Independent Accountants' Report on Applying Agreed Upon Procedures to Grant Agreement Expenditures

Southeast Local Development Corporation
Grant TN-12158-95-I-214-0607
Chattanooga, Tennessee

Submitted to the
OFFICE OF INSPECTOR GENERAL
OF THE
APPALACHIAN REGIONAL COMMISSION

Report No. 01-33 (H)

Prepared by

Leon Snead & Company, P.C.
May 11, 2001

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INDEPENDENT ACCOUNTANTS' REPORT ON APPLYING AGREED UPON PROCEDURES TO GRANT AGREEMENT EXPENDITURES

To the Inspector General of the Appalachian Regional Commission:

BACKGROUND AND OBJECTIVES

The Appalachian Regional Commission (ARC) is a regional economic development agency representing a unique partnership of Federal, state, and local government. The ARC is composed of the Governors of the 13 Appalachian states and a Federal Co-Chair appointed by the President. The geographical boundaries of the Appalachian Region extend from the southern tier counties in central and western New York to the northern counties in Alabama and Mississippi.

Each year Congress appropriates funds that ARC allocates among its member states in line with an allocation formula which is intended to provide a fair and reasonable distribution of available resources among the 13 Appalachian member states.

The Appalachian Regional Commission (ARC) awarded Grant TN-12158-95-I-214-0607, Inner City Industrial Park, Cavalier Corporation, to the Southeast Local Development Corporation (SLDC) which is located in Chattanooga, Tennessee. The $600,000 in ARC Section 214 grant funds awarded were to be used to fund part of the construction, inspection, engineering design, and demolition and removal costs associated with this project. The U.S. Department of Commerce, Economic Development Administration (EDA) was to provide an additional $2,600,000 in Federal funding for this project, and to administer the disbursement of ARC funds on the ARC's behalf. The grant objective was to remediate and clean up the Cavalier Industrial Site located in Chattanooga's inner city to create a new industrial park to be owned by Hamilton County and Chattanooga; renovate and modernize manufacturing space enabling an existing business enterprise to retain 170 jobs and create 110 new jobs at Cavalier Corporation; and open up 6 acres for future industrial use.

The Cavalier Corporation plant closed as of August 2000 and, thus, the objectives with respect to job creation and retention were not accomplished. The company ceased business operations because of large continuing losses with little chance of recovery as a result of the owner's death and few orders for its products.

Leon Snead & Company, P.C. is under contract to the Office of Inspector General (OIG) of the ARC to provide audit services. We performed agreed upon procedures on the grant expenditures reported to the ARC for the period December 27, 1995 through March 9, 1999. The objectives of our agreed upon procedures were to determine whether the reported grant expenditures were allowable, allocable, and reasonable and whether the grantee was in compliance with applicable laws and regulations.

SCOPE AND METHODOLOGY

We performed the procedures enumerated below, which were agreed to by the Inspector General of the Appalachian Regional Commission solely to assist you in evaluating grant expenditures by the grantee. This agreed-upon procedures engagement was performed in accordance with standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report.

Consequently we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

The provisions of Office of Management and Budget (OMB) Circular A-133 "Audits of States, Local Governments, and Non-Profit Organizations"; OMB Circular A-110 "Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Learning, Hospitals, and Other Non-Profit Organizations"; OMB Circular A-87 "Cost Principles for State, Local, and Indian Tribal Governments"; the Federal Drug-Free Workplace Act of 1998 (Public Law 100-690); the Federal Anti-Lobbying Act (Public Law 101-121); the Federal Acquisition Regulation (FAR); other Federal, state, or local procedures designed to insure fair and non-discriminatory procedures were used for the selection of participants; agreed to procedures that emphasize the expenditure of grant funds in line with the provisions of the grant agreement; and the ARC Code were used as the basis for determining allowable costs and compliance requirements. These agreed upon procedures were performed in accordance with generally accepted auditing standards and *Government Auditing Standards*, 1994 version, as amended, issued by the Comptroller General of the United States.

We were not engaged to, and did not, perform an examination, the objective of which would be the expression of an opinion on the financial statements of the grantee. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

We noted that the grantee reported expending all $600,000 in ARC grant TN-12158-95-I-214-0607 funds on this project. The grantee also reported contributing $1,162,612 in local grant matching expenditures. The EDA also contributed $2,600,000 to this project and the City of Chattanooga and Hamilton County, Tennessee each contributed $600,000 to this project.

We visited the Southeast Local Development Corporation's offices in Chattanooga, Tennessee during the period May 9-11, 2001.

Specifically we performed the following procedures:

- We discussed the history and background of the Inner City Industrial Park, Cavalier Corporation grant project with Southeast Local Development Corporation officials.

- We visited the Inner City Industrial Park, Cavalier Corporation grant project construction site to verify that the project had been completed and to get a better understanding of what the grant project entailed.

- We reviewed the available Cavalier Corporation financial records and other correspondence and made copies of records and correspondence.

- We scanned the documentation supporting the $3,200,000 in expenditures claimed for reimbursement on all 16 Form ED-113 Outlay Report and Request for Reimbursement for Construction Programs reports provided to us by the grantee for allowability, applicability, and reasonableness.

- We reviewed the documentary support in detail for $169,279 (74.7%) of the $226,559 in architectural engineering basic fees, all $29,944 of the reported project inspection/audit fees, and all $315,870 of the demolition and removal costs.

- We reviewed documentation supporting compliance with Environmental Protection Agency (EPA) site clean-up of hazardous waste requirements; compliance with local Historical Society site usage requirements; compliance with ARC/EDA requirements for placing demolition and removal work with minority and/or female contractors; correspondence and a copy of the Settlement Agreement breaking the lease between the SLDC and the Beacon Group/Cavalier Acquisition Corporation.

- We reviewed the Southeast Local Development Corporation Annual Financial Report for the Year Ended June 30, 2000; The Beacon Group, Inc. Consolidated Financial Statements and Supplementary Information for the periods ending December 31, 1996 and 1995, December 31, 1998 and 1997, and a draft copy of this information for the period December 31, 2000 and 1999; and copies of correspondence discussing pending or proposed future uses for the renovated Cavalier Corporation plant site.

- We compared the grant expenditures made with the approved project budget.

- We assessed the achievement of the grant objectives.

RESULTS

We noted the following.

> The available grant expenditure payment records indicated that $231,386 of the $600,000 in ARC grant funds committed to this project were used to fund project costs other than those specified in the grant project budget.

The ARC project budget called for the ARC to fund the three project cost classifications shown below as follows:

Cost Classification	Total Costs	ARC Funded
Construction Inspection	$ 75,000	$ 22,800
Engineering Design	200,000	33,977
Demolition & Removal	543,223	543,223
TOTAL	$ 818,223	$ 600,000

The actual ARC expenditures for Demolition and Removal were $315,870 leaving $227,353 unexpended ARC funds. The actual ARC expenditures for Engineering Design were $29,944 leaving $4,033 unexpended ARC funds. The total $231,386 unexpended ARC funds were used for other project costs. There was no evidence that ARC approved the changes to the original grant project budget. However, the grantee, SLDC, did not control the expenditures. Instead, the EDA controlled the ARC funds of $600,000 along with its own contribution of $2,600,000. The EDA expended the funds as needed to complete the project. So, there appears to be no reason to fault the grantee for not obtaining ARC approval for the changes to budget line items.

During our agreed upon procedures of the Beacon Group, Inc. Consolidated Financial Statements and Supplementary Information for calendar years 1995 through 2000 we noted that it was not readily apparent until the financial statements for the calendar year ended December 31, 1998 that the Beacon Group, Inc. and Cavalier Acquisition Corporation, its wholly owned subsidiary, were in serious financial distress. The Cavalier Corporation closed its plant and ceased operations in August 2000. Site renovation was essentially completed by August 1998. Thus, there appears to be no reason to fault the ARC, the EDA, or the SLDC for carrying out the project as planned. The final project expenditures were only $12,612 (0.3%) over budget, and the grantee paid for the project cost overrun.

Our agreed upon procedures also showed that the grantee and/or the EDA had contacted the Environmental Protection Agency (EPA) and had worked with them to assure that all of the work done on the site was EPA compliant. We also found that the grantee had coordinated the site renovation with the local Historical Societies and had obtained their approval to proceed with the site renovation. There was also documentation on file which showed that the grantee, or its agents, actively attempted to place the ARC financed demolition and removal work with minority and/or female contractors. We also found documentation showing that the grantee was actively attempting to finalize a Settlement Agreement with Cavalier Corporation, Cavalier's parent corporation, the estate of Cavalier Corporation's prior president, and the banks to break the 30-year lease the now defunct Cavalier Corporation has on the renovated, but unoccupied, plant site so that the site can be rented to local government tenants or used for other approved purposes. Finally we found that the grantee and/or the county was actively seeking a new tenant, or tenants, for the unoccupied plant site. As of the end of our field work, the county was working with Chattanooga and with area business institutions on a technology-based development plan that included linking to a fiber optic line along the Norfolk Southern railroad right of way which abuts the plant site.

CONCLUSION

Based on the results of our agreed upon procedures, in our opinion all $600,000 of the grant fund expenditures reported to the ARC as having been incurred and charged to the ARC for Grant TN-12158-95-I-214-0607 were allowable, allocable and reasonable and should be accepted by the ARC.

DISTRIBUTION

This report is intended for the information and use of the OIG and management of the ARC and should not be used for any other purpose. However, this report is a matter of public record and its distribution is not limited.

Leon Snead & Company, P. C.

LEON SNEAD & COMPANY, P. C.
May 11, 2001

GRANTEE COMMENTS

CHATTANOOGA AREA REGIONAL COUNCIL OF GOVERNMENTS
SOUTHEAST TENNESSEE DEVELOPMENT DISTRICT

Howell Moss
Chairman

Ronald L. Banks
Secretary

Claude Ramsey
Vice-Chairman

Elizabeth Akins
Treasurer

July 16, 2001

Ms. Alexis M. Stowe
Vice President
Leon Sneed & Company, P.C.
416 Hungerford Drive, Suite 400
Rockville, Md 20850

Dear Ms. Stowe:

Thank you for the opportunity to review and comment on the Draft Report regarding Grant TN-12158-95-I-214-0607. Included are three enclosures that address your request for additional information.

Enclosure Number 1 includes the Financial Assistance Award Letter and Budget received in our office on August 20, 2001. Also included are file copies are the Financial Assistance Award and Attachments signed by EDA and initialed by our office. We have requested of EDA our official signed copies from their file which had dated full signatures. We are unable to find our fully signed copies.

Enclosure Number 2 includes the basic Outlay Reports and Request for Reimbursement for Construction Programs 1 – 16. It is in these reports that EDA was informed of needed adjustment to the Approved Budget and transmittal of funds was assumed to reflect concurrence by EDA regarding these Budget Amendments. We have separated these basic pages but have also included Exhibit Number 3 that includes the full communication with EDA as these reports and requests for funds were being submitted.

We do not have any copies of communication between EDA and ARC in our file and are not familiar with their procedures regarding communication as funds are being approved and transferred. I assume that information would be available from those agencies.

In summary, we are in general agreement with your draft report. While there was some reduction in the demolition costs, some demolition costs, such as roofing, were combined with new construction and moved into that line item. Therefore the budget does not fully reflect those expenses as demolition costs per se.

Again thank you for the opportunity to respond. We appreciate your assistance. If there are questions or additional information needed, please give me a call at 423-266-5781.

Sincerely,

Joe W. Guthrie

Enclosures

P.O. BOX 4757 • 25 CHEROKEE BOULEVARD • CHATTANOOGA, TN 37405-0757
(423) 266-5781 • FAX (423) 267-7705

LEON SNEAD
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& Management Consultants

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leonsnead.companypc@erols.com

June 5, 2001

Mr. Hubert N. Sparks
Inspector General
Appalachian Regional Commission
1666 Connecticut Avenue, NW Suite 215
Washington, DC 20235

Subject: Draft Report No. 01-33 (H)
Grant TN-12158-95-I-214-0607
Southeast Local Development Corporation
Chattanooga, Tennessee

Dear Mr. Sparks:

Enclosed is the subject Draft Report, an original and one copy. We await your comments. Also, please indicate whether or not you want this draft report issued to the grantee for comments.

If you have any questions, please call me or Ed Schantin at (301) 738-8190.

Sincerely,

Alexis M. Stowe

Alexis M. Stowe
Vice President

Enclosure

Draft Independent Accountants' Report on Applying Agreed Upon Procedures to Grant Agreement Expenditures

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We requested, but were not provided, copies of any Grant Agreements between ARC and the SLDC or between the ARC and the EDA which specified the terms under which the EDA was to administer the ARC grant funds. We also did not receive a complete copy of the project budget and any subsequent revisions thereto. As a result, we were unable to determine if Grant TN-12158-95-I-214-0607 was ever amended, when the grant agreement was signed, or the inclusive dates of the grant period of performance.

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CONCLUSION

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