APPALACHIAN REGIONAL COMMISSION
OFFICE OF INSPECTOR GENERAL

AUDIT OF GRANT FUNDS

THE CONSERVATION FUND
ARLINGTON, VIRGINIA

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Prepared by
Leon Snead & Company, P.C.

LEON SNEAD
& COMPANY, P.C.

416 Hungerford Drive, Suite 400
Rockville, Maryland 20850
301-738-8190
fax: 301-738-8210
leonsnead.companypc@erols.com

Certified Public Accountants
& Management Consultants

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Appalachian Regional Commission
Office of Inspector General
1666 Connecticut Avenue, N.W.
Washington, DC 20009

Leon Snead & Company, P.C. has completed an audit of grant number WV-13336 awarded by the Appalachian Regional Commission (ARC) to The Conservation Fund (TCF). The audit was performed at the request of ARC, Office of Inspector General, to assist it in carrying out its oversight of ARC grant activities.

The audit objectives were to determine if: (a) the expenditures charged to the grant during the audit period were allowable, reasonable, and properly allocated; (b) matching funding was achieved and adequately documented; and (c) other requirements of the grant agreement were complied with. The audit was performed in accordance with Government Auditing Standards, OMB Circulars A-110 and A-122 and the ARC grant agreement. Audit work was conducted on June 23-27, 2003 at TCF offices in Arlington, Virginia.

The grant provided $100,000 in ARC funds for capital investment, $81,000 for establishing and operating the NCIF, and required the grantee to obtain $21,200 in non-ARC funding through matching contributions. The majority of grantee expenditures reviewed were allowable, reasonable, and properly allocated. However, we questioned $4,299 in claimed operating costs and $21,200 in claimed matching funding because there was not adequate supporting documentation to permit verification.

A draft report was provided to ARC program officials for comment on July 15, 2003. Written comments were received on October 7, 2003, and the report has been revised to give consideration to the ARC comments where necessary. The comments are included in their entirety in Appendix A.

Leon Snead & Company, P.C. appreciates the cooperation received from ARC and grantee personnel during the audit and the positive response to making improvements.

Leon Snead & Company, P.C.

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Introduction

Leon Snead & Company, P.C. has completed an audit of grant number WV-13336 awarded by the Appalachian Regional Commission (ARC) to The Conservation Fund (TCF). The audit was performed at the request of ARC Office of Inspector General (OIG) to assist it in carrying out its oversight of ARC grant activities.

The Conservation Fund is a national, non-profit organization established in 1985 to develop conservation solutions through partnerships with government, other non-profits, and private industry. TCF seeks to integrate community, economic and environmental goals by acquiring land, undertaking community initiatives, and providing leadership training. During the fiscal year ended December 31, 2002, TCF had total support and revenue of approximately $68 million and expenditures on Federal awards of approximately $3 million.

The subject ARC grant was awarded to TCF in April 1999 to establish and operate the West Virginia Natural Capital Investment Fund (NCIF). The NCIF is a wholly owned TCF subsidiary and is operated out of the TCF facilities at the Freshwater Institute in Shepherdstown, WV. The NCIF's purpose is to provide strategic capital, through loans and/or equity investments, to new and expanding businesses (in the natural resources field) located in economically distressed areas of West Virginia.

The overall NCIF approach is to provide investments of $50,000 to $250,000 to such businesses in order to reduce the risk so other commercial lenders will be willing to provide the major portion of the business' total funding needs. Loan repayments and other income are placed in NCIF's revolving fund and those funds are used to make new loans and investments. During three years of operation, the NCIF has made three loans totaling $139,500, an equity investment of $15,000 and has leveraged $712,804 in additional bank financing and owner's equity.

The grant provided $100,000 in ARC funds for capital investment, $81,000 for establishing and operating the NCIF, and required the grantee to obtain $21,200 in non-ARC funding through matching contributions. ARC also agreed to provide an additional $100,000 for NCIF capital investment purpose through a separate agreement it had with the Mountain Association for Community Economic Development.

Objectives, Scope, and Methodology

The audit objectives were to determine if: (a) the expenditures charged to the grant during the audit period were allowable, reasonable, and properly allocated; (b) matching funding was achieved and adequately documented; and (c) the grant agreement other requirements were complied with. The audit covered grant activities during the period April 1, 1999 to March 31, 2003 including the $81,000 claimed by the grantee against ARC funds and the $21,200 non-ARC matching funding claimed. Audit work was conducted on June 23-27, 2003 at the TCF offices in Arlington, Virginia.

We reviewed the grant agreement, OMB Circulars A-110 "Uniform Administrative Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations" and A-122 "Cost Principles for Non-Profit Organizations." We reviewed available grantee accounting and project management records and supporting documentation for expenditures reported. Selected costs claimed against the grant were reviewed in detail to verify if they were allowable and reasonable. We reviewed and discussed grantee policies and procedures applicable to administering the grant. We also reviewed reports of recent audits and reviews of the grantee to identify any problems or weaknesses and corrective actions taken.

The majority of grantee expenditures reviewed were allowable, reasonable, and properly allocated. However, we questioned $4,299 in claimed operating costs and $21,200 in claimed matching funding because there was not adequate supporting documentation to permit verification. Also, the indirect costs proposed by the grantee and accepted by ARC were not consistent with the grantee's rate negotiated with the Federal cognizant agency. The grantee complied with the grant agreement provisions and other important applicable requirements in most material respects. However, ARC provided advance funding that was not fully consistent with Circular A-122 requirement in the grant agreement.

These matters and other areas that could be improved are discussed in the findings and recommendations sections of the report.

The audit was performed in accordance with generally accepted auditing standards and *Government Auditing Standards*, as amended, and included testing of applicable internal controls necessary to achieve the audit objectives.

FINDINGS AND RECOMMENDATIONS

A. Documenting and Supporting Costs

The grantee's final budget and request for reimbursement submitted to ARC on June 9, 2003, indicated total expenditures of $81,000 for operating costs. To verify that these costs were allowable, reasonable, and properly allocated we selected several of the largest categories of costs claimed including salaries ($49,087), web site ($4,299), travel ($8,000), and indirect costs ($12,500). No exceptions were noted with salary costs claimed. However, we identified $4,299 in costs in other categories that we question due to lack of adequate supporting documentation. They were as follows:

Travel - $2,031 questioned:

- Airfare of $854 for Mr. Jenkins on 2/27/01. No airline or similar receipt was available to show that the airfare was used. The only documentation was a charged card bill.

- Rental car fee of $294 for Mr. Jenkins of 9/12/01. No receipt available.

- Airfare and other costs of $883 for Mr. Jenkins of 2/27/01. No documentation was available to show that the costs were attributable to ARC grant activities. The airfare documentation was inconsistent with trip description, and no support was available for the other cost.

We also noticed TCF's travel procedures do not required formal approval by a supervisor prior to travel to ensure that the travel is necessary and the estimated costs are reasonable.

Web Site - $1,063 questioned:

The grantee provided several documents as support for the $4,299 web site costs. One was a copy of a purchase order with Panda Consulting of Palm Beach, Florida, showing a cost of $3,000 to develop a web site for NCIF.

Others were two purchase orders for a total $795 to G.H. Bailey Company to design, write, and illustrate brochures for NCIF. NCIF staff stated these brochures related to the web site costs because they used the logo and some information from them. Based on the work description these costs seem to be more closely related to the "Brochures" line item contained in the budget. For purposes of the audit, it was decided to attribute the $795 to that cost category which is discussed in the paragraph below.

Time sheets for Carla Doggett, an employee at the Freshwater Institute, were also provided as support for the web site costs claimed. However, this individual was in a clerical position and there was nothing in the timesheets to indicate that this person worked directly on the web site activity, what was done, or for how long. NCIF staff stated that they did not have any documentation to show that a specific dollar figure related to this effort was used to develop the $4,299. Based on available documentation we accept the $3,000 but question the remaining $1,063 of the claimed costs.

TCF also could not provide documentation on the two contracting actions discussed above describing what the specific requirements were, the actions taken to select the source, and the basis on which the price paid was determined to be fair and reasonable. The need for TCF to establish written procurement procedures, including documenting cost/price analysis, was identified in an earlier review by U.S. Environmental Protection Agency contracting representatives. TCF staff told us such procedures have not yet been developed. Our audit reaffirms the need to do so.

Brochures - $1,205 questioned:

TCF claimed $2,000 for this work. No documentation could be provided to support any of these costs. However, as discussed above, we believe the $795 procurement from the Bailey Company should be allocated to this category rather than Web Site costs. Therefore, we question the $1,205 difference.

We are not questioning any of the indirect costs claimed and not recommending ARC disallow them. However, we determined that the amount proposed by TCF and accepted by ARC reflected a rate higher than the rate established by the Federal cognizant agency for TCF. The approved rate at the time was 20 percent. The effective rate accepted by ARC was 25 percent based on the amount of direct costs shown in the budget. Under OMB Circular A-122, appendix A, the established rate must be accepted by the Federal awarding agency unless there are circumstances that justify using a different rate. TCF staff told us they did not consider the approved TCF rate in developing the costs for this grant. The ARC grant coordinator stated that they do not routinely review proposed indirect costs before award so those costs were not reviewed or questioned in this case.

Corrective actions are needed to ensure that the grantee is reimbursed only for allowable costs under the grant and that future proposals are reviewed to verify that proposed indirect costs are appropriate and consistent with Federal requirements.

Recommendations

ARC should:

1. Disallow the $4,299 in expenditures claimed by TCF under the grant that are questioned unless additional documentation can be provided to clearly demonstrate the expenditures were made, were allocable to the ARC grant activities and funds, and are otherwise allowable under the agreement and Circular A-122 requirements.

2. Take necessary steps to ensure all future grant proposals containing indirect costs are reviewed to verify that such costs are justified, reasonable, and developed in accordance with the grantee's approved rate (when applicable) and requirements of Circular A-122.

3. Request TCF to expedite establishment of written procurement procedures and to amend its travel procedures to require formal approval prior to travel.

Management Response

In reference to the questioned costs of $4,299, the grantee provided ARC additional documentation for the $1,737 airfares and other travel cost for Jenkins. ARC concluded that this documentation was reasonable and acceptable. The grantee agreed with the remaining audit findings and will return $2,562 to ARC.

In its response to recommendation 2 on indirect costs ARC stated that their staff routinely take steps to ensure indirect costs are reasonable and meet acceptable parameters for the type of proposed grant activity. When applicable, ARC asks Grantees to confirm that the indirect rates charged are the approved federal rates.

The grantee has revised Chapter IX of the TCF Financial Management Handbook dealing with Government Grants, Cooperative Agreements and Awards with more detailed procurement procedures, including the competitive bid process, cost and price analysis, and sole source justifications. The revisions have been released and reviewed with all staff. Travel procedures have not been revised, and all travel will continue to be approved via the annual operating budget process.

Auditors Comments

The comments received from the grantee and ARC are considered responsive to finding and recommendations.

B. Documenting Matching Funding

The grantee did not have documentation in its grant files to verify that the $21,200 in third-party, in-kind contributions reported to ARC were actually received and that the amounts were reasonable and estimated according to Circular A-110 requirements.

Circular A-110, section .23 requires that, to be allowable as cost-sharing or matching on the grant, the contributions must be verifiable from the recipient's records. Contributed services must be documented, and to the extent feasible, supported by the same methods used by the recipient for its own employees. The basis for determining the value of the services must also be documented.

TCF reported receiving matching, in-kind services from the Mountain Association for Community Economic Development valued at $15,000 and from the West Virginia Small Business Development Center valued at $6,200. We asked to review the supporting documentation for these amounts and were told that we would have to contact the donor organizations to obtain such information. The grantee personnel responsible for obtaining and maintaining such documentation were not aware of the A-110 requirements.

Recommendation

ARC should:

4. Disallow the $21,200 claimed by the grantee as third-party matching unless documentation as required under Circular A-110 can be provided and verified. If the amounts are disallowed, necessary steps should be taken to ensure ARC policies regarding match funding requirements are complied with on this grant.

5. Require TCF to take action to ensure their procedures reflect Circular A-110 requirements for documenting matching amounts claimed and that grant managers are award to them.

Management Response

The grantee indicated in conversation with ARC that they inadvertently itemized the questioned costs as matching expenses. ARC informed the auditors, however, that the disallowance of the expenditure as matched funds will not affect the final reimbursement to the grantee as sufficient matched funds are provided by other sources to meet ARC matching requirements.

In response to the recommendation on modifying accounting procedures regarding matched funds, the grantee added more specific language on "billings" and the timing of cash advances to Chapter IX of the TCF Financial Management Handbook dealing with Government Grants, Cooperative Agreements and Awards. These revisions have also been released and reviewed with all staff.

Auditors Comments

The comments received from the grantee and ARC are considered responsive to the finding and recommendations.

C. Making Cash Advance

The grantee requested a $100,000 cash advance in December 1999 for the purpose of making NCIF capital investments under the grant. ARC approved and provided the requested amount. The TCF grant director stated that a potential investment was being developed at the time that required the amount requested but that the deal was not ever completed. The grantee did not make its first investment until June 28, 2001, for a total of $58,500. The total $100,000 advance provided by ARC was not used until the second investment for $50,000 was made in June 2002.

OMB Circular A-110, section .22, requires that cash advances be limited to the minimum amount needed by the grantee and timed in accordance with the actual, immediate cash requirements. The timing shall be as close as administratively as possible to the actual disbursement.

The advance approved and made by ARC in this case does not meet this requirement. The initial request appears to be justified and the failure of the investment to be completed is understandable. However, we do not believe ARC should have made the advance without some reasonable evidence that the investment would definitely be completed and TCF would therefore need the funds. Action is needed to help prevent this situation in the future.

Recommendation

6. ARC should ensure that all grant personnel responsible for approving cash advances are aware of Circular A-110 requirements and that advances to grantees for making loans or investments such as under WV-13336 are not made before reasonable assurance is obtained that the loan or investment will definitely be completed.

Management Response

ARC stated that in November 2001, they adopted "Development Venture Capital Application and Operating Guidelines". These guidelines provide a cash advance policy for grants which incorporate these guidelines in the grant agreement. Upon their adoption by the Commission, these guidelines should have been incorporated into the grant agreement for WV – 13336, thus averting the condition noted. Contract amendment action is being requested to make these guidelines applicable to this grant.

The grantee informed ARC that their accounting procedures have been amended and the staff was notified of the amended procedures regarding advance payment requests.

Auditors Comments

The comments received from the grantee and ARC are considered responsive to finding and recommendations.

D. Complying With Grant Guidelines

Investment policies developed by TCF to carry out NCIF activities have a provision that conflicts with special ARC guidelines contained in the grant agreement. One of the provisions in the ARC guidelines, contained in Supplement B to Part I of the agreement, is that the financing of real estate or buildings is an ineligible investment using ARC funds. Section 2.1 of the NCIF Investment Underwriting Guidelines permits the proceeds from NCIF loans to be used for real estate acquisition. This is not consistent with the grant agreement and therefore a potential non-compliance with ARC policies and requirements.

The ARC guidelines incorporated into the agreement for WV-13336 were initially developed for another ARC-funded effort, The Strategic Capital Investment Fund, operated by the Mountain Association for Community Economic Development. The NCIF was planned to be modeled after that fund and therefore ARC incorporated the same guidelines. The ARC grant coordinator stated that the guidelines do officially apply to the NCIF but that in retrospect there were some aspects in those guidelines that perhaps should not apply. He explained that ARC has since developed newer guidelines for such grant activities and those would likely be more applicable to the NCIF.

We did not see any evidence that any of the loans made to date violated the current grant guidelines. However, since NCIF is a revolving fund whereby loan repayments and other income can be used for future investments, and ARC has a financial interest in the NCIF until it is terminated, there is a potential that future loans could be made that would involve real estate acquisition and not be in compliance with the grant requirements. Corrective action is needed to ensure full compliance with ARC requirements.

Recommendation

7. ARC should either amend the agreement for WV-13336 to reflect the correct guidelines it requires the NCIF to comply with or require TCF to amend the

NCIF investment policies to accurately reflect and conform with the guidelines currently in the agreement.

Management Response

The grant agreement for WV–13336 will be amended to incorporate the "Development Venture Capital Application and Operating Guidelines", and to eliminate the Strategic Capital Investment Fund guidelines. The later guidelines were incorporated prior to the adoption of the "Development Venture Capital Application and Operating Guidelines" by the Commission. These later guidelines are no longer relevant and have been superceded by the "Development Venture Capital Application and Operating Guidelines".

Auditors Comments

The comments received from the grantee and ARC are considered responsive to finding and recommendations.

APPENDIX A

MANAGEMENT RESPONSE

facsimile transmittal

from the desk of Jeffrey H. Schwartz, Ed. D.
Acting Director
Program Operations Division
1666 Connecticut Avenue, NW, Suite 700
Washington, DC 20009-1068
jschwartz@arc.gov
Telephone: 202-884-7721 Fax: 202-884-7691

To:	Leon Sneed	**Fax Number:**	301-738-8210
From:	Jeff Schwartz	**Date:**	10/7/2003
Re:	Draft audit report of WV-13336	**Pages:**	4 (including cover sheet)
CC:			

☐ Urgent ☐ For Review ☐ Please Comment ☐ Please Reply ■ As requested/ promised ☐ For your information

Audit Recommendations
ARC should:

1. *Disallow certain costs.*
Grantee Response #1: See attached.
ARC Response: Grantee has provided additional documentation regarding some of the questioned costs. This documentation appears reasonable and acceptable. Other costs, totaling $2,562, will be returned to ARC by the Grantee, who agrees with the audit findings relative to them.

2. *Ensure grant proposals received by ARC are reviewed to verify that indirect costs are reasonable.*
Grantee Response: None required.
ARC Response: ARC staff routinely take steps to ensure indirect costs are reasonable and meet acceptable parameters for the type of proposed grant activity. When applicable, ARC asks Grantees to confirm that the indirect rates charged are the approved federal rates.

3. *Request TCF establish written procurement procedures regarding travel.*
Grantee Response #2: See attached.
ARC Response: Grantee response is deemed sufficient.

4. *Disallow $21,200 in match claimed by grantee as third-party match.*
Grantee Response: In conversations, the grantee indicated they inadvertently itemized the questioned items as matching expenses.

ARC Response: ARC concurs with the auditor's recommendation. These expenditures should not be considered as match for the purposes of this grant. However, disallowance of these expenditures as match will not affect the final reimbursement to the grantee as sufficient match is provided by other sources to meet ARC matching requirements.

5. *Require TCF to modify their accounting procedures regarding match.*
   Grantee Response #3: See attached.
   ARC Response: Grantee response is deemed sufficient.

6. *Ensure all grant personnel are aware of A-110 advance requirements.*
   Grantee Response #4: None required, but provided. The grantee has amended their accounting procedures, and notified appropriate staff, regarding advance payment requests.
   ARC Response: In November 2001, ARC adopted "Development Venture Capital Application and Operating Guidelines". These guidelines provide a cash advance policy for grants which incorporate these guidelines in the grant agreement. Upon their adoption by the Commission, these guidelines should have been incorporated into the grant agreement for WV-13336, thus averting the condition noted. Contract amendment action is being requested to make these guidelines applicable to this grant. (See Answer 7 below.)

7. *Amend grant agreement to reflect correct guidelines.*
   Grantee Response: None required.
   ARC Response: ARC will amend the grant agreement for WV-13336 to incorporate the "Development Venture Capital Application and Operating Guidelines" and eliminate the Strategic Capital Investment Fund guidelines. The later guidelines were incorporated prior to the adoption of the "Development Venture Capital Application and Operating Guidelines" by the Commission. These later guidelines are no longer relevant and have been superceded by the "Development Venture Capital Application and Operating Guidelines".

The Conservation Fund (TCF)

Audit of ARC grant #WV-13336 – Findings and Recommendations

The "draft audit report" noted that the majority of expenditures reviewed were allowable, reasonable, and properly allocated, and that TCF complied with the grant agreement provisions and other important requirements in most material respects. However, the following matters were brought to our attention and require improvement and/or further documentation:

1) **Recommendation**: Disallow the $4,299 in expenditures claimed by TCF under the grant that are questioned unless additional documentation can be provided . . . .

   TCF Response: Additional documentation is attached for the $853.75 in airfare incurred by Marten Jenkins on 2/27/01 and the $432.91 in airfare and $450.00 in registration fees incurred by Marten Jenkins on 2/28/01 – 3/02/01. All of these expenses were necessary, reasonable and allocable to the ARC grant.

   The remaining expenditures questioned, including $294 for a rental car, $1,063 for Web Site development, and $1,205 for brochures should be refunded to ARC as they were miss-coded and should not have been allocated to the ARC grant (total amount = $2,562).

2) **Recommendation**: Request TCF to expedite the establishment of written procurement procedures and to amend its travel procedures to require formal approval prior to travel.

   TCF Response: We have revised Chapter IX of the TCF Financial Management Handbook dealing with Government Grants, Cooperative Agreements and Awards (copy attached) with more detailed procurement procedures, including the competitive bid process, cost and price analysis, and sole source justifications. The revisions have been released and reviewed with all staff. Travel procedures have not been revised, and all travel will continue to be approved via the annual operating budget process.

3) **Recommendation**: Require TCF to take action to ensure their procedures reflect A-110 requirements for documenting matching amounts claimed and that grant managers are aware of them.

   TCF Response: We have revised Chapter IX of the TCF Financial Management Handbook dealing with Government Grants, Cooperative Agreements and Awards with more detailed procedures regarding documentation and substantiation of matching costs, and the revisions have been released and reviewed with all staff.

4) **Recommendation**: ARC should ensure that all grant personnel responsible for approving cash advances are aware of A-110 requirements and that advances to grantees for making loans or investments such as under WV-13336 are not made before reasonable assurance is obtained that the loan or investment will definitely be completed.

   TCF Response: Although this recommendation was addressed more directly to ARC, we felt that the recommendation was also applicable to TCF and thus warranted further attention. In response to this recommendation we added more specific language on "billings" and the timing of cash advances to Chapter IX of the TCF Financial Management Handbook dealing with Government Grants, Cooperative Agreements and Awards. These revisions have also been released and reviewed with all staff.