



March 16, 2006

Memorandum for: The Federal Co-Chair
 ARC Executive Director

Subject: OIG Report 06-06
 Review of Revolving Loan Fund (RLF)
 Operated by the East Central Planning and
 Development District
 Newton, Mississippi

Attached is the subject report dealing with the RLF grant to the East Central Planning and Development District. Currently, the East Central Planning and Development District RLF grant had a balance of \$478,499. The East Central Planning and Development District received its initial RLF grant in 1988 with a grant of \$158,000. As of April 30, 2005, the East Central Planning and Development District had three loans outstanding, with an unpaid balance totaling approximately \$ 237,329.

The report includes six recommendations. This report will be kept open until the recommendations have been satisfied.

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

Clifford H. Jennings
Inspector General

Attachment

cc: Director for Program Operations
 Director for Finance and Administration
 Mary Moran



**AUDIT OF THE ARC REVOLVING LOAN
FUND OPERATED BY
EAST CENTRAL PLANNING AND
DEVELOPMENT DISTRICT
NEWTON, MISSISSIPPI**

ARC GRANT NUMBER: (MS-10282-89-I-302-0330)

March 8, 1988 through April 30, 2005

ARC OIG Report Number: 06-06

Date: March 7, 2006

CAUTION: Certain information contained herein is subject to disclosure restrictions under the Freedom of Information Act, 5 U.S.C. 522 (b) (4). Distribution of this report should be limited to Appalachian Regional Commission and other pertinent parties.

**ALLMOND & COMPANY
Certified Public Accountants
8181 Professional Place, Suite 250
Landover, Maryland 20785
(301) 918-8200**

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ALLMOND & COMPANY

8181 PROFESSIONAL PLACE, SUITE 250
LANDOVER, MARYLAND 20785

CERTIFIED PUBLIC ACCOUNTANTS

(301) 918-8200
FACSIMILE (301) 918-8201

MARVIN C. ALLMOND, CPA

Appalachian Regional Commission
Office of Inspector General

INDEPENDENT AUDITOR'S REPORT

We have audited the Appalachian Regional Commission (ARC) Revolving Loan Fund (RLF) grant Schedule of Fund Balance of East Central Planning and Development District as of April 30, 2005, and the related Statement of Source and Application of Funds for the period of March 8, 1988 through April 30, 2005. These financial statements are the responsibility of East Central Planning and Development District. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. We also used the ARC Office of Inspector General (OIG) Audit Guide of ARC Revolving Loan Funds as a guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the accompanying ARC RLF grant financial statements present fairly in all material respects the financial position of East Central Planning and Development District's fiduciary activities as of April 30, 2005 and the source and application of funds resulting from fiduciary activities for the period of March 8, 1988 through April 30, 2005 in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated November 18, 2005 on our consideration of East Central Planning and Development District's internal control over ARC RLF grant financial reporting and on our tests of compliance with certain provisions of laws and regulations, included herein. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Allmond & Company

Allmond & Company
Landover, Maryland
November 18, 2005

**EAST CENTRAL PLANNING AND DEVELOPMENT DISTRICT
SCHEDULE OF FUND BALANCE**

AS OF APRIL 30, 2005

Cash in Bank	\$ 169,687
Loans Outstanding	<u>237,329</u>
Fund Balance	<u>\$ 407,016</u>

**EAST CENTRAL PLANNING AND DEVELOPMENT DISTRICT
STATEMENT OF SOURCE AND APPLICATION OF FUNDS**

For the period March 8, 1988 through April 30, 2005

SOURCE OF FUNDS

ARC Grant	\$ 478,499
Loan Principal Repayments	400,670
Loan Interest Income	153,745
Investment Interest Income	23,139
Fees Charged	11,608
Other	<u>0</u>
Total Funds Available	<u>\$1,067,661</u>

APPLICATION OF FUNDS

Cash in Bank	\$ 169,687
Loans Disbursed by Grantee	638,000
Grant Funds Returned to ARC	258,971
Administrative Costs	30,799
Application of Funds Not Accounted For	<u>(29,796)</u>
Total Funds Applied	<u>\$1,067,661</u>



MARVIN C. ALLMOND, CPA

Appalachian Regional Commission
Office of Inspector General

**REPORT ON COMPLIANCE AND ON INTERNAL CONTROLS
OVER FINANCIAL REPORTING BASED ON
AN AUDIT OF THE FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

We have audited the Appalachian Regional Commission (ARC) Revolving Loan Fund (RLF) grant financial statements of East Central Planning and Development District as of and for the period of March 8, 1988 through April 30, 2005, and have issued our report thereon dated November 18, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

COMPLIANCE

As a part of obtaining reasonable assurance about whether East Central Planning and Development District's ARC RLF grant financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered East Central Planning and Development District's internal control over financial reporting for the ARC RLF grant in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal controls over financial reporting. However, we noted certain matters involving internal controls over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant

deficiencies in the design or operation of the internal controls over financial reporting that, in our judgment, could adversely affect East Central Planning and Development District's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Six reportable conditions were identified during the audit and are described in the accompanying Summary Report.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal controls over financial reporting would not necessarily disclose all reportable conditions that are considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness.

This report is intended solely for the information and use of the ARC; however, the final report is a matter of public record and its distribution is not limited.

Allmond & Company

Allmond & Company
Landover, Maryland
November 18, 2005

SUMMARY REPORT

INTRODUCTION

The Appalachian Regional Commission (ARC) makes grants to grantees. The grantee uses the grant funds to make loans to achieve economic benefits for a designated project area. As the loans are repaid, the principal funds and interest in excess of expenses are returned to the Revolving Loan Fund (RLF) to make other loans. The program's primary goal is private sector job creation and capital formation, specifically in the Appalachian region.

ARC requires that RLF projects be administered in accordance with the grantee's RLF plan. This plan explicitly defines the specific objectives and operating procedures, including the standards and selection criteria that are used to grant funds through the RLF for loans. ARC does not approve or review the RLF loans on an individual basis. ARC monitors the RLF project grantee objectives for conformance with guidelines, the RLF plan and other grant agreement conditions. The grantee is required to submit financial and progress reports to the ARC on a bi-yearly basis.

OBJECTIVES OF THE AUDIT

The objectives of the audit were (1) to determine whether East Central Planning and Development District (ECPDD) is administering its ARC RLF in accordance with the ARC approved grant and did not violate any restrictions imposed by the terms and conditions of the RLF grant, (2) to determine whether the accounting, reporting and internal control structure of the ECPDD provides for the disclosure of pertinent financial and operation information applicable to the revolving loan program, and (3) to determine whether the objectives of the grant are being met.

BACKGROUND

In March 1988, ARC granted the ECPDD \$158,000 in accordance with Grant Number MS-1082-89-I-302-0330. The ECPDD has been an active lender through the RLF program since 1989. Currently, the ECPDD RLF grant with ARC has a balance of \$478,499. Since the inception of the original grant to ECPDD, the grant program has expanded to create assistance loans for capital investments for the creation and/or retention of jobs in the East Central region of the State of Mississippi.

SCOPE OF AUDIT

Allmond & Company, a certified public accounting firm, was contracted by the ARC's Office of Inspector General (OIG) to perform a financial, compliance, and internal control audit in accordance with Government Auditing Standards and ARC, OIG Audit Guide for Revolving Loan Funds of the ARC grants administered by the ECPDD for the period March 8, 1988 through April 30, 2005.

As of April 30, 2005, ECPDD had three ARC RLF loans outstanding, with an unpaid balance of \$237,329.

AUDIT RESULTS

As a result of the audit performed, we concluded that (1) ECPDD was administering its ARC RLF in accordance with the ARC approved grant and nothing came to our attention that they were violating restrictions imposed by the terms and conditions of the RLF grant, (2) ECPDD 's accounting, reporting, and internal control structure provided for the disclosure of pertinent financial and operation information applicable to the revolving loan program, and (3) ECPDD was meeting the objectives of the grant program. We found no material weaknesses and six reportable conditions.

REPORTABLE WEAKNESS IN INTERNAL CONTROL

Finding 1: Unreconciled Difference in Cash Balance and Funds Available for Loans

ECPDD reconciliation procedures over cash and/or funds available for loans is not design to explain or reconcile the differences between the funds available for loans reported on the Statement of Funds Available as of April 30, 2005 and the ARC revolving loan fund (RLF) cash balance reported per general ledger and bank as of April 30, 2005. Our procedures revealed a difference of \$29,796 between the funds available for loans and the cash balance per bank. ECPDD was unable to provide an explanation or reconciliation to support the accuracy and reasonableness of the difference.

The *Standards for Internal Controls in Federal Government* issued by the Government Accountability Office (GAO) states, "Control activities occur at all levels and functions of an entity. They include a wide range of diverse activities such as approvals, authorizations, verifications, reconciliations, performance reviews, maintenance of security, and the creation and maintenance of records which provide evidence of execution of these activities as well as appropriate documentation."

Failure to maintain accurate records could result in funds being expended for purposes contrary to ARC objectives and/or a reduction in the RLF capital base and the amount of funds available to loan. In addition, the lack of the reconciliation directly affects ECPDD ability to adequately identify the source and application of federal activities. Specifically, ECPDD inability to account for the application of \$29,796 reported on the Statement of Sources and Application of Funds.

Recommendation:

We recommend that ECPDD reconcile the general ledger and bank statement balance to the funds available for loans balance on the Statement of Funds Available. The resulting reconciling items should be properly documented and transfers executed to correct the

bank account and general ledger account balances to properly reflect the ARC funds available.

Auditee's Response:

The auditee did not concur with the finding. The fiscal officer stated that ARC policies and procedures do not require a separate bank account to maintain ARC funds. Additionally, there is no requirement for the bank account to agree to the funds available balance on the Statement of Funds available.

Auditor's Conclusion:

We believe that, with the implementation of the recommendation noted above, ECPDD will be in compliance with the requirements and responsibilities of its ARC approved grant, and its internal control structure will be strengthened.

Finding 2: Administrative Costs were Unsupported

ECPDD Administrative Costs reported on the Statement of Funds Available as of April 30, 2005 was not properly supported by underlying calculations or other documentation. Specifically, ECPDD was unable to provide supporting documentation or underlying calculations for approximately \$13,244 of the total \$30,799 in administrative costs. The unsupported cost appeared to have been incurred in the period May 1989 through October 1996.

ARC Business Development Revolving Loan Fund Guidelines, revised October 1999, states, "Grantees must keep complete records (e.g., time cards, logs, invoices, vouchers) to document those administrative costs. Administrative costs include direct costs that are specifically identifiable to an RLF cost and indirect costs which are incurred for common objectives."

Failure to maintain accurate records could result in funds being expended for purposes contrary to ARC objectives.

Recommendation:

We recommend that ECPDD management and employees adhere to the RLF Guidelines, which states that grantees must keep complete records to document administrative costs.

Auditee's Response:

The auditee did not concur with the finding. ECPDD stated that the cost activity periods of May 1989 through October 31, 2002 fall outside of their records retention policy.

Auditor's Conclusion:

We believe that with the implementation of the recommendation noted above, ECPDD will be in compliance with the requirements and responsibilities of its ARC approved grant, and its internal control structure will be strengthened.

Finding 3: Delinquent Loan Repayments not Reported to ARC Timely

Due to the inadequate design of internal controls over reporting delinquent payments, ECPDD did not report to ARC delinquent loan repayments in a timely manner. In particular, our procedures revealed that one borrower was one-month delinquent for over 26 months and no action was taken to collect the unpaid amount. Additionally, this delinquency was not properly reported to ARC on the List of Loans Outstanding. ARC Business Development Revolving Loan Fund Guidelines, revised October 1999, states, "Schedule B-3 requires a statement from the grantee on each delinquent loan outlining the actions underway to resolve the situation and/or preserve ARC's financial interests. Schedule B-3 is used to report grantee actions taken to resolve the delinquent status of certain loans."

Recommendation:

We recommend that ECPDD management design procedure to properly monitor loan repayments monthly and timely correspond with the borrower when payments are not received. Any communication with the borrower regarding delinquencies should be documented in the loan files whether the communication is verbal or written. All delinquencies should be properly reported on the semi-annual Listing of Loan Outstanding.

Auditee's Response:

The auditee concurred with the finding. The auditee stated that the missing loan payment was an oversight by ECPDD. The borrower was going to be contacted immediately to bring the loan current.

Auditor's Conclusion:

We believe that with the implementation of the recommendation noted above, ECPDD will be in compliance with the requirements and responsibilities of its ARC approved grant, and its internal control structure will be strengthened.

Finding 4: Employee Timesheets not Approved by Supervisor

Testing of internal controls over the payroll processing procedures revealed that semi-monthly timesheets for one employee were not signed by the employee's supervisor. We observed that the Executive Director's timesheets were not signed by a member of the

Board of Directors. ECPDD accounting procedures manual requires that each employee's time sheet be approved in writing by an assigned supervisor. In addition, the *Standards for Internal Controls in the Federal Government*, issued by the Government Accountability Office (GAO), states, "Proper Execution of Transactions and Events, Transactions and other significant events should be authorized and executed only by persons acting within the scope of their authority. This is the principle means of assuring that only valid transactions to exchange, transfer, use, or commit resources and other events are initiated or entered into. Authorizations should be clearly communicated to managers and employees."

Recommendation:

We recommend that a designated member of the ECPDD's Board of Directors indicate approval of the Executive Director's semi-monthly time and attendance form by signing it.

Auditee's Response:

The auditee did not concur with the finding. The auditee explained that the Executive Director does not have a supervisor to sign his timesheets. The members of the Board of Directors are not available to sign the Executive Director's timesheets.

Auditor's Conclusion:

We believe that with the implementation of the recommendation noted above, ECPDD will be in compliance with the requirements and responsibilities of its ARC approved grant, and its internal control structure will be strengthened.

Finding 5: Employee Timesheets Altered Without Evidence of Employee's Approval

Testing of internal controls over payroll processing procedures revealed several instances where the bookkeeper, employee's supervisor, or someone else altered the time sheets after submission by the employee. ECPDD accounting procedures manual requires that any correction be made in ink and initialed by the employee.

Recommendation:

We recommend that ECPDD adhere to the policies and procedures documented in their manual by ensuring that employees make any timesheet corrections in ink and initial the changes or instruct the employee to prepare a new timesheet to properly reflect the correct time allocation.

Auditee’s Response:

The auditee did not concur with the finding. The fiscal officer stated, “approval of any timesheet corrections is being documented by the employee’s immediate supervisor, or by the fiscal department staff for administrative changes such as the use of annual leave when sick leave is exhausted. The guidelines do not require both the employee and supervisor to approve the timesheet, and all entries on the timesheet are documented by the appropriate personnel.”

Auditor’s Conclusion:

We believe that the implementation of the policies and procedures documented in the accounting manual would reduce the risk of inaccurate time and attendance data being recorded in their system and its internal control structure will be strengthened.

Finding 6: Segregation of Duties not Observed in Processing and Accounting for Payroll

While testing the operating effectiveness of internal controls over processing payroll, we noted improper segregation of duties regarding the custody of time and attendance records and paycheck preparation. Specifically, our procedures revealed that the same person performs the duties of maintaining the time and attendance records and preparing paychecks. Proper internal control procedures require that the duties of maintaining time and attendance records and preparing paychecks be segregated. Failure to segregate these duties could lead to the misappropriation of funds.

In addition the *Standards for Internal Controls in the Federal Government*, issued by the Government Accountability Office (GAO) states, “key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event.”

Recommendation:

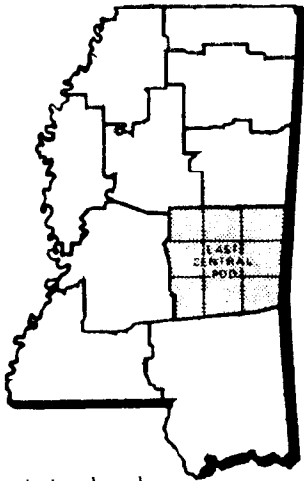
We recommend that the ECPDD management implement procedures that appropriately segregate the duties of maintaining time and attendance records and preparing paychecks.

Auditee’s Response:

The auditee did not concur with the finding. ECPDD stated, “Review of the timesheets and payroll information is done by the Fiscal Officer before the payroll clerk prepares the checks, and the payroll checks are periodically reconciled by the Fiscal Officer to ensure they reflect the reviewed information.”

Auditor's Conclusion:

We agree that implementation of the controls procedures would ensure that approval processes are not circumvented. Accordingly, the observation of an official's signature is an indication that he or she was aware and approved the transaction.



EAST CENTRAL PLANNING & DEVELOPMENT DISTRICT

P. O. BOX 499 - NEWTON, MISSISSIPPI 39345 - PHONE 601-683-2007

MR. BILL RICHARDSON, Executive Director

"Assisting local
units of Government"

BOARD OF DIRECTORS

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Newton County

Mr. Wilson Hallman, Vice President
Smith County

Mrs. Dot Merchant, Secretary
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Mr. Jimmie Smith, Treasurer
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Mr. Tony Fleming
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Scott County

Mr. Bob Cook
Director at Large

Mr. Paul Mosley
Director at Large

Mr. Leon Baxstrum
Director at Large

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Mr. Troy Chickaway
Director at Large

Mr. Tim Tubby
Director at Large

Mr. J.E. "Evon" Smith
Director at Large

Mr. Rayburn Waddell
Director at Large

Mr. Freddie Owens
Director at Large

January 24, 2006

Mr. Marvin Allmond, CPA
Allmond & Company, CPA's
8181 Professional Place, Suite 250
Landover, MD 20785

RE: RESPONSE TO DRAFT AUDIT REPORT TO ARC

Dear Mr. Allmond:

We received the draft copy of your audit report dated November 18, 2005 on January 17, 2006. We request and would appreciate the inclusion of our entire verbatim response in your final report. I hope that you would agree that paraphrasing might sometimes give a less than complete understanding of our response.

We take exception to the presentation of the financial statements in the audit report. The semi-annual report filed with the Appalachian Regional Commission for the period ending April 30, 2005 should have formed the basis of the financial statements, and appears to have been used as such except for the "Cash in Bank" and "Application of Funds Not Accounted For" line items which were created by your audit staff. The semi-annual report indicates "Funds Available for Loans" of \$139,891 as the amount that was reserved for future loan activity, and this amount should have been reported in the financial statements.

As more fully explained in our response to Internal Control Finding #1, we segregate the ARC RLF transactions in the accounting records utilizing restricted fund balance accounts. These restricted accounts do agree materially to the total amount reported as "Funds Available for Loans" and "Unpaid Loan Balance" to ARC. The internally designated bank account does not necessarily represent the amount of funds held for future loans, nor is it required to. Your staff's creation of the "Application of Funds Not Accounted For" line item to reconcile the difference between the cash account balance and the "Funds Available for Loans" is inappropriate.

Our responses to the internal control findings are as follows:

1. Unreconciled Difference in Cash Balance and Funds Available for Loans.

The *Grant Agreement* in section 2-8.1 calls for separate accounts to be used in the financial records of the District for ARC RLF activity. *OMB Circular A-110*, Section ___.21(b)(2) requires that the accounting records adequately identify the source and application of federal activities. We meet these requirements by accounting for current fiscal activity in a separate revenue and expense fund and by accounting for grant-to-date activity in a separate restricted fund balance account. These restricted account activities were subjected to the required annual audit procedures required by *OMB Circular A-133* and the RLF program. A separate cash account is not required under ARC guidelines.

The “ARC RLF Savings” cash account is an internally designated account used for the purpose of ensuring that all ARC RLF payments are posted to the correct revenue and expense fund and for allocating interest revenue to the ARC RLF program. Most of the difference between the balance in this account and the “Funds Available for Loan” on the semi-annual report is attributable to not transferring cash for allocations of the RLF operating expenses into the District’s general bank account. These activities were properly accounted for in the revenue and expense account and corresponding restricted fund balance account in the appropriate fiscal year, but the cash account was not subsequently adjusted for them. The remaining difference can be traced back to periods prior to 1996 which is beyond the records retention requirements detailed in our response to Internal Control Finding #2; however, we do not believe that any amounts were improperly recorded into the restricted fund balance during those periods either. This amount is not “Application of Funds Not Accounted For” as indicated in the financial statements prepared by your staff.

In addition, this cash account is not identified on any reports that are prepared for use outside of the district’s internal accounting staff. It is the restricted fund balance account that is used to determine what assets are being held for ARC. This internally designated cash account should be treated like a pooled cash account consisting partly of amounts held in restriction for future ARC loan activity and partly of amounts payable to ECPDD’s general bank account for reimbursement of allocated expenditures.

In order to avoid future confusion, we will either transfer the previously allocated expenditures into the general bank account or do away with the separate bank account altogether and move to a single pooled cash account that includes the ARC RLF program; however, we do not believe there is a violation of program guidelines or required internal controls.

2. Administrative Costs were Unsupported.

ARC RLF Guidelines specify in Section VI(F)(6) that the records retention requirements of *OMB Circular A-102* and/or *A-110* apply to this program. *OMB Circular A-102* does not apply to our organization, and *OMB Circular A-110*, Section ___.53 requires records to be maintained for a period of three years from the date reports are submitted to the granting federal agency unless

there is litigation, claim, or unresolved audit findings. The *Grant Agreement* in Section 2-8.3 requires an annual audit to be performed in accordance with *OMB Circular A-128* (since superceded by *OMB Circular A-133*).

We have had audits in accordance with *OMB Circular A-133*, submitted copies of the reports to ARC as required, and no litigation or claims against the ARC RLF program have been initiated. As of November 11, 2005 (the beginning date of the audit procedures), records were available to support the activity for the period covered by the October 31, 2002 report and thereafter as is required by program guidelines.

In order to comply with the Auditor's recommendation, RLF program administrators would have to keep documentary evidence of all expenditures made directly to the program, to an allocated cost pool, and to the indirect cost pool for an indefinite period of time regardless if those expenditures had been subject to required audit procedures under *OMB Circular A-133*. This is not only impractical, it is not required under the records retention requirements of the program.

The cost activity periods of May 1989 through October 1996 fall outside of the records retention policy specified in *OMB Circular A-110*, and therefore we do not believe there is a violation of program guidelines.

3. Delinquent Loan Repayments not Reported to ARC Timely.

This was one isolated instance where the subsequent loan payment was received less than one month after the missed payment and the loan analysis generated by the loan servicing software did not indicate the loan was more than 30 days behind. It is important to note that the loan was not 26 months delinquent, but rather was due to one payment that was missed 26 months ago. Subsequent payments were received. We will review all ARC loans to ensure that all scheduled loan payments have been received. We will also document oral communication with borrowers regarding payments.

4. Employee Timesheets not Approved by Supervisor.

Attachment B to *OMB Circular A-122*, Section (7)(m)(2)(c) requires that time reports be signed by the employee, or by a responsible supervisory official having first hand knowledge of the activities performed by the employee. Section 7(m)(1) of the same publication requires charges for salaries and wages to be based on documented payrolls approved by a responsible official(s) of the organization.

The employee in question, the Executive Director, does sign his timesheet, and the President of the Board of Directors approves the payroll prior to distribution. The Executive Director's salary is approved by the board annually, his salary is recorded in the indirect cost pool and is not charged directly to any program, and no discrepancy was noted between the amount authorized and paid to him. We believe this procedure meets the program guidelines and the lack of a specific signature on the individual timesheets is not a weakness in internal controls.

We will take this suggestion under advisement in clarifying our internal accounting policies and procedures related to payroll; however, we do not believe there is a violation of program guidelines.

5. Employee Timesheets Altered Without Evidence of Employee's Approval.

Attachment B to *OMB Circular A-122*, Section 7(m)(2)(c) requires that time reports be signed by the employee, or by a responsible supervisory official having first hand knowledge of the activities performed by the employee. Approval of any timesheet corrections is being documented by the employee's immediate supervisor, or by fiscal department staff for administrative changes such as the use of annual leave when sick leave is exhausted. The guidelines do not require both the employee and supervisor to approve the timesheet, and all entries on the timesheet are documented by the appropriate personnel.

As stated in "Objectives of the Audit", objective #2 was "to determine whether the accounting, reporting, and internal control structure of the ECPDD provides for the disclosure of pertinent financial and operation information applicable to the revolving loan program." The finding does not take exception with any required procedures, but rather with additional procedures outlined in the District's internal accounting policy. As such, we do not believe a condition reportable to the Appalachian Regional Commission exists.

Although the District's internal accounting procedures should not be authoritative in determining internal control weaknesses if the actual procedures followed are sufficient to meet program guidelines, we will take this suggestion under advisement in clarifying our internal accounting policies and procedures.

6. Segregation of Duties not Observed in Processing and Accounting for Payroll.

Existing procedures currently exist to ensure that the approval process is not circumvented. Review of the timesheets and payroll information is done by the Fiscal Officer before the payroll clerk prepares the checks, the detailed payroll register is initialed by the Fiscal Officer, and the payroll checks are periodically reconciled by the Fiscal Officer to ensure they reflect the reviewed information. These procedures are already in place and have been followed.

The original finding provided to us at the exit conference was "Improper Separation of Duties for Custody of Time Records and Paycheck Preparation" and involved only the situation that the payroll clerk prepared paychecks and maintained the timesheets. The original recommendation was "that the duties of maintaining time and attendance records and preparing paychecks be segregated." Our initial response detailing the above procedures was intended to refute the allegation that a weakness in internal controls existed simply because the payroll clerk maintained the timesheets. Sufficient other controls were in place to keep one person from controlling all key aspects of the payroll process.

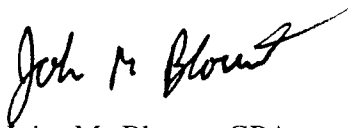
That the above control procedures were not observed is directly attributable to the fact that your audit staff did not inquire about or test further mitigating procedures after making the

determination that physical custody of the records was improper for the payroll bookkeeper.

The conclusion that implementation of the controls procedure would meet internal control requirements is unnecessary given that they are already in place.

We take our responsibilities seriously in protecting the government's interest in the ARC RLF program assets and ensuring they are utilized for the purpose they were intended. While we do not agree that your findings represent reportable conditions, we do appreciate the opportunity to document our reasoning and will await further correspondence from the Appalachian Regional Commission.

Sincerely,

A handwritten signature in black ink that reads "John M. Blount". The signature is written in a cursive style with a long, sweeping underline that extends to the right.

John M. Blount, CPA
Fiscal Officer