



September 8, 2004

Memorandum for:    The Federal Co-Chair  
                                  ARC Executive Director

Subject:                OIG Report 04-15  
                                  Review of Revolving Loan Fund (RLF) Grants for the  
                                  Regional Development and Energy Corporation

Attached are copies of the subject report dealing with the RLF grants to the Regional Development and Energy Corporation (REDEC). REDEC received its initial RLF grant in 1980. As of September 30, 2003, REDEC has received \$1,450,000 in ARC RLF grants, and has 40 loans outstanding, with unpaid balances totaling approximately \$1,230,500.

The report contains two recommendations. The responses by the grantee and ARC are considered responsive to the recommendation. They have agreed to take the necessary steps outlined in the recommendations.

This report is considered closed. However, ARC staff should verify that the promised actions have indeed taken place. Please contact me if you have any questions on this issue.

A handwritten signature in black ink, appearing to read "Cliff H. Jennings", written in a cursive style.

Clifford H. Jennings  
Inspector General

Attachment

cc:     Director for Program Operations  
          Director for Finance and Administration



**LEON SNEAD  
& COMPANY, P.C.**

*Certified Public Accountants  
& Management Consultants*

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

**MEMORANDUM**

**DATE:** September 3, 2004

**TO:** Clifford Jennings, Inspector General  
Appalachian Regional Commission  
Office of Inspector General  
1666 Connecticut Avenue, N.W. Room 215  
Washington, DC 20009-1068

**FROM:**   
Leon Snead, President

**SUBJECT:** Final Audit Reports

Leon Snead & Company is submitting to ARC and Grantee Officials five copies of the audit reports for the following assignments.

Buckeye Hills – Hocking Valley Regional District  
Buckeye Hills – Hocking Valley Regional District (Distressed)  
Southern Tier Enterprise Development Organization  
Regional Economic Development and Energy Corporation

Enclosure

---

**APPALACHIAN REGIONAL COMMISSION  
OFFICE OF INSPECTOR GENERAL  
AUDIT OF REVOLVING LOAN FUND  
Regional Economic Development  
and Energy Corporation**

---

**Report No. 04-15  
September 2004**

**Prepared by  
Leon Snead & Company, P.C.**



LEON SNEAD  
& COMPANY, P.C.

Certified Public Accountants  
& Management Consultants

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

September 1, 2004

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

Leon Snead & Company, P.C. has completed an audit of the Regional Economic Development and Energy Corporation (REDEC) Revolving Loan Fund (RLF). The audit was performed at the request of the Appalachian Regional Commission's (ARC), Office of the Inspector General (OIG) to assist in carrying out its oversight of ARC activities.

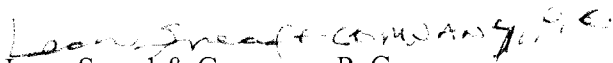
The audit objectives were to determine if: (1) the grantee complied with the requirements of applicable laws, OMB Circulars, ARC Guidelines and its grant agreement and operating plan (2) the grantee's internal control policies and procedures were adequate to assure that RLF transactions were properly recorded, and accurately and timely reported to the ARC on its semiannual reports, (3) administrative costs reported on the semiannual reports were allowable, supported and reasonable, and (4) appropriate actions have been taken to resolve or correct deficiencies identified in prior audits and reviews.

The audit determined that, overall, the REDEC: (1) operated the RLF in compliance with ARC regulations and guidelines, the grant agreement, and operating plan; and (2) implemented sufficient internal controls to assure semiannual reports to ARC were completed in a timely manner. However, we noted that REDEC's RLF Operating Plan did not fully meet ARC requirements; and (2) the September 30, 2003, semiannual report submitted to ARC was not accurate.

A draft report was provided to ARC and RLF officials for comment on July 7, 2004. The Executive Director, ARC agreed with the findings and recommendations. The comments of the Executive Director are included in their entirety in Appendix A.

Leon Snead & Company appreciates the cooperation and assistance received from REDEC and ARC personnel during the audit.

Sincerely,

  
Leon Snead & Company, P. C.

## TABLE OF CONTENTS

---

Introduction.....	1
Objective, Scope and Methodology.....	1
Summary of Audit.....	2
Findings and Recommendation.....	3
1. RLF Operating Plan .....	3
2. Semiannual Financial Reports .....	4
Appendix A – Management Response.....	5

## **Introduction**

Leon Snead & Company, P.C. has completed an audit of the Revolving Loan Fund (RLF) grant awarded by the Appalachian Regional Commission (ARC) to Regional Economic Development and Energy Corporation (REDEC). The audit was performed at the request of ARC's Office of the Inspector General (OIG) to assist it in carrying out its oversight of ARC grant activities.

REDEC was incorporated on August 26, 1980, under Section 402 of the Not-for-Profit Law of the State of New York. The corporation was formed to promote economic and energy development within the counties of Chemung, Schuyler and Steuben. REDEC's primary objectives are to: (1) facilitate increased local energy reliance; (2) conduct scientific research; and (3) operate a revolving loan fund for the advancement of economic, energy and scientific development projects and activities.

REDEC received its initial RLF grant in 1980. As of September 30, 2003, REDEC had received \$1,450,000 in ARC grant funds, and had 40 loans outstanding, with unpaid balances totaling approximately \$1,230,500.

A RLF is a business development revolving loan fund that is used by eligible grantees to make loans to create and/or save jobs. As borrowers repay loans, the money is returned to the RLF to make other loans. RLF loans are not intended to match or replace the capacity of lending institutions, rather, RLF's fill gaps in local lending, and provide capital which otherwise would not be available for economic development.

The grantee is required to administer the RLF in accordance with its grant agreement and operating plan. The operating plan, developed by the grantee as part of the grant agreement, defines specific objectives and operating procedures, including standards and selection criteria for loans in the portfolio. ARC does not review and approve individual loans made by the RLF. Instead, ARC monitors RLF activities for conformance with applicable laws, RLF Guidelines, operating plan, and other conditions of the grant agreement.

## **Objectives, Scope, and Methodology**

The audit objectives were to determine if: (1) the grantee complied with applicable laws, OMB Circulars, ARC Guidelines, its grant agreement and operating plan, (2) the grantee's internal control policies and procedures were adequate to assure that RLF transactions were properly recorded, and accurately and timely reported to ARC on its semiannual reports, (3) administrative costs reported on semiannual reports were allowable, supported and reasonable, and (4) appropriate actions have been taken to resolve or correct deficiencies identified in prior audits and reviews. The audit covered REDEC activities during the period October 1, 2002 to March 31, 2004. Audit fieldwork was completed at REDEC on June 29, 2004.

We reviewed grantee policies and operating procedures to gain an understanding of the grantee's system of administrative and accounting controls. In addition, we accessed the accounting and administrative controls established by REDEC to assure RLF operations adhered to applicable ARC Guidelines, OMB regulations, and REDEC's grant agreement and operating plan. The audit included tests of REDEC's subsidiary and detailed loan records to assure the financial information submitted to ARC was supported. We verified that loans made by the grantee complied with ARC Guidelines and the RLF operating plan. We performed tests of selected administrative costs claimed by REDEC to validate that the costs were allowable, reasonable and supported. We also reviewed REDEC's most recent single audits, and ARC internal reviews to ensure that corrective actions were taken on any reportable or material weaknesses identified in the reports.

The audit was performed in accordance *Government Auditing Standards*, and included appropriate tests necessary to achieve the audit objectives.

### **Summary of Audit**

The audit determined that REDEC: (1) generally operated the RLF in compliance with ARC guidelines, the grant agreement, and operating plan; and (2) implemented sufficient internal control policies and procedures to assure semiannual reports to ARC were completed in a timely manner. However, we determined REDEC needed to strengthen its procedures and controls to ensure that the RLF Operating Plan fully meets ARC requirements, and semiannual financial reports are accurate. These matters are discussed in the Findings and Recommendations section of this report.

## **FINDINGS AND RECOMMENDATIONS**

### **1. RLF Operating Plan**

The current REDEC RLF Operating Plan did not include a certification or statement of assurance that the RLF will be managed and operated in accordance with ARC requirements and regulations. Consequently, the Operating Plan did not fully comply with ARC regulations.

ARC RLF Guidelines, Section III.C.2 requires that the Plan include an affirmation that the grantee understands and agrees to operate the RLF in accordance with the ARC policies contained in the Guidelines. ARC relies on this affirmation as a basis for releasing loan funds.

We reviewed REDEC's current RLF Operating Plan to determine whether the plan included the requirements specified in the ARC RLF Guidelines. We determined that the Plan did not include assurances or certifications that the RLF will be managed and operated in accordance with ARC policies and guidelines. We discussed this matter with REDEC officials. They agreed that the current Plan did not include this requirement, and the Plan needed to be revised accordingly.

Prior to completing the audit fieldwork, REDEC revised its Operating Plan. We reviewed the revised Plan and determined it now included appropriate assurances that the RLF will be managed and operated in accordance with ARC requirements. Consequently, no recommendations are being made.

### **Management Response**

Although we did not make a recommendation, the ARC Executive Director and REDEC concurred with the finding. The Executive Director stated that ARC has received a revised operating plan from REDEC, and it included the required affirmation that the RLF will be operated in accordance with the ARC RLF Guidelines.

### **Auditor's Comments**

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



## **2. Semiannual Financial Reports**

REDEC's September 30, 2003, semiannual financial report was inaccurate. The report understated three cost elements by approximately \$1,500. As a result, ARC did not receive accurate and complete cost information.

ARC RLF Guidelines, Section VI.E requires grantees to provide accurate and timely financial reports. Section VI.F.6 states that grantee reports and accounting systems must include an accurate accounting for any principle repayments, loan interest, loan fees, or other income generated by the RLF, and must document how these funds are used.

We reviewed REDEC's accounting records to identify the costs and expenditures for the period April 1, 2003 through September 30, 2003, and compared this data with the amounts reported on the September 30, 2003, semiannual financial report. We determined that three cost elements were understated. The cost elements and amounts of understatement were as follows.

- Loan fees were understated by \$1,200.
- Investment interest was understated by \$115.
- Late payments were understated by \$134.

REDEC officials agreed these cost elements were understated on the semiannual report. They believed the understatements occurred because necessary adjustments were made to the accounting records after the report was prepared. They stated that ARC had changed their semiannual financial reporting period, and the ending date for the next report was June 30, 2004. They agreed to review the understatements, and make appropriate adjustments on June 30, 2004, report.

### **Recommendation**

ARC should ensure REDEC's June 30, 2004, semiannual financial report accurately reflects the loan fees, investment interest and late payments associated with the RLF.

### **Management Response**

The ARC Executive Director concurred with the finding and recommendation. The Executive Director stated that ARC relies on the grantee's accuracy certification on Schedule B-1 of the RLF Financial Report, and REDEC's annual independent audit report to ensure the accuracy of all financial information.

### **Auditor's Comments**

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

**APPENDIX A  
MANAGEMENT RESPONSE**



APPALACHIAN  
REGIONS  
COMMISSION

*A Proud Past,  
A New Vision*

August 26, 2004

Leon Snead, President  
Leon Snead & Company, P.C.  
416 Hungerford Drive, Suite 400  
Rockville, Maryland 20850

Subject: Management Response to ARC Inspector General Audit of the ARC Funded Revolving Loan Fund at the Regional Economic Development and Energy Corporation, Painted Post, New York performed by Leon Snead & Company, P.C.

Dear Mr. Snead:

Thank you for your thorough examination of the Regional Economic Development and Energy Corporation (REDEC) ARC RLF grant. The assistance provided by this examination will aid REDEC in keeping their RLF Operating Plan fully compliant with ARC RLF Guidelines. Please correct the typographical error on the first line (RFL) of the third paragraph of the introduction on page 1 of the draft report. According to grant records at ARC REDEC accepted their initial grant offer on September 29, 1980. As of September 30, 2003 REDEC had received \$1,450,000 in ARC grant funds. Please change the second sentence accordingly.

RLF Operating Plan.

ARC agrees with the finding that the REDEC RLF Operating Plan did not include an affirmation that the ARC funded RLF would be operated in accordance with ARC RLF polices contained in the BDRLF Guidelines


ARC has received a revised operating plan from REDEC. This plan included the required affirmation that the ARC funded RLF would be operated in accordance with ARC RLF polices contained in the BDRLF Guidelines. The required affirmation is signed by the grantee's Executive Director who is also the Project Director, as required by ARC BDRLF Guidelines, paragraph III.C.2.

Semiannual Financial Reports.

ARC agrees with the finding and recommendation regarding the accuracy of semiannual financial reports.

ARC relies on the accuracy certification of the grantee on Schedule B-1 of the RLF Financial Report and the REDEC annual independent auditors report to ensure the accuracy of all financial information. The independent auditors' report of Carnevale Niles Whitney & Davis, P.C. dated November 5, 2003 stated that the statements were presented fairly in all material respects.

Sincerely,

  
Thomas M. Hunter  
Executive Director