

**MEMORANDUM REPORT ON REVIEW OF
NORTH CENTRAL PENNSYLVANIA REGIONAL PLANNING &
DEVELOPMENT COMMISSION
(NCPRPDC)
RIDGWAY, PENNSYLVANIA**

**SECTION 302 (A)(1) ADMINISTRATIVE GRANT FOR LOCAL
DEVELOPMENT DISTRICT**

ARC Grant Number: PA-0708B

Grant Period: Fiscal Years Ending June 30, 2002, 2003, and 2004

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.*

Report Number: 06-15

Date: March 15, 2006

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Prepared By:

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Certified Public Accountants
304 Middletown Park Place, Suite C
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TO: Appalachian Regional Commission (ARC)
Office of Inspector General (OIG)

FROM: Tichenor & Associates, LLP
Louisville, Kentucky

REPORT FOR: Federal Co-Chair Anne B. Pope
ARC Executive Director Thomas M. Hunter
OIG Report Number: 06-15

SUBJECT: Memorandum Report on Review of North Central Pennsylvania
Regional Planning & Development Commission (NCPRPDC),
Section 302 (A)(1) Administrative Grant for Local Development
District, ARC Grant Number: PA-0708B.

PURPOSE: The purpose of our review was to determine if (a) the total funds provided to NCPRPDC for its Administrative Grant were expended in accordance with the ARC approved grant budget and did not violate any restrictions imposed by the terms and conditions of the grant; and (b) the accounting, reporting, and internal control systems provided for disclosure of pertinent financial and operating information

BACKGROUND: ARC awarded Grant Number PA-0708B to NCPRPDC for the fiscal years ending June 30, 2002, 2003, and 2004. Total ARC grant funding was for an amount not to exceed \$357,058 or 50 percent of actual, reasonable, and eligible project costs. ARC required that the grant be matched with \$357,058 or 50 percent in cash, contributed services, or in-kind contributions, as approved by the ARC. The ARC made payments to NCPRPDC in fiscal year 2002, 2003, and 2004, totaling \$261,014 as follows:

For The Fiscal Year Ended June 30, 2002: \$77,057

For The Fiscal Year Ended June 30, 2003: \$105,319

For The Fiscal Year Ended June 30, 2004: \$78,638

The grant is to provide funds for the purpose of assisting and enabling NCPRPDC to establish and expand economic development services that are deemed to be useful and pertinent to the accomplishment of the objective and purposes of the ARC.

The main objective of NCPRPDC is to help local entities in a six-county Appalachian region plan and develop projects to boost economic activity and the quality of life for the citizens of the region. In addition, NCPRPDC researches sources of funding available to local entities, and assists in the application and reporting process for the applicable funding.

The funds will provide assistance to NCPRPDC to pay for the costs of operating the office, which consist primarily of personnel costs and indirect costs.

SCOPE: We performed a review of the grant as described in the Purpose above. Our review was based on the terms of the grant agreement and on the application of certain agreed-upon procedures previously discussed with the ARC, OIG. Specifically, we determined if the tasks described above were being performed, if the accountability over ARC funds is sufficient as required by applicable Office of Management and Budget (OMB) Circulars, and if NCPRPDC was in compliance with the requirements of the grant agreement. Our results and recommendations are based upon those procedures. These review procedures were performed in accordance with applicable Government Auditing Standards.

REVIEW RESULTS:

The following results are based on our review performed at NCPRPDC in Ridgway, PA:

A. Incurred Costs

NCPRPDC's financial records report total program costs of \$522,028 for fiscal years ending June 30, 2002, 2003, and 2004. Of these costs, \$261,014 (50%) was attributed to ARC expenditures, with the remaining \$261,014 (50%) attributed to matching and in-kind expenditures.

For The Fiscal Year Ended June 30, 2002: \$154,114

For The Fiscal Year Ended June 30, 2003: \$210,638

For The Fiscal Year Ended June 30, 2004: \$157,276

B. Internal Controls

During the course of the review, we reviewed NCPRPDC's system of internal controls. One area of weakness was identified that could have affected the accountability of costs or compliance with the terms of the grant agreement.

FINDING 1. No Mandatory Vacation Requirement for Employees In Key Financial Positions

Proper internal control procedures require that all employees in key financial positions be required to take annual vacations.

The detection of misappropriation of funds is made more difficult by not requiring that employees in key financial positions take annual vacations.

Presently, employees in key financial positions are not required to take annual vacations.

We recommend that all employees in key financial positions be required to take annual vacations.

In response to our draft report, NCPRPDC management stated that they will be updating their Personnel Policies and Employee Handbook to require that employees in key financial positions take mandatory annual vacations. (See attached grantee response.)

We believe that implementation of the above recommendation will strengthen NCPRPDC's systems of internal controls.

C. Compliance

As part of obtaining reasonable assurance about whether NCPRPDC 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 review, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards which are described in the accompanying findings.

FINDING 1. Predetermined budget estimates are used to directly and indirectly charge salary and benefits cost to ARC and are not adjusted to actual costs as required by Federal cost principles.

OMB Circular A-122, Attachment B, para. 7.m.(a) states that reports of salaries and wages must reflect an after-the-fact determination of the actual activity of each employee. Budget estimates, such as estimates determined before the services are performed, do not qualify as support for charges to awards and are expressly unallowable. OMB Circular A-122 does allow for the interim use of estimated costs provided they are adjusted to actual costs at least annually.

NCPRPDC used predetermined budget estimates for certain administrative personnel to direct charge a portion of their salary and benefits to ARC and other programs, as well as for charging an associated indirect percentage of those employees' time to these programs. Salary and benefit costs charged based on these budget estimates were not adjusted to actual costs prior to the end of the reporting period. These estimates were based on prior year histories, rather than actual current-year data.

NCPRPDC management stated that they were aware of the Federal cost principles regarding payroll charges, but did not know that using these percentages to determine

hours charged to various programs was unacceptable. NCPRPDC management also stated that it has been using this method for many years and has been audited dozens of times with no audit findings to further emphasize why this was accepted as the NCPRPDC practice for determining hours charged to these programs.

We recommend the disallowance of \$197,032 of salary and benefit costs, which represent 100% of the salary and benefit costs directly charged to ARC by employees who assign time to the ARC Administrative Grant. All of the employees who assign time to this particular grant based their hours charged on predetermined budget estimates. The salary and benefit costs being recommended for disallowance in fiscal year 2002, 2003, and 2004 is as follows:

For The Fiscal Year Ended June 30, 2002: \$59,984

For The Fiscal Year Ended June 30, 2003: \$76,196

For The Fiscal Year Ended June 30, 2004: \$60,852

In response to our draft report, NCPRPDC management stated that the difference between actual and budgeted time was not material and therefore it would not be cost effective to adjust to actual. NCPRPDC management further stated that they have taken corrective action and employees' actual time is now being charged to the various programs. (See attached grantee response.)

NCPRPDC management also stated that because the costs involved are not unallowable costs under the guidelines of the grant, in their opinion our recommendation should have been the corrective action mentioned above, not the disallowance of 100% of the costs. (See attached grantee response.)

Because predetermined budget estimates of employees' time are expressly disallowed under OMB Circular A-122, we continue to recommend the disallowance of \$197,032 of salary and benefit costs.

FINDING 2. Associated indirect percentages being charged to the ARC program are based on predetermined budget estimates and are not adjusted to actual as required by Federal cost principles.

Furthermore, we recommend that the associated indirect percentages being charged to the ARC program, based on predetermined budget estimates, also be disallowed. As it would not be easily determinable for us to assign a dollar amount to the indirect portion being charged by these employees to the ARC grant, we recommend that ARC hold the grantee responsible for providing these amounts along with the appropriate documentation to support their calculations to the ARC.

In response to our draft report, NCPRPDC management stated that indirect cost percentages are based off of direct hours charged to each program and the difference between actual and budgeted time was not material and therefore would not be cost effective to adjust to actual. (See attached grantee response.)

Because predetermined budget estimates of employees' time are expressly disallowed under OMB Circular A-122, we continue to recommend that the associated indirect percentages being charged to the ARC program, based on these predetermined budget estimates, also be disallowed.

This report is intended solely for the information and use of the ARC and NCPRPDC, and is not intended to be and should not be used by anyone other than these specified parties.

Tichenor & Associates, LLP

Tichenor & Associates, LLP

Louisville, Kentucky

January 20, 2006

Grantee Response

North Central Pennsylvania Regional Planning and Development Commission

A Pennsylvania Local Development District "LDD"

651 Montmorenci Road Ridgway, PA 15853

Phone (814) 773-3162 Fax (814) 772-7045 e-mail - ncprpdc@ncentral.com www.ncentral.com/~ncprpdc

February 28, 2006

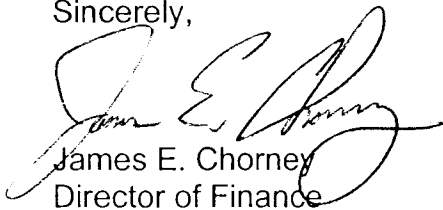
William R. Tichenor, CPA
Managing Partner
Tichenor & Associates, LLP
304 Middletown Park Place, Suite C
Louisville, KY 40243

Dear Mr. Tichenor:

Enclosed is North Central Pennsylvania Regional Planning and Development Commission's response to the purposed findings in the Draft audit report for the Appalachian Regional Commission.

Please let me know if you have any questions regarding this information.

Sincerely,



James E. Chorney
Director of Finance

North Central Pennsylvania Regional Planning and Development Commission

A Pennsylvania Local Development District "LDD"

651 Montmorenci Road Ridgway, PA 15853

Phone (814) 773-3162 Fax (814) 772-7045 e-mail - ncprpdc@ncentral.com www.ncentral.com/~ncprpdc

North Central Pennsylvania Regional Planning and Development Commission's response to the Appalachian Regional Commission Draft Audit Report prepared by Tichenor & Associates.

B. Internal Controls

Finding 1. Grantee's Response: North Central Pennsylvania Regional Planning and Development Commission will be updating the Personnel Policies and Employee Handbook to include a section that employees in key financial positions be required to take mandatory annual vacations.

Contracts: PA-13868-0-1, 21-769-0001, PA-12904G, PA-14570, PA-8312, PA-0708B

C. Compliance

Finding 1. Grantee's Response: North Central Pennsylvania Regional Planning and Development Commission has used this method of allocation for over 20 years and in that time North Central's contention has always been it is an issue of materiality in that the variance between actual and budgeted time was not material and therefore it would not be cost effective to adjust it to actual. This process has been through countless Federal, State and OIG audits, including previous audits from Tichenor & Associates, and if there was an issue with the methodology used to allocate these costs why is this only now being brought to our attention. According to Dave Zylks who was a senior manager of Tichenor & Associates this is a common problem nationwide that very few organizations have perfected, in our region alone we are aware of several agencies that would fall in the same dilemma we are currently faced with, if this were such a overwhelming issue one would think that the Federal agencies responsible for oversight of these funds would try to correct the problem by providing training as to the acceptable methods rather than singling one agency out to make an example of them.

In light of the current circumstances North Central has taken corrective action prior to the issuance of this report to remedy the concerns brought forth in it, the employees in question have been allocated entirely to one program or they have started to use hourly timesheets that are used to derive a percentage to distribute costs. It is our opinion that this should have been the recommendation of this report, not to disallow 100% of the costs. The costs involved in this discussion are not unallowable costs under the guidelines of the grant and should not be considered that way.

The disallowance of these costs seems to be an extreme penalty for an organization that has provided exceptional service to the community for over 30 years and could adversely affect the operations of the entire commission. Even if we were to calculate the costs in question from budgeted to actual amounts would the difference be material and would it be cost beneficial to try to determine that amount. We doubt that if there was a difference that it would be close to the amounts that Tichenor & Associates are sighting within this report and we suggest that the recommendations being made be disregarded due to the fact there was value received by the Appalachian Regional Commission contracts for the service that were provided.

Finding 2. Grantee's Response: The indirect cost percentages of North Central Pennsylvania Regional Planning and Development Commission are based off of direct hours worked within each program and North Central's contention has always been it is an issue of materiality in that the variance between actual and budgeted time was not material and therefore it would not be cost effective to adjust it to actual.

Contracts: PA-8312, PA-0708B