
**APPALACHIAN REGIONAL COMMISSION
OFFICE OF INSPECTOR GENERAL**

AUDIT OF GRANT AWARD
Appalachian Sustainable Development
Abingdon, Virginia

Final Report Number: 19-01
Grant Number: PW-18601
October 2018

Prepared by:

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October 16, 2018

Appalachian Regional Commission
Office of the Inspector General
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Washington, DC 20009

Leon Snead & Company, P.C. completed an audit of grant PW-18601 awarded by the Appalachian Regional Commission (ARC) to Appalachian Sustainable Development (ASD) in Abingdon, Virginia. The audit was conducted at the request of the ARC Office of Inspector General to assist the office in its oversight of ARC grant funds.

The audit objectives were to determine whether: (1) program funds were managed in accordance with the ARC and Federal grant requirements; (2) grant funds were expended as provided for in the approved grant budget; (3) internal grant guidelines, including program (internal) controls, were adequate and operating effectively; (4) accounting and reporting requirements were implemented in accordance with generally accepted accounting principles (or other applicable accounting and reporting requirements); and (5) the matching requirements; and (6) the established performance measures were met or likely to be met.

Overall, ASD's financial management and administrative procedures and related internal controls were adequate to manage the funds under the ARC grant audited. However, we noted several areas that could be improved, including the allocation of grant costs, non-competitive procurement, and the estimates and timely expenditures of grant advances. Financial and project reporting requirements were being met and the progress reports were considered excellent in their content and format. The non-federal matching funds were being documented and it appeared the matching requirements would be fully met by the end of the grant. We questioned \$154,000 of costs on two contracts because the non-competitive awards were not adequately justified and the required costs analysis was not performed prior to the award for either contract. Also, we questioned \$24,148 in costs that were allocated to the grant as shared costs, such as trucking fees, fuel, and utilities, because the allocation basis was not adequately supported and consistent. The questioned costs, procedural issues, and recommended corrective actions are discussed in the Findings and Recommendations section of this report.

Leon Snead & Company appreciates the cooperation and assistance received from the ASD and ARC staffs during the audit.

Sincerely,

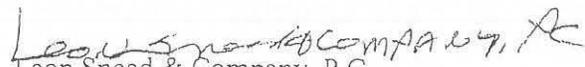

Leon Snead & Company, P.C.

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Background

Leon Snead & Company, P.C. completed an audit of grant PW-18601 awarded by the Appalachian Regional Commission (ARC) to Appalachian Sustainable Development (ASD) in Abingdon, Virginia. The audit was conducted at the request of the ARC Office of Inspector General to assist the office in its oversight of ARC grant funds.

The grant was awarded under the Partnership for Opportunity and Workforce and Economic Revitalization (POWER) initiative, which is a multi-agency effort to invest resources into the communities that were negatively impacted by changes in the coal economy. The project is The Central Appalachian Food Enterprise Corridor, which is designed to coordinate local food distribution networks throughout the coal-impacted areas of Ohio, West Virginia, Tennessee, Southwest Virginia, and Eastern Kentucky. The networks are intended to connect established and emerging producers to wholesale distribution markets in order to achieve new job creation, industry diversification, and new business start-ups. ASD, as the primary grantee, is responsible for administering the overall project and funds in partnership with other organizations in the region, including the Appalachian Center for Economic Networks and Unlimited Future, Inc., which both served as sub-grantees.

Objectives, Scope, and Methodology

The audit objectives were to determine whether: (1) program funds were managed in accordance with the ARC and Federal grant requirements; (2) grant funds were expended as provided for in the approved grant budget; (3) internal grant guidelines, including program (internal) controls, were adequate and operating effectively; (4) accounting and reporting requirements were implemented in accordance with generally accepted accounting principles (or other applicable accounting and reporting requirements); and (5) the matching requirements; and (6) the established performance measures were met or likely to be met.

The grant covered the period September 1, 2016 to September 1, 2018, and provided \$1,500,000 in ARC funding and required \$798,140 in non-federal matching funds from ASD. The funding was used to cover salaries, travel, contractual costs, equipment purchases, and participant training. Planned non-federal matching funds included contributed ASD and partner salaries, equipment, and other operating costs. The grant was open and active at the time of the audit. ASD reported ARC expenditures of \$1,269,855 and non-federal matching of \$697,320 as of April 30, 2018, for a total of \$1,967,175. We tested \$417,833 of the ARC expenditures and \$128,377 of non-federal matching funds to determine if the charges were properly supported and allowable.

We reviewed documentation provided by ASD and interviewed the Executive Director and other personnel to obtain an overall understanding of the grant activities, accounting system, and general operating procedures and controls applicable to the grant. We reviewed financial and project progress reports to determine if they were submitted to ARC in accordance with requirements. We reviewed the most recent A-133 audit report to identify any issues impacting the ARC grant and the grant audit. We reviewed matching funds documentation to determine if requirements were met. We evaluated grant results discussed in the project progress reports to determine if the planned performance goals and objectives were met.

The primary criteria used in performing the audit were 2 CFR 200, the ARC Code, and the grant agreement. The audit was performed in accordance with the *Government Auditing Standards*.

The on-site fieldwork was performed at the ASD offices in Abingdon, Virginia during August 6 - 10, 2018. The preliminary results were discussed with the ASD staff at the conclusion of the on-site visit and they were in general agreement with the issues identified and the related recommended actions.

Summary of Audit Results

Overall, ASD's financial management and administrative procedures and related internal controls were adequate to manage the funds under the ARC grant audited. However, we noted several areas that could be improved, including the allocation of grant costs, non-competitive procurement, and the estimates and timely expenditures of grant advances.

Financial and project reporting requirements were being met and the progress reports were considered excellent in their content and format. The non-federal matching funds were being documented and it appeared the matching requirements would be fully met by the end of the grant.

We questioned \$154,000 of costs on two contracts because the non-competitive awards were not adequately justified and the required costs analysis was not performed prior to the award for either contract. Also, we questioned \$24,148 in costs that were allocated to the grant as shared costs, such as trucking fees, fuel, and utilities, because the allocation basis was not adequately supported and consistent.

The grant had not ended at the time of the audit, so the final project progress report and performance results were not yet available. Interim results as of April 30, 2018 showed that four of seven planned output and outcome goals had been met, exceeded, or on track. These included 204 businesses improved out of a projected 150, 314 businesses served out of a projected 450, 726 jobs retained out of a projected 250, and two plans/reports had been prepared out of a projected three. There were three goals that had not been met as of April 30, 2018. A goal was set for obtaining \$2,000,000 of leveraged private investment under the grant, but only \$570,615 had been achieved. This was mostly because a large investment for a food processing operation expected to be established by an out-of-state company did not occur. New businesses created as of April 30, 2018 was listed as 35 out of a projected 95 and listed 74 new jobs created out of a projected 120. ASD was optimistic that additional progress was possible on these goals after the grant ends, as the program continues to reach out to new areas and participants, and they were planning to continue providing ARC information on these goals.

The questioned costs, procedural issues, and recommended corrective actions are discussed in the Findings and Recommendations section of this report.

Findings and Recommendations

A. Allocation of Grant Costs

We questioned \$24,148 of the costs charged to ARC's grant because the allocation basis used by the recipient was not documented in its accounting records, and the actual percentage used varied at times for the same type of costs.

Per the cost principles in 2 CFR 200.405, if a cost benefits the ARC grant and other ASD work or projects, it may be allocated either on a proportional basis that can be easily identified or any other reasonable documented basis. The cost principles and generally accepted accounting principles expect that the allocation basis, once established, would be applied consistently unless the basis is revised and documented.

We selected a sample of costs charged to the grant and examined the supporting documentation to verify they were properly supported, reasonable, and allowable. In reviewing these costs and documentation provided, we identified several categories of costs where ASD was allocating a portion of the total invoice or receipt amount to ARC grant funds and the rest to one or more other activities or accounts.

The allocation rates used for the expense categories to determine the charges to ARC were not consistently applied for each cost category. For example, we determined that Gas and Electric costs were allocated between 40% and 48%, Fuel costs were allocated between 15% and 16%, Truck/Hauling fees were allocated between 15% and 100%, and Vehicle Maintenance costs were allocated between 15% and 33%. Lacking sufficient supporting documentation and a clear explanation of the allocation basis used and the reasons for rate fluctuations, we were unable to fully verify the reasonableness and support for these costs. As a result, we questioned the dollar amounts sampled in these categories: \$4,509 for Gas and Electric, \$1,135 for Vehicle Maintenance, \$5,363 for Truck Fuel, and \$13,141 for Truck/Hauling fees, for a total of \$24,148 in questioned costs.

Recommendations

Prior to submitting the final financial SF-270 report to ARC to close out the grant, ASD should:

1. Establish and document a reasonable basis for allocating costs to ARC funds for all the cost categories questioned, as well as any other cost categories not included in the audit sample.
2. Apply the formal rates that are established and adjust the previous amounts charged to the ARC grant for those costs.
3. Use the adjusted amounts in preparing the final SF-270 report for final reimbursement, refunding any excess prior reimbursement, if applicable.
4. Attach a description of the documented basis used to support the SF-270 report.
5. Revise the ASD policies and procedures to establish requirements compliant with federal guidance for determining which costs can be allocated and what the most reasonable basis of these costs is to ARC and other grants.
6. Ensure the basis and rates are documented and consistently followed in recording costs on all grants.

Grantee's Response

The grantee responded they concur with the finding and they have implemented the six recommendations. They stated they have implemented a policy that all grants that include allocated costs must have a documented reasonable basis for how the costs are allocated and this documentation will be stored with grant files and followed by program and financial personnel when creating reports and preparing reimbursement requests.

Auditor's Comments

ARC will determine whether the actions identified in the grantee's response are adequate to resolve the finding and close the recommendations.

B. Documentation of Non-Competitive Procurements

ASD awarded two contracts for consulting and professional services on a non-competitive basis; however, the procurement files were not documented with justification for the sole source procurements. Also, there was no evidence that a cost analysis had been performed to support that the contract prices were fair and reasonable before the contracts were awarded. Therefore, we questioned the total \$154,000 charged to ARC grant funds for these two contracts.

The primary federal policies and requirements applicable to procurement under this grant are contained in Procurement Standards, 2 CFR 200.318 through 200.326. Grantees like ASD are expected to use their own documented procurement procedures provided the procurements meet applicable Federal law and the procurement standards listed above. The standards in sections 318-326 include:

- Maintaining records sufficient to document the procurement history, including rationale for procurement method, contract type used, contractor selection, and basis for the contract price;
- All procurements being conducted in full and open competitive basis except for certain situations provided in the standards, such as an item or service being available from only one source;
- Performing some type of price or cost analysis on every procurement;
- Identifying and negotiating profit separately where there is not price competition or whenever cost analysis is performed.

Section Four of ASD's written policies, "Procurement Policies and Procedures," reflected many of the federal requirements. These included:

- Documenting procurements, including at least the basis for the selection, basis for reasonableness of cost, and basis for payment;
- Maximizing open and free competition regardless of the dollar value;
- Performing some type of price or cost analysis for every procurement;
- Requiring that non-competitive negotiations have a written determination by the Executive Director that competitive negotiation or bidding was not feasible.

ASD awarded a \$94,000 consulting contract to Small World Strategies LLC (that operates as Kallan Strategic Partners), and a \$60,000 professional services contract to New Ventures Advisors. Both were awarded on a non-competitive basis without identifying alternative sources or soliciting other offers or proposals. In reviewing the award and supporting documentation, we determined that ASD did not prepare a written justification or perform and document a cost analysis for either contract prior to award as required under both the federal and ASD policies. A written justification was prepared after the award following inquiries by ARC staff and was provided to us. Generally, ASD justified the two awards on the basis of the contractors having unique knowledge and experience in the local food industry, and ASD and the partners having previous experience with them. While this information covered some of the criteria for the contract selections, the justification was not adequate since it did not provide evidence to fully support the non-competitive selection, such as identifying other possible qualified sources.

2 CFR 200.323 states that the method and degree of analysis depends on the procurement situation, but as a starting point, the grantee must develop and utilize its own independent cost estimate in analyzing the proposed costs. Cost analysis is normally applicable to all non-competitive awards. It entails obtaining and examining the individual proposed costs, such as labor hours, rates, profit, etc., and comparing them to the internal estimate and applying other methods to determine if they are reasonable.

This occurred because ASD did not have written procurement policies and procedures that adequately established these requirements or provided guidance on when a cost analysis was necessary. As a result, the federal requirements and ASD's policies were not complied with, and the process for the awarding of the two contracts was not adequately supported.

Recommendations

Prior to submitting the final SF-270 financial report for grant close-out and obtaining final payment, ASD should:

1. Obtain information on the contracts with Kallan and New Ventures necessary to evaluate the individual costs and profit and determine the total amount reasonable to charge to ARC grant funds.
2. Make adjustments to the accounting records and amounts charged to ARC funds as needed based on this assessment.
3. Provide this information as support with the final SF-270 report and final reimbursable amount, and submit a refund if applicable.
4. Revise ASD procurement policies to ensure all the requirements in 2 CFR 200.318-326 are fully reflected and implemented, especially to ensure written justifications are required for all non-competitive procurements and that contractor cost details are obtained and an analysis is performed and documented on such procurements.

Grantee's Response

The grantee responded they concurred with the finding and are implementing the four recommendations. They stated, "ASD takes our responsibility for stewarding the funds entrusted to us very seriously. We are completely committed to making the best and most efficient use of the funds we are granted and we have updated our policies and procedures to abide by the regulations in 2 CFR 200.318-326. We wish to note that ASD used the competitive procurement process for all other equipment and services purchased using ARC POWER funding. We viewed these two consultants as partners in this work and integral to project success, which is why they were named in the proposal. That being said, this audit has helped us understand the distinctions we should have drawn and the processes we will need to follow in the future to ensure that federal policies are followed strictly to avoid the appearance of impropriety or unfair competitive advantage."

Auditor's Comments

ARC will determine whether the actions identified in the grantee's response are adequate to resolve the finding and close the recommendations.

C. Grant Advances

ASD requested funding in advance during the grant period. Grant officials typically submitted an SF-270 report every 120 days requesting advance funding for the next period. We reviewed two periods during which advance funding was requested, an advance of \$268,611 requested on 9/15/2017, and an advance of \$245,872 requested on 1/31/2018. We determined that on both advances, ASD had not completely expended the amount of advance funding received by the end of the 120 day period for which it was requested. On the \$268,611 advance, there was \$47,849 (18%) of ARC funds that had not been expended within 120 days after it was received. On the \$245,872 advance, \$74,572 (30%) had not been expended by the end of the 120 day period. Guidance under 2 CFR 200.305 allows grantees to obtain advance funding if they establish written procedures to minimize the time elapsing between the transfer of funds and the disbursement of funds. The amounts requested should reflect the minimum required to meet their immediate cash needs and be timed as closely as possible to when the actual disbursements are made. In addition, ARC allows grantees to obtain advance funding necessary to meet needs within the established reporting period, which for this grant was 120 days.

ASD had written procedures for cash management and how to process the drawdown of grant funds. However, the procedures did not provide guidance on how to keep advance requests to a minimum or how to ensure funds are dispersed timely and fully.

Recommendation

ASD should monitor each individual advance received as well as review and update their cash management policies and procedures related to requesting and utilizing advances of federal grant funds to ensure that the estimates for amounts requested are adequately documented and reflect the minimum amount of cash needed for the related period and the amounts received are expended timely and in total by the end of the period on which the request was based.

Grantee's Response

The grantee responded they concurred with the finding and have updated the cash management section of their Standards for Financial Management in accordance with the recommendation.

Auditor's Comments

ARC will determine whether the actions identified in the grantee's response are adequate to resolve the finding and close the recommendation.

October 12, 2018

Mr. Leon Snead
Leon Snead & Company, P.C.
416 Hungerford Dr # 400
Rockville, MD 20850

RE: ARC POWER Grant# PW-18601

Dear Mr. Snead,

Following please find Appalachian Sustainable Development's (ASD's) response to the audit findings provided to ASD on September 14, 2018.

ASD's response includes the following attachments:

1. Updated Internal Controls Manual
2. Allocation Methodology for the ARC POWER grant PW-18601
3. Justification for Procurement by Noncompetitive Proposal for New Venture Advisors
4. Profitability Calculation for New Venture Advisors CONFIDENTIAL
5. Justification for Procurement by Noncompetitive Proposal for Kallan Strategic Partners
6. Profitability Calculation for Kallan Strategic Partners CONFIDENTIAL

ASD concurs with the findings of the audit but wishes to make note of a consideration on the non-competitive procurement of the two contractors. ASD takes our responsibility for stewarding the funds entrusted to us very seriously. We are completely committed to making the best and most efficient use of the funds we are granted and we have updated our policies and procedures to abide by the regulations in 2 CFR 200.318-326. We wish to note that ASD used the competitive procurement process for all other equipment and services purchased using ARC POWER funding. We viewed these two consultants as partners in this work and integral to project success, which is why they were named in the proposal. That being said, this audit has helped us understand the distinctions we should have drawn and the processes we will need to follow in the future to ensure that federal policies are followed strictly to avoid the appearance of impropriety or unfair competitive advantage.

AUDIT RESPONSE

A. Allocation of Grant Costs Recommendations

Prior to submitting the final financial SF-270 report to ARC to close out the grant, ASD should:

1. Establish and document a reasonable basis for allocating costs to ARC funds for all the cost categories questioned, as well as any other cost categories not included in the audit sample.

Completed

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Appendix I

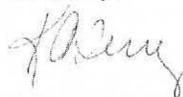
2. Apply the formal rates that are established and adjust the previous amounts charged to the ARC grant for those costs. **Completed**
3. Use the adjusted amounts in preparing the final SF-270 report for final reimbursement, refunding any excess prior reimbursement, if applicable. **Completed**
4. Attach a description of the documented basis used to support the SF-270 report. **Please see Attachment #2.**
5. Revise the ASD policies and procedures to establish requirements compliant with federal guidance for determining which costs can be allocated and what the most reasonable basis of these costs is to ARC and other grants. **Please see Attachment #1, Page 10.**
6. Ensure the basis and rates are documented and consistently followed in recording costs on all grants. **ASD has implemented a policy that all grants that include allocated costs must have a documented reasonable basis for how the costs are allocated. Documentation will be stored with grant files and followed by program and financial personnel when creating reports and preparing reimbursement requests.**

B. Documentation of Non-Competitive Procurements Recommendations

1. Obtain information on the contracts with Kallan and New Ventures necessary to evaluate the individual costs and profit and determine the total amount reasonable to charge to ARC grant funds. **Please see Attachments #3-6. (Note: New Venture Advisor's Non-Disclosure Agreement required that they not be named in the profitability calculation document)**
2. Make adjustments to the accounting records and amounts charged to ARC funds as needed based on this assessment. **Completed**
3. Provide this information as support with the final SF-270 report and final reimbursable amount, and submit a refund if applicable. **Completed**
4. Revise ASD procurement policies to ensure all the requirements in 2 CFR 200.318-326 are fully reflected and implemented, especially to ensure written justifications are required for all non-competitive procurements and that contractor cost details are obtained and an analysis is performed and documented on such procurements. **Please see attachment #1, Pages 77-80.**

Please let me know if you require any additional information to conclude this process. We appreciate the guidance provided by the auditor and, it should be noted, are sharing these findings (via webinars) with our nonprofit partners to ensure that these lessons can be of benefit to a wide range of nonprofits.

Sincerely,



Kathlyn Terry
Executive Director

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