

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**THE NEXT DOOR FOUNDATION  
CLAIMED UNALLOWABLE  
INDIRECT COSTS  
AND DID NOT DOCUMENT  
THE FUNDING SOURCE OF  
PROGRAM EXPENDITURES  
IN ACCORDANCE WITH  
FEDERAL REQUIREMENTS**

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Gloria L. Jarmon  
Deputy Inspector General  
for Audit Services

September 2019  
A-05-18-00008

# *Office of Inspector General*

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## **OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS**

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.

## Report in Brief

Date: September 2019

Report No. A-05-18-00008

U.S. DEPARTMENT OF HEALTH & HUMAN SERVICES  
**OFFICE OF INSPECTOR GENERAL**



### Why OIG Did This Review

HHS provides funding through numerous programs that support the health and education of children. A prior review of Wisconsin's Maternal, Infant, and Early Childhood Home Visiting (MIECHV) program found that, among other things, the Next Door Foundation, Inc. (NDF), claimed unallowable costs associated with its MIECHV program. From Federal fiscal year (FFY) 2011 through 2017, NDF's HHS grant funding grew from approximately \$1.7 million to \$16.5 million, and NDF receives grants from multiple HHS funding sources.

Our objective was to determine whether NDF claimed and accounted for HHS grant funds in accordance with Federal requirements.

### How OIG Did This Review

We reviewed HHS grant funding and expenditures for FFYs 2016 and 2017 (October 1, 2015, through September 30, 2017). Our review covered HHS program grants for which NDF claimed \$33.2 million in costs during the audit period.

To determine whether NDF used HHS grant funds in accordance with Federal requirements, we obtained a list of expenditures for the selected grants in our review from NDF's general ledger. We conducted a detailed review of 100 judgmentally selected transactions from this list, totaling approximately \$1.7 million.

## The Next Door Foundation Claimed Unallowable Indirect Costs and Did Not Document the Funding Source of Program Expenditures in Accordance With Federal Requirements

### What OIG Found

NDF did not always claim and account for HHS grant funds in accordance with Federal requirements. We identified unallowable claims for indirect costs totaling \$142,104. We also identified other costs totaling \$15,618 that did not fully meet Federal requirements but were related to the purpose of the grant. These costs included \$9,968 for contractual services and \$5,650 for cost transfers. In addition, NDF's financial management system was not in compliance with Federal regulations. NDF claimed unallowable costs because it did not always follow its policies and procedures for claiming and accounting for HHS grant funds.

### What OIG Recommends and Next Door Foundation's Comments

We recommend that NDF refund \$142,104 in unallowable indirect costs and work with its HHS funding agencies to ensure proper claiming of indirect costs, ensure that contractual agreements are signed and in place before services are provided, ensure that cost transfers meet applicable criteria and are fully documented, and ensure that the financial management system accurately matches expenditures with the source of funds.

In written comments on our draft report, NDF did not concur with our first finding that the 10 EHS-CCP partners should be considered subrecipients and that the indirect costs claimed totaling \$142,104 should be disallowed. NDF concurred with our findings regarding contractual agreements, cost transfers, and accounting for HHS grant expenditures and described steps it has taken or plans to take to implement new processes or systems.

We maintain that the 10 EHS-CCP partners were subrecipients and that the indirect costs claimed totaling \$142,104 should be disallowed. We acknowledge that NDF may not have intended to make a subaward; however, its intent (or decision not to seek prior approval) does not support the classification of partners as contractors. As stated in 45 CFR § 75.2, subawards may be provided by a non-Federal entity to a subrecipient through any form of legal agreement, even an agreement considered to be a contract.

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## INTRODUCTION

### WHY WE DID THIS REVIEW

The U.S. Department of Health and Human Services (HHS) provides funding through numerous programs that support the health and education of children. A prior review of Wisconsin's Maternal, Infant, and Early Childhood Home Visiting (MIECHV) program found that, among other things, the Next Door Foundation, Inc. (NDF), claimed unallowable costs associated with its MIECHV program.<sup>1</sup> From Federal fiscal year (FFY) 2011 to 2017, NDF's HHS grant funding grew from approximately \$1.7 million to \$16.5 million, and NDF receives grants from multiple HHS funding sources.

### OBJECTIVE

Our objective was to determine whether NDF claimed and accounted for HHS grant funds in accordance with Federal requirements.

### BACKGROUND

NDF, a not-for-profit organization in Milwaukee, Wisconsin, has served children and families since 1969. Its mission is to support the intellectual, physical, and emotional development of children by partnering with their families for success in school and the community. NDF's vision is to position children and families for long-term success. NDF receives grants from HHS's Administration for Children and Families (ACF) for Head Start (HS), Early Head Start (EHS), and the Early Head Start Child Care Partnership (EHS-CCP). NDF also receives pass-through funds for the Health Resources and Services Administration's MIECHV program and the ACF Healthy Marriage and Responsible Fatherhood program.

As part of its EHS-CCP program, NDF partners with 10 organizations to provide services to eligible children. The goals of NDF's EHS-CCP program are to:

- increase access to coordinated, comprehensive services for low-income infants and toddlers and their families in child care;
- increase the capacity of childcare providers serving low-income families; and
- foster strong partnerships that in turn strengthen the local early childhood system and services.

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<sup>1</sup> *Wisconsin Did Not Always Comply With Maternal, Infant, and Early Childhood Home Visiting Program Requirements*, A-05-15-00049, issued September 2017. Available at <https://oig.hhs.gov/oas/reports/region5/51500049.asp>. Accessed on March 21, 2019.

Subawards provided by a non-Federal entity to a subrecipient for the purposes of carrying out a portion of a Federal award create a Federal assistance relationship with the subrecipient (45 CFR §§ 75.2 and 75.351). Subawards may be provided by a non-Federal entity to a subrecipient through any form of legal agreement, even an agreement considered to be a contract (45 CFR § 75.2). According to 45 CFR § 75.351, the non-Federal entity should consider the following five characteristics when determining whether to classify another non-Federal entity as a subrecipient. The non-Federal entity:

- determines who is eligible to receive what Federal assistance;
- has performance measurements in relation to whether objectives of a Federal program were met;
- is responsible for programmatic decision-making;
- is responsible for adherence to applicable Federal program requirements specified in the Federal award; and
- in accordance with its agreement, is using Federal funds to carry out a program for a public purpose specified in the authorizing statute, as opposed to providing goods or services for the benefit of the pass-through entity.

A non-Federal entity does not have to meet all of these characteristics to be considered a subrecipient; it is the substance of the relationship that is important. In contrast, characteristics of a contractor include, but are not limited to, providing goods or services within normal business operations to many purchasers, providing goods and services ancillary to the Federal program, and not being subject to compliance requirements of the Federal program (45 CFR § 75.351(b)).

## **HOW WE CONDUCTED THIS REVIEW**

We reviewed HHS grant funding and expenditures for FFYs 2016 and 2017 (October 1, 2015, through September 30, 2017). Our review covered HHS grants for which NDF claimed \$33.2 million in costs during the audit period. Appendix B includes a detailed list of NDF's HHS grant expenditures during FFYs 2016 and 2017.

To determine whether NDF used HHS grant funds in accordance with Federal requirements, we obtained a list of expenditures for the selected grants in our review from NDF's general ledger. We conducted a detailed review of 100 judgmentally selected transactions from this list, totaling approximately \$1.7 million. The transactions we selected were intended to cover a mix of expenditure types such as salaries, fringe benefits, equipment, renovations, consultants, travel, indirect costs, high-dollar costs, and cost transfers.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix A contains the details of our audit scope and methodology.

## **FINDINGS**

NDF did not always claim and account for HHS grant funds in accordance with Federal requirements. We identified unallowable claims for indirect costs totaling \$142,104. We also identified other costs totaling \$15,618 that did not fully meet Federal requirements but were related to the purpose of the grant. These costs included \$9,968 for contractual services and \$5,650 for cost transfers. In addition, NDF's financial management system was not in compliance with Federal regulations. NDF claimed unallowable costs because it did not always follow its policies and procedures for claiming and accounting for HHS grant funds.

### **THE NEXT DOOR FOUNDATION CLAIMED UNALLOWABLE INDIRECT COSTS**

Federal regulations (45 CFR § 75.414(f)) allow for any non-Federal entity that has never received a negotiated indirect cost rate to elect to charge a de minimus rate of 10 percent of modified total direct costs (MTDCs), which may be used indefinitely. MTDCs exclude, among other things, the portion of each subaward in excess of \$25,000 (45 CFR § 75.2).

NDF claimed \$142,104 in unallowable indirect costs because it (1) inaccurately considered its EHS-CCP partners to be contractors rather than subrecipients and (2) failed to exclude the portion of each subaward in excess of \$25,000. Using the de minimus indirect rate of 10 percent of MTDCs, NDF claimed \$167,104 in indirect costs associated with \$1,671,038 in payments made to 10 EHS-CCP partners during our audit period. However, as detailed below, NDF should have considered EHS-CCP partners to be subrecipients rather than contractors and should have claimed indirect costs of only \$2,500 for each of the 10 partners, for a total of \$25,000.

According to the terms of NDF's Memorandum of Agreement (MOA) with its partners, EHS-CCP partners are responsible for adhering to many of the same requirements imposed on NDF by the EHS program (both regulations and other standards), as well as other Federal requirements. EHS-CCP partners (1) are responsible for adhering to EHS<sup>2</sup> and other Federal requirements, (2) use EHS funds in accordance with the MOA to carry out the EHS program for public purposes, and (3) are not providing goods or services for the benefit of NDF.

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<sup>2</sup> While the program is referred to as "EHS-CCP," the services provided by the partners are intended to be fully compatible with the intent and philosophy of the EHS program. For that reason, we use both terms interchangeably in this section.



Specifically, the MOAs stipulate that partners:

- meet all of the standards and requirements of the Office of Head Start and develop services that are fully compatible with the intent and philosophy of the EHS program and meet all Head Start Program Performance Standards;
- ensure that all documentation, records, reporting, and standards adhere to the Head Start Act and the Head Start Program Performance Standards;
- employ staff to fully implement the requirements of the Head Start Program Performance Standards;
- enroll only children who are eligible for the EHS program;
- conduct health and safety screenings and assessments; and
- provide mental health services and disabilities services.

Moreover, NDF's partners do not provide services to NDF that are like those provided by contractors. Specifically, as described above, EHS-CCP partners are not providing goods or services that are ancillary to the operation of the EHS program; partners are providing the very services that are established and required by the EHS program. Therefore, NDF should have determined that its EHS-CCP partners are subrecipients and should not have included in its MTDC the portion of each subaward in excess of \$25,000.

## **THE NEXT DOOR FOUNDATION CLAIMED COSTS THAT DID NOT MEET FEDERAL REQUIREMENTS**

### **The Next Door Foundation Paid for Contractual Services Without Having a Signed Agreement**

According to 45 CFR § 75.459, professional services costs are allowable when reasonable in relation to the services rendered and when not contingent upon recovery of the costs from the Federal Government. Allowability of these costs is subject to a number of factors, including the adequacy of the contractual agreement, which includes a description of the service, estimate of time required, rate of compensation, and termination provisions.

NDF claimed \$9,968 for nursing services provided by the Children's Hospital and Health System even though NDF did not have a signed contractual agreement in effect during the period of our review. NDF provided two agreements with Children's Hospital and Health System. One covered the period August 1, 2015, through July 31, 2016, and the other covered August 1, 2016, through July 31, 2017. The payment we reviewed covered services provided in August 2016. However, the documentation provided by NDF showed that the agreement covering the hours billed in this transaction was not signed by either party until after

December 2016, raising questions regarding the adequacy and validity of the contractual agreement prior to being signed. Therefore, costs incurred prior to the signed contract are considered unallowable and should not have been charged to the grant.

### **Cost Transfers Were Not Supported**

Per the HHS Grants Policy Statement, page II-43, cost transfers by recipients between grants, whether as a means to compensate for cost overruns or for other reasons, generally are unallowable. The transfer must be supported by documentation that fully explains how the error occurred and by a certification of the correctness of the new charge by a responsible official of the recipient, subrecipient, or contractor. An explanation merely stating that the transfer was made “to correct error” or “to transfer to correct project” is not sufficient.

NDF transferred \$5,650 from the HS program to the Healthy Marriage and Responsible Fatherhood program. This cost transfer was not supported by documentation that fully explained the reason for the transfer, including how the error occurred and certification of the correctness of the new charge. NDF stated that it made the cost transfer because funding for the Healthy Marriage and Responsible Fatherhood program had not been received at the time the cost was incurred, so HS grant funding was initially used to cover the costs. The costs appeared to be allowable and related to the purpose of the grant to which they were transferred; however, NDF’s own policy states that “. . .[it] adheres to the requirements of its grants which may prohibit loaning funds between programs . . . .”

### **THE NEXT DOOR FOUNDATION DID NOT APPROPRIATELY ACCOUNT FOR HHS GRANT EXPENDITURES**

Federal regulations (45 CFR § 75.302(b)) require each non-Federal entity’s financial management system to provide for the following:

- identification in its accounts of all Federal awards received and expended and the Federal programs under which they were received;
- accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the reporting requirements set forth in §§ 75.341 and 75.342; and
- records that adequately identify the source and application of funds for federally funded activities, i.e., records that contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, expenditures, income, and interest and are supported by source documentation.

NDF was not in compliance with the applicable criteria for financial management systems. Specifically, NDF did not identify the funding source of expenditures showing whether they

were funded with (1) grant revenue or (2) associated non-Federal cost share revenue at the time NDF recorded the transactions in its financial management system.

To illustrate this matter, we could not confirm the source of funds for \$65,711 in costs for a playground at the Oliver Wendell Holmes School. The school, part of the Milwaukee Public Schools system, houses several NDF HS classrooms. NDF officials indicated that they intended to use HS grant funding to pay for the playground and obtained ACF's prior approval for the purchase; however, because of a series of delays in identifying a location to build the playground, funding in the grant lapsed. NDF officials explained that they then used non-grant funding to pay for the playground. The coding in NDF's financial management system did not have the functionality to identify whether grant funding or non-grant funding paid for the playground. Therefore, there was no assurance that expenditures reported on the Federal financial reports were paid with Federal grant funds.

### **RECOMMENDATIONS**

We recommend that the Next Door Foundation, Inc.,:

- refund \$142,104 in unallowable indirect costs and work with its HHS funding agencies to ensure proper claiming of indirect costs,
- ensure that contractual agreements are signed and in place before services are provided,
- ensure that cost transfers meet applicable criteria and are fully documented, and
- ensure that the financial management system accurately matches expenditures with the source of funds.

### **NEXT DOOR FOUNDATION COMMENTS**

In written comments on our draft report, NDF did not concur with our first finding that the 10 EHS-CCP partners should be considered subrecipients and that the indirect costs claimed totaling \$142,104 should be disallowed. NDF contended that the partners are contractors because they (1) provided early childhood services as part of normal business operations, (2) provided early childhood services to other customers, (3) operated in a competitive environment, and (4) were not responsible for eligibility determination.

NDF stated that "partners were not contracted for Next Door's own use . . . ." NDF also stated that it retained and performed substantial responsibilities to carry out the performance of the EHS program and to assure compliance with the Head Start Program Performance Standards.

Further, NDF indicated that its EHS-CCP grant required enrollment of and service to 344 infants and toddlers, and that it served 40 children in its own facility and 304 children through slots

purchased from the 10 qualified early childhood providers operating in its geographical area. NDF said that these 10 partners were required to recruit the contracted number of children within HHS eligibility guidelines; recruit and employ credentialed teachers, per Head Start Performance Standards; and implement a specific curriculum, in a classroom setting, with specific staff-to-child ratios.

NDF contended that it never intended to classify these partners as subrecipients and therefore did not request prior approval from the Office of Head Start, as would be required for work subawarded under the Federal award. Further, NDF stated that the prior-approval requirements do not apply to the acquisition of supplies, material, equipment, or general support services. NDF believed that its agreement with the partners constituted general support.

NDF concurred with our findings regarding contractual agreements, cost transfers, and accounting for HHS grant expenditures and described steps it has taken or plans to take to implement new processes or systems. NDF said that, as of 2017, it had implemented a centralized process to ensure that NDF's president reviews and executes all agency contracts before services are provided. NDF said that, as of January 2019, it had implemented a new system that will require proper approvals to ensure that cost transfers are fully documented. Last, NDF said that, beginning in its FY 2020, it will use funding source codes to document expenditures and that it is currently seeking a new accounting system that may be better able to align revenue and expenditures based on funding sources.

NDF's written comments are included in their entirety as Appendix C. NDF also provided additional contracting and procurement policies, as well as Internal Revenue Service (IRS) Form 990s for seven of its partners. The policies are not attached to this report because we have not verified NDF's planned corrective actions, and the IRS Form 990s are available to the general public.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

We acknowledge that the 10 childcare partners operated in a competitive environment to provide childcare services. However, the childcare partners also exhibited characteristics indicative of a subrecipient. A contract is for the purpose of obtaining goods and services for the non-Federal entity's own use (45 CFR § 75.351(b)). In its comments, NDF stated that "partners were not contracted for Next Door's own use . . . ."

We also acknowledge that NDF both retained partners and performed activities required by the EHS program. Subrecipients, however, are not required to carry out the entire Federal award. A subaward is for the purpose of carrying out a portion of a Federal award (45 CFR §§ 75.2 and 75.351(a)). Partners carried out portions of the Federal program. The MOA required the partners to provide services required by the EHS program related to education, health, and safety. Specifically, as NDF acknowledges, partners were responsible for recruiting children who met HHS eligibility guidelines and recruiting and employing credentialed teachers, per

Head Start Performance Standards, to implement a specific curriculum, in a classroom setting, with specific staff-to-child ratios.

We further acknowledge that NDF may not have intended to make a subaward; however, its intent (or decision not to seek prior approval) does not support the classification of partners as contractors. As stated in 45 CFR § 75.2, subawards may be provided by a non-Federal entity to a subrecipient through any form of legal agreement, even an agreement considered to be a contract. NDF's decision to not request prior approval for its agreements with the 10 partners and the belief that the agreements with the 10 partners constitute general support services are not relevant to the classification of partners as contractors.

Accordingly, we maintain that the 10 EHS-CCP partners were subrecipients and that the indirect costs claimed totaling \$142,104 should be disallowed.

## **APPENDIX A: AUDIT SCOPE AND METHODOLOGY**

### **SCOPE**

Our review covered HHS grants for which NDF claimed \$33,164,725 in costs during FFYs 2016 and 2017. We obtained a list of expenditures from NDF's general ledger during our audit period for five of the grants totaling \$22,972,814. We then judgmentally selected 100 of these transactions totaling \$1,752,523 for detailed review.

We did not perform an overall assessment of NDF's internal control structure. Rather, we reviewed only the internal controls that pertained directly to our objective.

We performed fieldwork from January through December 2018 at NDF's office in Milwaukee, Wisconsin.

### **METHODOLOGY**

To accomplish our objective, we:

- reviewed applicable Federal laws, regulations, and policies on HHS grant awards;
- met with ACF officials prior to contacting NDF to discuss the plan for review;
- met with NDF officials to determine the policies, procedures, and controls related to monitoring and reporting of program grant funds;
- reviewed NDF's financial management system policies, procedures, and internal controls to determine whether it could account for multiple HHS grant funding sources;
- obtained a list of HHS grant awards made to NDF for the audit period;
- reconciled costs claimed by NDF with cash drawdowns and accounting records for the five grant awards reviewed;
- obtained a list of costs claimed by NDF for the five grant awards reviewed;
- judgmentally selected and reviewed various types of costs claimed;
- reviewed NDF's use of HHS funds per Federal requirements; and
- discussed the results of our review with ACF and NDF officials.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## APPENDIX B: NEXT DOOR FOUNDATION'S HHS GRANT EXPENDITURES

Award Type	Grant Number	HHS Operating Division & Grant Title	FFR Reporting Period Dates	Expenditures
Direct	05HP0029-01	ACF: Early Head Start - CCP	10/1/15 through 12/31/16	\$4,679,619
Direct*	05HP0029-02	ACF: Early Head Start - CCP	7/1/16 through 9/30/17	\$5,143,156
Direct	05HP0029-03	ACF: Early Head Start - CCP	7/1/17 through 9/30/17	\$1,120,243
Direct*	05CH010263-01	ACF: Early Head Start	10/1/15 through 9/30/17	\$4,171,646
Direct	05CH010263-02	ACF: Early Head Start	4/1/17 through 9/30/17	\$918,846
Direct	05CH8281-08	ACF: Early Head Start	10/1/15 through 3/31/16	\$410,911
Direct	05CH8319-03	ACF: Head Start	10/1/15 through 12/31/15	\$638,268
Direct*	05CH8319-04	ACF: Head Start	10/1/15 through 9/30/17	\$12,839,237
Direct	05CH8319-05	ACF: Head Start	4/1/17 through 9/30/17	\$2,424,024

<b>Total Direct Awards</b>	<b>\$32,345,950</b>
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Subaward*	90FK0049	ACF: Healthy Marriage and Responsible Fatherhood Grants	10/1/15 through 9/30/17	\$121,670
Subaward*	CFA0064	HRSA: Maternal, Infant, and Early Childhood Home Visiting Program	10/1/15 through 9/30/17	\$697,105

<b>Total Subawards</b>	<b>\$818,775</b>
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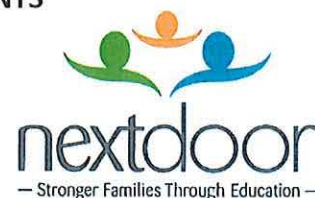
<b>Total HHS Grant Expenditures During Audit Period</b>	<b>\$33,164,725</b>
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\* Costs associated with this award were included in the judgmental sample selection.



## APPENDIX C: NEXT DOOR FOUNDATION COMMENTS



July 22, 2019

To: Sheri L. Fulcher  
Regional Inspector General for Audit Services  
Office of Inspector General  
Office of Audit Services, Region V  
233 North Michigan, Suite 1360  
Chicago, IL 60601

Re: Report Number: A-05-18-00008

Dear Ms. Fulcher:

This letter summarizes our response to the audit finding included in the above referenced report.

- Next Door Foundation, Inc. does not concur with the finding that the ten (10) Early Head Start – Child Care Partners should be deemed “sub-recipients” and that the indirect costs claimed, totaling \$142,104 should be disallowed.

### I. Basis for Non-concurrence

The OIG report cited certain characteristics of sub-recipients included in 45 CFR Part 75.351 as follows:

Subawards provided by a non-Federal entity to a subrecipient for the purposes of carrying out a portion of a Federal award create a Federal assistance relationship with the subrecipient (45 CFR §§ 75.2 and 75.351). Subawards may be provided by a non-Federal entity to a subrecipient through any form of legal agreement, even an agreement considered to be a contract (45 CFR § 75.2). According to 45 CFR § 75.351, the non-Federal entity should consider the following five characteristics when determining whether to classify another non-Federal entity as a subrecipient. The non-Federal entity:

- determines who is eligible to receive what Federal assistance;
- has performance measurements in relation to whether objectives of a Federal program were met;
- is responsible for programmatic decision-making;
- is responsible for adherence to applicable Federal program requirements specified in the Federal award; and

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- in accordance with its agreement, is using Federal funds to carry out a program for a public purpose specified in the authorizing statute, as opposed to providing goods or services for the benefit of the pass-through entity.

The Next Door Foundation, Inc. classified the ten (10) Early Head Start – Child Care Partnerships as “contractors,” based upon the following regulation;

45 CFR Part 75.351

(b) **Contractors.** A contract is for the purpose of obtaining goods and services for the non-Federal entity's own use and creates a procurement relationship with the contractor. See § 75.2Contract. Characteristics indicative of a procurement relationship between the non-Federal entity and a contractor are when the contractor:

- 1) Provides the goods and services within normal business operations;
- 2) Provides similar goods or services to many different purchasers;
- 3) Normally operates in a competitive environment;
- 4) Provides goods or services that are ancillary to the operation of the Federal program; and
- 5) Is not subject to compliance requirements of the Federal program as a result of the agreement, though similar requirements may apply for other reasons.

Partners were not contracted for Next Door's own use, rather the intent of the grant was to broaden and strengthen the partner's services to the community. This grant allowed the partners to provide services to the community.

(c) **Use of judgment in making determination.** In determining whether an agreement between a pass-through entity and another non-Federal entity casts the latter as a subrecipient or a contractor, the substance of the relationship is more important than the form of the agreement. All of the characteristics listed above may not be present in all cases, and the pass-through entity must use judgment in classifying each agreement as a subaward or a procurement contract.

As noted in Exhibit X, the ten contractors clearly met the characteristics outlined in 75.351 (b) due to:

- a. Each contractor was operating in the business of early childhood, prior to contracting with Next Door Foundation, Inc.
- b. Each contractor served more customers than Next Door Foundation, Inc., evidence by the percentage of EHS-CCP revenue to total revenue. In addition, this contract is incidental to the total business of the partner. (See Exhibit X)



- c. Each contractor operated in a competitive environment; as there are numerous early childhood service providers in the Milwaukee area for which parents as well as Next Door Foundation, Inc. could seek for services.
- d. Neither contractor had the responsibility to determine eligibility, which authority was retained by Next Door Foundation, Inc. staff. (Determining eligibility is a primary characteristic of a sub-recipient).

A non-Federal entity does not have to meet all of these characteristics to be considered a subrecipient; it is the substance of the relationship that is important. In contrast, characteristics of a contractor include, but are not limited to, providing goods or services within normal business operations to many purchasers, providing goods and services ancillary to the Federal program, and not being subject to compliance requirements of the Federal program (45 CFR § 75.351(b)).

- II. Grantee retained and performed substantial responsibilities to carry out the performance of the Early Head Start Program and to assure compliance with the Head Start Program Performance Standards. This is evident by the following:

Next Door Foundation, Inc. project staff and their roles in performing the requirements of the Head Start Program Performance Standards; reflect that direct services required by Head Start were retained by the grantee.

- **Director of Childcare Partnerships**

The Director is responsible for EHS-CCP (Early Head Start Child Care Partnership) child health and development, education and child development, child health and safety, nutrition, family support and engagement, community collaborations, governance, ERSEA, and general oversight and management of the EHS-CCP program. This position will provide guidance and oversee all Next Door staff in this program. The Director will ensure all federal and state regulations are followed with fidelity.

- **CCP Manager**

CCP manager is responsible for overall contractual compliance of Child Care Partner programs at Next Door. The CCP Manager ensures that adequate ongoing monitoring and record-keeping/reporting systems are in place to ensure compliance with local, state and federal requirements. The CCP Manager position also has responsibility for ensuring consistency in the delivery of School Readiness aspects of the program and supervision/oversight of the Instructional Coaches within the partnership.

- **Instructional Coaches**

The Instructional Coach supports embedded professional development of teaching staff at partner sites to ensure teacher's instructional strategies are effective in helping children increase social emotional and academic skills to succeed in an

elementary school setting. The Instructional Coach collaborates with partner site leadership to ensure educational programs comply with state licensing, Young Star, Office Of Head Start Performance Standards, and policies and procedures.

**Family advocates are responsible for attaining information from families related to eligibility. That information is then turned in to ERSEA staff to finalize eligibility. Communication is then provided directly to supporting family advocate and partner. See further details related to position responsibilities below.**

▪ **Family Advocate Supervisor**

The Family Advocate Supervisor works as part of an interdisciplinary team to ensure families are welcomed into the program and receive high quality support services according to the families' strengths, interests and needs. The Family Advocate Supervisor supervises the Family Advocate Specialist (FAS) team in all aspects of programming including recruitment, enrollment, family partnership agreements and other casework activities. The Family Advocate Supervisor is responsible for creating strong family and community partnerships, involving parents in all aspects of the program (including program governance), and assure compliance with all Head Start requirements including health and dental.

▪ **Family Advocate**

The Family Advocate Specialist has a primary role on the Next Door's interdisciplinary team for engaging and involving families of children at school through activities, practices and services that support parents as the primary nurturers, experts and teachers of their child in order to promote and sustain their child's learning development and academic; and life success. The Family Advocate Specialist has a specific and intentional role in the following three areas of work with families:

- Activities/strategies that promote and enhance the parent-child relationship.
- Activities/strategies that engage parents in discussions about their child's growth and development and provide parents information and opportunities to learn about concrete things they can do to promote their child's learning.
- Activities/strategies that encourage parents' involvement in the education of their child and in their child's school both at Next Door and in the K-12 system. This includes helping parents recognize and expect "quality education;" know how to access quality elementary schools; and learn how to advocate for a quality education for their child.

▪ **Enrollment and Retention Specialist**

The Enrollment and Retention Specialist assists Next Door programs in all requirements and standards related to ERSEA (Eligibility, Recruitment, Selection,



Enrollment and Attendance). The Enrollment and Retention Specialists develops and maintains relationships with families and ensure that they receive comprehensive services throughout their participation in the partnership program. The Enrollment and Retention Specialist is responsible for conducting community outreach and recruitment efforts to identify eligible families, encourage them to apply and assist them with the enrollment process. The Enrollment and Retention Specialist works closely with his/her immediate supervisor, the Family Support Supervisors, Family Advocate Specialists and partner staff to ensure all program options are at full enrollment, and to support attendance benchmarks.

▪ **Disabilities & Mental Health Specialist**

Disability and Mental Health Specialist supports Early Head Start programs at our partner sites in developing and implementing IFSP's for children with suspected and diagnosed disabilities, identify mental health concerns and make referrals to appropriate clinicians. The Disability and Mental Health specialist provides training to partner site staff based on Professional Development needs and goals.

▪ **Health Services Specialist**

The health services specialist works closely with the Health Services Supervisor to plan, coordinate and monitor compliance with Head Start Performance Standards and Wisconsin licensing laws. This position will assist with child health requirements, screenings and assessments and implement training for education to parents, partner staff and volunteers.

These positions are evidence that all services required by the Head Start Performance Standards except "teachers," were performed by Next Door Foundation, Inc.

If "the intent to delegate" performance of such required services to the contractors, the amounts paid to them would have substantially increased, for such services to be delivered in accordance with grant terms and conditions:

III. As outlined in ACF-IM-15-03, the Office Of Head Start's Early Head Start Child Care Partnership initiative was created to enhance the quality of care to low income infants and toddlers (and their families), who were being serviced by family child care homes and day care centers. The target of the partnerships were those infant and toddlers whose parents/guardians were being subsidized by the Office of Child Care, also within the Department of Health and Human Services.

In addition to serving infants and toddlers receiving child care subsidies, the initiative expanded Early Head Start Services to infants and toddlers meeting eligibility requirements.

The Next Door Foundation, Inc.'s grant required the enrollment and service to 344 infants and toddlers. While 40 children were served in its owned facilities, The Next Door Foundation, Inc. "purchased 304 slots" from the ten (10) qualified early childhood providers operating in its geographical area. These (10) contractors were essentially required to recruit the contracted number of children within "the DHHS eligibility guidelines" and recruit and employ credentialed teachers (as per Head Start Performance Standards), to implement a specific curriculum, in a classroom setting, with specific staff/child ratio.

In order for the grantee to be compliant with the grant terms and conditions, the Memorandum of Understanding (MOU) with each contractor included provisions to assure that the environment at the contractor's sites relating to licensing, health and safety, and other regulations were in compliance with the Head Start Program Performance Standards. These provisions were not intended to be "delegating the responsibilities" of the program to the contractors but rather assuring health and safety environments for the children for whom slots were being purchased.

#### Prior Approval – (45 CFR Part 75.308 (c))

If the Next Door Foundation, Inc. intended to classify these contractors as sub-recipients, prior approval would have been requested to the Office Of Head Start as required by 45 CFR Part 75.308 (c), which states "grant recipients must request prior approvals from HHS for one or more of the program or budget related reasons."

(vi) The sub-awarding or contracting out any work under a Federal award, including fixed amounts of any sub-awards as described in 75.353.

This provision does not apply to the acquisition of supplies, material, equipment or general support services. Next Door Foundation, Inc. contract with the partners constituted general support (not a sub-award).

#### IV. Correction Action Planned

In conclusion, Next Door Foundation, Inc.'s did not intend to make a sub-award, and accordingly, did not request prior approval. Next Door Foundation, Inc. will amend its MOU's for subsequent periods, to include applicable basis for contractor determination and clarity with respect to general all-inclusive language requiring adhering to the Head Start Performance Standards. In contrast, those provisions will clarify that the partners will make available, provide access, and allow Next Door Foundation, Inc. to perform such services "in accordance with Head Start Program Performance Standards."



- Next Door Foundation, Inc. concurs with the finding that contractual agreements are signed and in place before providing services.

Pursuant to 45 CFR 75.459(b)(8) professional service costs are allowable based on a number of factors, including the adequacy of the contractual agreement which includes a description of the services, estimate of time required, rate of compensation and termination provisions.

As of 2017 a centralized process was implemented in which the president reviews and executes all agency contracts before services are in place. In addition a database and recordkeeping process has been implemented that ensures proper documentation is centralized and knowledgeable by all applicable departments (fiscal, facilities, programming, etc.).

Please see attached policy, Contract, Agreement, Memorandum of Understanding and Partnership Policy and Procedure, which has corrected this issue of concern.

- Next Door Foundation, Inc. concurs with the finding that cost transfers must meet applicable criteria and are fully documented.

Pursuant to 45 CFR 74.53 or 92.42 supporting documentation including a full explanation of how the error occurred and a certification of the correctness of new charges by a responsible official of the recipient, sub recipient or contractor must be of record.

Upon implementation of a new payroll system in January 2019 financial services has implemented a process where as retro entries related to payroll/benefit re classes must be processed within the system using a workflow that includes all applicable approvals beginning with the supervisor, including the employee and ending with the Vice President or President's final approval. Specific reasoning related to the correcting entry must be reflected as supporting documentation with the appropriate sign off based on the financial authorization approval level policy. Entries not related to the payroll system requires the same level of documentation and approval authority.

Please see attached Policy, Procurement Procedures, which includes financial authorization limits that will be used to correct this issue of concern.

- Next Door Foundation, Inc. concurs with the finding that the financial management system does not directly reflect match expenditures with the source of funds.

Pursuant to 45 CFR 75.439(b)(3) prior approval from the HHS awarding agency for capital expenditures for improvements to land, building or equipment which materially increase their value or useful life is required.

According to the Office of Inspector General proper documentation related to funding that covers specific expenditures is not properly reflected within the financial management system. In an effort to accommodate a clearer process has been identified whereas the same funding source coding that captures specific revenue sources will also be used to capture expenditures. This change will be reflected as of FY20 beginning July 1, 2019. A new accounting system that may be more capable of aligning revenue and expenditures based on funding sources is being sought at this time as an additional corrective action to this concern. However, please note that the distinguishment that is currently in place reduces any charges to federal funding sources equivalent to the other revenue sources aligned within specific departments to ensure charges are reflected accordingly.

If you require additional information, please do not hesitate to contact me or Nicole Landry, Director of Finance.

Sincerely,

Dr. Tracey Sparrow  
President  
Next Door Foundation, Inc.

CC: Nicole Landry  
Director of Finance



Exhibit X

Summary of Contractors – Revenue Analysis Subtotal of Revenues					
Contractor	Gross Revenue	Program Revenue (Fee for Service)	EHS-CCP Payments (completed by NDF)	%	Reference
COA Youth and Family Centers	6,490,909	2,400,339	357,050	14.87	2017
Jo's Early Learning Academy	N/A		36,512		
Kindercare Education	N/A		276,979		
LaCausa, INC	20,584,305	7,337,040	200,574	2.7	2017
Malaika Early Learning Center	1,851,662	1,078,232	98,627	9.1	2015
Neighborhood House of Milwaukee	2,415,902	255,524	67,806	26.5	2016
St. Ann's Center for Intergenerational Care	9,169,211	5,871,608	221,912	3.7	2017
St. Joseph's Academy	5,609,676	5,420,771	122,336	2.2	2016
Stepping Stones	N/A		42,201		
YMCA Of Milwaukee, INC.	11,020,324	9,334,050	247,043	2.6	2017

References

1. Federal Form 990 – 2018
2. Federal Form 990 – 2017
3. Federal Form 990 – 2016
4. Federal Form 990 - 2015
5. Not Available – No tax exempt organization

It should be noted that the contractors included the fees paid by the Next Door Foundation, Inc. under Program Service Revenue, in their Federal form 990's as opposed to "grants," as would be required if they were sub-recipients.