



August 4, 2005

Memorandum for: The Federal Co-Chair
 ARC Executive Director

Subject: OIG Report 05-19
 Review of Revolving Loan Fund (RLF) Grants for the
 Tri-County Council for Western Maryland, Incorporated

Attached are copies of the subject report dealing with the RLF grants to the Tri-County Council for Western Maryland, Incorporated (the Council). The Council received its initial RLF grant in 1985. As of February 28, 2005, the Council had received \$1,146,700 in ARC RLF grants, and has 17 loans outstanding, with unpaid balances totaling approximately \$1,041,000.

The report contains two recommendations. The responses by the grantee and ARC are considered responsive to the recommendations. 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.

Clifford H. Jennings
Inspector General

Attachment

cc: Director for Program Operations
 Director for Finance and Administration

**APPALACHIAN REGIONAL COMMISSION
OFFICE OF INSPECTOR GENERAL
AUDIT OF REVOLVING LOAN FUND
Tri-County Council for Western Maryland,
Incorporated
Cumberland, Maryland**

**Report No. 05-19
July 2005**

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



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July 26, 2005

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 Tri-County Council for Western Maryland, Incorporated (the Council) Revolving Loan Fund (RLF). The audit was performed at the request of the Appalachian Regional Commission (ARC), Office of the Inspector General (OIG), to assist in its oversight of ARC operations.

The primary objective of the audit was to ensure that the Council operated the ARC RLF in accordance with the grant agreement, and its RLF operating plan. The audit covered the period October 1, 2003 through April 7, 2005. Audit work at the grantee's office was completed on April 7, 2005.

The audit determined that the Council: (1) generally operated the RLF in compliance with ARC regulations and guidelines, the grant agreement, and operating plan; and (2) implemented sufficient internal control policies and procedures to assure semiannual reports to ARC were completed accurately and timely. However, we determined that the Council needed to strengthen its procedures and controls to ensure: (1) the RLF Operating Plan fully complies with ARC requirements; and (2) excess loan funds are refunded to ARC. These areas are discussed in the Findings and Recommendations section of this report.

A draft report was provided to ARC and RFL officials on May 19, 2005. The ARC Director of Finance and Administration provided documentation in a letter dated June 24, 2005 addressing our audit recommendations. These comments are included in their entirety in Appendix A.

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

Sincerely,

Leon Snead & Company, P.C.
Leon Snead & Company, P. C.

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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 the Tri-County Council for Western Maryland, Incorporated (the Council). 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.

The Council was established in 1971 to serve Garrett, Allegany and Washington counties. The purposes for which the Council was formed include: (1) advancing the economic, social, and cultural welfare of its constitute counties; (2) conducting a continuing comprehensive development planning program; (3) serving as a cooperative economic, social and cultural development agency; (4) providing assistance and support to public and private institutions, organizations, agencies and groups; (5) providing liaison with local, State and Federal agencies; (6) planning and preparing studies to support comprehensive development planning; and (7) participating in Federal government-sponsored development programs and activities, including those authorized by the Appalachian Regional Development Act of 1965.

The Council received its ARC grant on July 1, 1985. As of February 28, 2005, the Council had received \$1,146,700 of ARC funds, and had 17 outstanding loans with unpaid balances totaling approximately \$1,041,000.

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 plans, 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

Council activities during the period October 1, 2003 to April 7, 2005. Audit fieldwork was completed at the Council on April 7, 2005.

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 the Council to assure RLF operations adhered to applicable ARC Guidelines, OMB regulations, and the Council's grant agreement and operating plan. The audit included tests of the Council'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 the Council to validate that the costs were allowable, reasonable and supported. We also reviewed the Council's most recent single audit, 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 with *Government Auditing Standards*, and included appropriate tests necessary to achieve the audit objectives.

Summary of Audit

The audit determined that the Council: (1) generally operated the RLF in compliance with ARC guidelines, the grant agreements, and operating plans; and (2) implemented sufficient internal control policies and procedures to assure semiannual reports to ARC were completed accurately and timely. We determined, however, that the Council needed to strength its procedures and controls to ensure: (1) the RLF Operating Plan fully complies with ARC requirements; and (2) excess loan funds are refunded to ARC. These areas are discussed in the Findings and Recommendations section of this report.

FINDINGS AND RECOMMENDATIONS

1. RLF Operating Plan

The Council's current RLF Operating Plan did not include: (1) a certification or statement of assurance that the RLF will be managed and operated in accordance with ARC requirements; and (2) information on the commercial lending experience of the Loan Review Committee members. Consequently, the Council was not fully complying with ARC requirements.

ARC RLF Guidelines, Section III.C.2 requires that Operating Plans 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.

Section III.C.1.d of the Guidelines states that RLF Operating Plans must include the names of Loan Review Committee members and a description of each member's commercial loan experience.

We reviewed the Council's current RLF Operating Plan to determine whether it included the requirements specified in the ARC RLF Guidelines. We determined that the Operating Plan did not include: (1) assurances or certifications that the RLF will be operated in accordance with ARC policies and procedures; and (2) information on the commercial loan experience of the Loan Review Committee members. We discussed these matters with Council officials. They agreed the Operating Plan should be revised to include the required affirmation and information on the commercial lending experience of the Loan Review Committee members.

Recommendation

ARC should require the Council to revise its RLF Operating Plan to include: (1) assurances that the RLF will be managed and operated in accordance with the ARC RLF Guidelines; and (2) information on the commercial lending experience of the Loan Review Committee members.

Management Response

The ARC Director of Finance and Administration responded that the Council provided ARC a revised Revolving Loan Fund Management Plan. The revised Plan included appropriate assurances that the RLF will be managed and administered in accordance with the ARC RFL Guidelines. The revised Plan also included a current list of loan review committee members and their commercial lending experience.

Auditor's Comments

The comments are responsive to the finding and recommendation.

2. Excess Loan Funds

The Council had excess loan funds of \$30,177 that should be refunded to ARC.

ARC RLF Guidelines, Section VI.D, "Excess Unloaned Funds" states that a grantee holding unloaned RLF cash in excess of 25% of the outstanding loan principal or in excess of \$200,000, as reported in the grantee's semiannual financial report, is deemed to be holding excess unloaned cash. If the next semiannual financial report shows that excess cash is still being held, the grantee must return the excess funds to ARC.

We determined that the March 31, 2004 and August 31, 2004 semiannual financial reports showed that the Council had excess unloaned cash. The amount of excess cash as of March 31, 2004, was approximately \$67,000. As of August 31, 2004, the amount of excess cash was approximately \$46,000. We also determined that the semiannual financial report for the period ending February 28, 2005 showed that the Council still had excess cash. The amount of excess cash as of February 28, 2005 was \$30,177. On March 28, 2005, the ARC RLF Program Manager directed the Council to immediately refund this amount to ARC.

We discussed this matter with Council officials. They stated that checks are prepared and processed on or about the 15th of each month. Consequently, they planned to refund the excess cash to ARC on about April 15, 2005.

Recommendation

ARC should ensure the Council refunds \$30,177 of excess cash.

Management Response

The ARC Director of Finance and Administration responded that the Council returned \$30,777 of excess loan funds to ARC on April 26, 2005.

Auditor's Comments

The comments are responsive to the finding and recommendation.



**APPALACHIAN
REGIONAL
COMMISSION**

*A Proud Past,
A New Vision*

June 24, 2005

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 Center for the Tri-County Council for Western Maryland performed by Leon Snead & Company, P.C.

Dear Mr. Snead:

Thank you for your examination of the Tri-County Council for Western Maryland (TCCWM) ARC RLF grant contract MD-9235. The assistance provided by this examination will enhance ARC's oversight over the grantee's activities. The following is provided as comment on the draft report.

The Audit of Revolving Loan Fund states on page 1, Introduction section, that the Tri-County Council for Western Maryland that TCCWM is a wholly owned instrumentality of the Appalachian Regional Commission. This is not true. The Appalachian Regional Commission does not have any wholly owned instrumentalities.

RLF Operating Plan

The Tri-County Council for Western Maryland has provided ARC with a revised ARC Revolving Loan Fund Management Plan. The revised plan includes the grantee assurance, signed by the TCCWM Executive Director, required by paragraph III.C.2. ARC BDRLF Guidelines. This item is considered closed.

The revised TCCWM ARC RLF Management Plan includes as attachment A a current list of loan review committee members and their commercial lending experience. The current membership complies with ARC BDRLF Guideline requirements. This item is considered closed.

Excess Loan Funds

The grantee returned \$30,777 in excess unloaned cash to ARC on April 26, 2005. This amount was returned to the TCCWM RLF Grant on April 27, 2005. This item is closed.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert M. Decker", written in a cursive style.

Robert M. Decker, Director
Finance and Administration