants Improper Payment Review* for its FY 2021 AFR risk assessment, we do not believe that the Agency adequately concluded that the grants payment stream was no longer likely to make significant improper and unknown payments under the statutory threshold. Moreover, even had the Agency been able to implement the updated SOP, we would have still needed to determine whether the revised SOP—which included only limited cost-allowance principles—would be sufficient to determine PIIA compliance. Accordingly, we believe that it is necessary for the Agency to conduct an off-cycle risk assessment for the grants payment stream rather than wait another three years.

## The Risk Assessments for Programs on the Three-Year Review Cycle Were Insufficient, and the Agency Lacked Clear Guidance for Conducting the Assessments

The EPA conducted 12 risk assessments for the eight payment streams that had outlays over \$10 million. However, none of the 12 assessments contained sufficient support for the weighting methodology used for each program and risk, with the exception of the grants payment stream. We found that the risk assessments were insufficient or that they only accounted for a portion of the payment stream. Further, the Agency lacked a standard methodology to adequately determine program susceptibility to making improper payments. Table 4 presents the results of our analysis of the risk assessments for the payment streams with annual outlays of more than \$10 million.

**Table 4: The OIG’s review of the EPA’s risk assessments**

Payment stream	Risk assessment	Deficiencies the OIG identified
<b>Commodities</b>	1 qualitative 1 quantitative	<ul style="list-style-type: none"> <li>No support provided for the process to assign scores to the qualitative risk assessment.</li> <li>Insufficient support to verify the error rate or estimated dollars for the quantitative risk assessment.</li> </ul>
<b>Contracts</b>	2 qualitative 1 quantitative	<ul style="list-style-type: none"> <li>No support provided for the process to assign scores to the qualitative risk assessment.</li> <li>No consolidated qualitative risk-assessment score provided.</li> <li>Insufficient support to verify the error rate or estimated dollars for the quantitative risk assessment.</li> </ul>
<b>Clean Water State Revolving Fund</b>	1 qualitative	<ul style="list-style-type: none"> <li>Incomplete with not all required data included.</li> <li>No support provided for the process to assign scores to the qualitative risk assessment.</li> </ul>
<b>Drinking Water State Revolving Fund</b>	1 qualitative	<ul style="list-style-type: none"> <li>Incomplete with not all required data included.</li> <li>No support provided for the process to assign scores to the qualitative risk assessment.</li> </ul>
<b>Hurricane Sandy</b>	1 quantitative	<ul style="list-style-type: none"> <li>Insufficient support to verify the error rate or estimated dollars for the quantitative risk assessment.</li> <li>No analysis of unknown payments.</li> </ul>
<b>Payroll</b>	1 quantitative	<ul style="list-style-type: none"> <li>Insufficient support to verify the error rate or estimated dollars for the quantitative risk assessment.</li> </ul>
<b>Purchase Card</b>	2 qualitative	<ul style="list-style-type: none"> <li>No support provided for the process to assign scores to the qualitative risk assessment.</li> <li>No consolidated qualitative risk-assessment score provided.</li> </ul>
<b>Grants</b>	1 quantitative	<ul style="list-style-type: none"> <li>No cost principles included. See OIG analysis of grants payment stream in Table 3.</li> </ul>
<b>Total</b>	<b>12 Assessments</b>	

Source: OIG analysis of payment stream risk assessments. (EPA OIG table)

### *Payment Streams Complicated the Risk-Assessment Process*

To conduct risk assessments, the Agency divided improper payment reviews into payment streams instead of programs (see Chapter 1, Table 1). Appendix C to OMB Circular A-123 allows agencies to determine the most appropriate grouping of activities that would constitute a program. However, it states the grouping should be in a manner that most clearly identifies and reports improper payments for the agency. In addition, Appendix C to OMB Circular A-123 states that the agency should not put

activities into groupings that may mask significant improper payment estimates by the large size or scope of the grouping. We identified more than 40 programs with outlays over the \$10-million threshold. The OCFO did not provide a reconciliation of these programs; therefore, we could not determine which programs were included in the ten payment streams. The risk assessments were ultimately compiled by payment streams, and program risk information was disjointed, sometimes missing, and incomplete. The decision to delineate programs via payment streams and the lack of standards to outline the process for conducting the risk assessments led to them being incomplete. For example, the Hurricane Sandy payment stream had outlays greater than \$10 million. The Agency advised that the risk assessment for the Hurricane Sandy payment stream was included in the Clean and Drinking Water State Revolving Fund assessments. However, it was not clear to us that the Hurricane Sandy payments were included in those assessments because the Agency did not delineate the programs captured within each payment stream. As such, we could not determine whether the Agency appropriately evaluated this payment stream for compliance.

### ***The OCFO Did Not Have a Process for Conducting Risk Assessments***

OCFO officials and staff indicated significant deficiencies in both the risk-assessment process and the scoring methodology. OCFO officials stated that the risk-factor weighting methodology was subjective in nature and structured around the judgment or experience of the payment-integrity reviewer. OCFO staff told us that, unlike the *Standard Operating Procedure Grants Improper Payment Review* for risk assessments, they do not have an SOP for performing the risk assessments for payment streams other than the grants payment stream. This lack of guidance includes an absence of standard policies and procedures for identifying risk factors for the improper-payment reporting or the risk-factor weighting process. Lastly, reviewers stated that they did not have enough time to fully complete the assessments for two of the payment streams—the Clean and Drinking Water State Revolving Funds.

## **Conclusions**

The EPA may not have reported \$10,256,781 in improper grant payments, of which approximately \$8.6 million is potentially subject to recovery. This oversight occurred because the Agency did not apply the cost-allowance principles in its review of grants payments. Further, by not having an adequate methodology for scoring risk assessments, the Agency's risk-assessment process does not provide reasonable assurance in determining whether payments streams are susceptible to significant improper payments.

When the EPA reports unreliable improper payment estimates in the AFR, Agency leadership, Congress, and the public cannot be assured that the EPA has the appropriate internal-control measures and focused strategies to identify and reduce the risk of improper payments. Improving SOPs and considering the allowability of grant costs would aid the EPA in more accurately estimating improper payments and lead to better use of funds for environmental and supporting programs.

## **Recommendations**

We recommend that the chief financial officer:

1. Review the OIG-identified questioned costs for the grants payment stream, determine the payment allowability, recover costs as appropriate, and recalculate the error rate.

2. Conduct an off-cycle risk assessment, applying the *Standard Operating Procedure Grants Improper Payment Review*, dated September 2021, and include the risk assessments in the *Agency's Fiscal Year 2023 Agency Financial Report*, ensuring that the risk assessments contain:
  - a. An assessment of all programs and activities with outlays greater than \$10 million.
  - b. An identification of which programs and activities with annual outlays exceeding the statutory threshold are included in each risk assessment.
  - c. A mechanism for identifying, accounting for, estimating, and reporting improper and unknown payments and for detailing efforts taken to prevent and reduce such payments.
3. For payment streams other than the grants payment stream, update the standard operating procedures so that they establish a sufficient methodology for programs and activities with outlays of more than \$10 million to adequately conclude whether they are susceptible to significant improper payments. The standard operating procedures should identify which programs or activities are included.
4. Periodically train Agency personnel on and provide completed course training certificates for:
  - a. The *Standard Operating Procedure Grants Improper Payment Review*, dated September 2021, which includes the *Payment Integrity Information Act Review Checklist*. Such training should include any updates to these documents and emphasize the application of the cost-allowance principles and adherence to the terms and conditions of federal awards.
  - b. All standard operating procedures, as well as any updates to them, implemented for other payment streams.

## Agency Response and OIG Assessment

The Agency provided a response to our draft report (Appendix B). In that response, the OCFO stated that it disagrees with the OIG's finding that the EPA was not compliant with FY 2021 OMB improper payment reporting requirements. The OCFO stated that the finding implies that it did not follow improper payment requirements because its review was based on OMB Memorandum M-18-20, *Improving the Management of Federal Programs and Projects through Implementing the Program Management Improvement Accountability Act (PMIAA)*. OMB Memorandum M-18-20, which was issued in June 2018 and preceded OMB Memorandum M-21-19 and Appendix C to OMB Circular A-123, was the guidance in place when the EPA started its improper grant payments review in October 2020. In the OCFO's view, OMB Memorandum M-21-19 and Appendix C to OMB Circular A-123, which were issued in March 2021 and guided the OIG's review, should not be applied retroactively. However, the OCFO agrees with the OIG that cost principles should be incorporated in grants payment stream improper payment reviews.

The OIG maintains that its finding of noncompliance is appropriate. Both OMB Memorandums M-18-20 and M-21-19 define improper payments to mean any payment that was an incorrect amount under any "legally applicable requirements," which would include the cost principles set forth in 2 C.F.R. part 200, subpart E, that govern federal grants, to determine program susceptibility to improper payments. In

addition, the OIG's determination of noncompliance was based not only on the nonapplication of cost principles for the grants payment stream but also on the deficiencies noted in this report regarding the other payment stream risk-assessment methodologies that did not sufficiently determine whether a program exceeded the statutory threshold.

With regard to specific report recommendations, the OCFO responded that it agreed with Recommendation 1. The OCFO has referred the OIG-questioned costs to the Office of Grants and Debarment to determine which costs are improper. Any costs deemed improper will be reported in the FY 2022 AFR. However, the OCFO did not state that it would include a recalculated error rate or recover costs that were deemed improper. Therefore, we consider this recommendation unresolved.

The OCFO stated that it agreed with Recommendation 2, but its corrective actions did not fully address all the parts of the recommendation. More specifically:

- Recommendation 2 stated that the Agency should conduct an off-cycle risk assessment for the grants payment stream, with three subparts for what the off-cycle assessment should include. While, as discussed below, the OCFO stated that it agreed with the recommendation subparts, it did not expressly state that it would conduct an off-cycle review.
- For Recommendation 2a, the OCFO stated that it agreed with our recommendation to do an assessment of all programs and activities with outlays greater than \$10 million. However, the OCFO did not state that it would provide an assessment. Instead, the OCFO stated that it would "provide documentation to support the OMB's approval" of the OCFO's use of payment streams.
- For Recommendation 2b, although the OCFO stated that it agreed with our recommendation for an identification of programs and outlays exceeding the statutory threshold, it stated that it already has documented methodologies for identifying, accounting for, estimating, and reporting improper and unknown payments. In its response, the OCFO proposed to consolidate the various existing methodologies; however, the OIG concluded in this report that those methodologies do not sufficiently address the weighting methodology required to be used to measure program risk. As such, the consolidation of existing methodologies does not satisfy the intent of the recommendation.
- For Recommendation 2c, although the OCFO stated that it agreed with our recommendation for establishing a mechanism for identifying, accounting for, estimating, reporting, and preventing improper and unknown payments, the OCFO stated that it will assess the roles and responsibilities regarding the incorporation of cost principles and implement them into the FY 2023 improper payment review. However, it is unclear how this action ties to the recommendation, which is to provide a mechanism for addressing, reporting, and preventing improper and unknown payments.

Based on the above, we consider Recommendation 2 unresolved.

The OCFO agreed with Recommendation 3, stating that it would update current internal guidance documents into a consolidated SOP. The OCFO provided a corrective action completion date of October 1, 2022. This corrective action satisfies our recommendation; therefore, we consider this recommendation resolved with corrective actions pending.

Recommendation 4 stated that the OCFO should train Agency personnel on all improper payment SOPs, including training specific to the cost-allowance principles for the grants payment stream. While the OCFO agreed that it would “coordinate all payment streams to ensure that agency personnel are trained and documentation of the training is retained,” the OCFO did not expressly agree to provide training with respect to the application of the cost-allowance principles for the grants SOP. Since the OCFO only partially addressed the overall recommendation, we consider Recommendation 4 unresolved.

# Status of Recommendations and Potential Monetary Benefits

RECOMMENDATIONS							Potential Monetary Benefits (in \$000s)
Rec. No.	Page No.	Subject	Status <sup>1</sup>	Action Official	Planned Completion Date		
1	13	Review the OIG-identified questioned costs for the grants payment stream, determine the payment allowability, recover costs as appropriate, and recalculate the error rate.	U	Chief Financial Officer			\$8,624
2	14	Conduct an off-cycle risk assessment, applying the <i>Standard Operating Procedure Grants Improper Payment Review</i> , dated September 2021, and include the risk assessments in the Agency's <i>Fiscal Year 2023 Agency Financial Report</i> , ensuring that the risk assessments contain: <ul style="list-style-type: none"> <li>a. An assessment of all programs and activities with outlays greater than \$10 million.</li> <li>b. An identification of which programs and activities with annual outlays exceeding the statutory threshold are included in each risk assessment.</li> <li>c. A mechanism for identifying, accounting for, estimating, and reporting improper and unknown payments and for detailing efforts taken to prevent and reduce such payments.</li> </ul>	U	Chief Financial Officer			
3	14	For payment streams other than the grants payment stream, update the standard operating procedures so that they establish a sufficient methodology for programs and activities with outlays of more than \$10 million to adequately conclude whether they are susceptible to significant improper payments. The standard operating procedures should identify which programs or activities are included.	R	Chief Financial Officer	10/1/2022		
4	14	Periodically train Agency personnel on and provide completed course training certificates for: <ul style="list-style-type: none"> <li>a. The <i>Standard Operating Procedure Grants Improper Payment Review</i>, dated September 2021, which includes the <i>Payment Integrity Information Act Review Checklist</i>. Such training should include any updates to these documents and emphasize the application of the cost-allowance principles and adherence to the terms and conditions of federal awards.</li> <li>b. All standard operating procedures, as well as any updates to them, implemented for other payment streams.</li> </ul>	U	Chief Financial Officer			

<sup>1</sup> C = Corrective action completed.

R = Recommendation resolved with corrective action pending.

U = Recommendation unresolved with resolution efforts in progress



## ***Key Definitions***

**Improper Payment:** A payment that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements.

**Payment Integrity Information Act of 2019:** An Act that requires agencies to identify, report, and reduce improper payments in their programs. Federal agencies are required to assess and identify high-risk or significant programs and activities and share these findings in an annual publication.

**Questioned Cost:** A cost that is questioned by the auditor because of an audit finding, including that the cost resulted from a violation or possible violation of statute, regulation, or the terms and conditions of the award or that the cost was not supported by adequate documentation.

**Unknown Payment:** A payment that cannot be determined to be proper or improper because of insufficient or lacking documentation.

## Agency Response to Draft Report



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY

WASHINGTON, D.C. 20460

June 7, 2022

OFFICE OF THE  
CHIEF FINANCIAL OFFICER

### MEMORANDUM

**SUBJECT:** Response to the Office of Inspector General Draft Report, Project No. OA-FY22-0028, *"The EPA Was Not Compliant with the Payment Integrity Information Act for Fiscal Year 2021,"* dated May 20, 2022

**FROM:** Faisal Amin, Chief Financial Officer  
Office of the Chief Financial Officer

**Amin,  
Faisal**

Digitally signed by  
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Date: 2022.06.07  
04:56:56 -04'00'

**TO:** Khadija Walker, Director  
Business Operations Audits  
Office of Audit

Thank you for the opportunity to respond to the issues and recommendations in the subject draft report. The following is a summary of the U.S. Environmental Protection Agency's overall position, along with its position on the report's recommendations.

### AGENCY'S OVERALL POSITION

The draft report contains four recommendations for the Office of the Chief Financial Officer. The OCFO generally agrees with the Office of Inspector General's recommendations. However, the OCFO does not support the finding of non-compliance. The OIG's decision to not find the OCFO compliant implies the agency did not follow improper payment regulations applicable during our FY 2021 improper payment review, which began in October 2020 and concluded in March 2021.

The OCFO's FY 2021 review was based on the Office of Management and Budget's guidance M-18-20, "Requirements for Payment Integrity Improvement." Historically, the OIG has found the OCFO to be compliant with improper payment regulations. The OCFO acknowledges that the OIG had unofficially recommended incorporating the cost principles in title 2 of the Code of Federal Regulations, part 200, subpart E, following previous OCFO reviews of improper payments for grants. The OMB guidance at the time of our previous reviews and at the time the OCFO initiated our FY 2021 review, though, did not require incorporating cost principles.

During the OIG's exit conference with the OCFO, the OIG stated it followed updated *Appendix C to OMB Circular A-123*, guidance issued through M-21-19 on March 5, 2021, which directed Inspectors General to begin assessing the adequacy of methodologies used to determine whether costs were improper or unknown. The OIG stated that its audit of the OCFO's FY 2021 review, and any audit or evaluation

performed by the OIG after the issuance of the March 2021 OMB guidance, must follow the new guidelines regardless of when the OCFO's FY 2021 review was performed. Based upon the updated standards, the OIG determined the OCFO could not adequately assess improper or unknown payments for the grant payment stream due to the lack of incorporating the cost principles in part 200 of title 2 of the C.F.R. in our FY 2021 review.

The OCFO does not agree that the M-21-19 guidance should be applied retroactively. Incorporation of the cost principles subpart of part 200 of title 2 of the C.F.R. would have necessitated a more detailed review beyond the scope of the OCFO's review performed in FY 2021. Based on the OIG's interpretation of M-21-19, the agency would not have been able to conduct full cost principle reviews on the 240 sampled grant payment drawdowns in time to support this audit.

Although the OCFO does not agree with the OIG's finding of non-compliance, we agree with the OIG's recommendations, based upon updated OMB guidance, that 2 C.F.R., part 200, Subpart E – Cost Principles should be incorporated in grant payment stream improper payment reviews. The OCFO will work with the Office of Mission Support's Office of Grants and Debarment to determine the next steps for completing the corrective actions discussed below.

#### AGENCY RESPONSE TO DRAFT REPORT RECOMMENDATIONS

No.	Recommendation	High-Level Corrective Action(s)	Estimated Completion Date
1	Review the OIG-identified questioned costs for the grants payment stream, determine the payment allowability, recover costs as appropriate, and recalculate the error rate.	1. <u>Agree</u> . The OCFO completed its review of the OIG-identified questioned costs and determined, based on the existing standard operating procedures, that the costs were properly documented. The OCFO provided the OGD and the Grants Management Officers with the questioned costs to determine if these costs should be considered improper. Based on the OGD's and GMOs' review, the OCFO will include any costs identified as improper in the FY2022 Agency Financial Report.	11/15/2022
2	Conduct off-cycle risk assessment, applying the Standard Operating Procedure Grants Improper Payment Review, dated September 2021, and include the risk assessments in the Agency's Fiscal Year 2023 Agency Financial Report, ensuring that the risk assessments contain:  a. An assessment of all programs and activities with outlays greater than \$10 million.	2a. <u>Agree</u> . The OCFO defines its programs by payment stream. All programs and activities with outlays greater than \$10 million are included within one or more payment streams. The OCFO will provide documentation to support the OMB's approval for the OCFO's process.	10/1/2022
		2b. <u>Agree</u> . The OCFO has a documented methodology for identifying, accounting for, estimating, and reporting improper payments and unknown payments. The OCFO agrees and will consolidate the various methodologies.	10/1/2022

	<p>b. An identification of which programs and activities with annual outlays exceeding the statutory threshold are included in each risk assessment.</p> <p>c. A mechanism for identifying, accounting for, estimating, and reporting improper and unknown payments and for detailing efforts taken to prevent and reduce such payments.</p>	2c. <u>Agree</u> . The agency will assess the roles and responsibilities regarding the incorporation of cost principles and implement them into the FY 2023 improper payment review.	10/1/2022
3	For payment streams other than the grants payment stream, update standard operating procedures that establish a sufficient methodology for programs and activities with outlays of more than \$10 million to adequately conclude whether they are susceptible to significant improper payments. The standard operating procedure should identify which programs or activities are included.	3. <u>Agree</u> . Per approval from the OMB, the OCFO defines programs and activities by payment streams. All expenditures of the agency are represented in at least one of the payment streams. The OCFO currently has documentation defining how to conduct reviews of non-grant payment streams. However, the OCFO agrees to update current internal guidance documents into a consolidated standard operating procedure, to include the agency's methodology for identifying, accounting for, estimating, and reporting improper payments and unknown payments.	10/1/2022
4	<p>Periodically train Agency personnel on and provide completed course training certificates for:</p> <p>a. The Standard Operating Procedure Grants Improper Payment Review, dated September 2021, which includes the Payment Integrity Information Act Review Checklist, as well as any updates, to emphasize the application of the cost-allowance principles and the adherence to the terms and conditions of the federal awards.</p> <p>b. All standard operating procedures, as well as any updates, implemented for other payment streams.</p>	<p>4a. <u>Agree</u>. The agency will assess the roles and responsibilities regarding the incorporation of cost principles and implement them into the FY 2023 improper payment review.</p> <p>4b. <u>Agree</u>. The OCFO will coordinate all payment streams to ensure that agency personnel are trained and documentation of the training is retained.</p>	<p>12/1/2022</p> <p>12/1/2022</p>

## CONTACT INFORMATION

If you have any questions regarding this response, please contact the OCFO's Audit Follow-up Coordinator, Andrew LeBlanc, at [leblanc.andrew@epa.gov](mailto:leblanc.andrew@epa.gov) or (202) 564-1761.

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