Office of Inspector General
Corporation for National and Community Service

FISCAL YEAR 2012 EVALUATION OF THE CORPORATION'S COMPLIANCE WITH IMPROPER PAYMENTS ELIMINATION AND RECOVERY ACT (IPERA)

OIG REPORT 13-04

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This report was issued to Corporation management on March 14, 2013. Under the laws and regulations governing audit follow-up, the Corporation is to make final management decisions on the report's findings and recommendations no later than September 16, 2013 and complete its corrective actions by March 14, 2014. Consequently, the reported findings do not necessarily represent the final resolution of the issues presented.

Office of Inspector General

Corporation for NATIONAL & COMMUNITY SERVICE

March 14, 2013

TO: Wendy Spencer
Chief Executive Officer

FROM: Stuart Axenfeld
Assistant Inspector General for Audit

SUBJECT: Office of Inspector General (OIG) Report 13-04: *Fiscal Year 2012 Evaluation of the Corporation's Compliance with Improper Payments Elimination and Recovery Act (IPERA)*

Attached is the final report on the OIG's *Fiscal Year 2012 Evaluation of the Corporation's Compliance with Improper Payments Elimination and Recovery Act (IPERA)*. This evaluation was performed by OIG staff in accordance with the Quality Standards for Inspection and Evaluation.

Under the Corporation's audit resolution policy, a final management decision on the findings in this report is due by September 16, 2013. Notice of final action is due by March 14, 2014.

If you have questions pertaining to this report, please contact Thomas Chin, Audit Manager, at (202) 606-9362 or t.chin@cncsoig.gov; or me at (202) 606-9360 or s.axenfeld@cncsoig.gov.

Attachment

cc: Robert Velasco II, Chief Operating Officer
David Rebich, Chief Financial Officer
Douglas Hilton, Director of Accountability and Oversight

CONTENTS

TABLE OF ACRONYMS

AFR	Agency Financial Report
FFR	Federal Financial Report
FY	Fiscal Year
IPIA	Improper Payments Information Act of 2002
IPERA	Improper Payments Elimination and Recovery Act
OIG	Office of Inspector General
OMB	Office of Management and Budget

EXECUTIVE SUMMARY

In response to the President's July 2010 mandate on implementing the Improper Payments Elimination and Recovery Act (IPERA), the Office of Inspector General (OIG), Corporation for National and Community Service (Corporation) performed an evaluation of the Corporation's compliance with IPERA. The objective of our evaluation was to determine whether the Corporation performed its improper payments assessment in compliance with IPERA, applicable Executive Orders, and the Office of Management and Budget (OMB) guidance.

For the second year in a row, the OIG concludes that the Corporation continues to understate its improper payments and has not accurately assessed the susceptibility of at least some of its programs. Six OIG audits of AmeriCorps State and National grantees—representing a small fraction of the grant portfolio—in Fiscal Year (FY) 2012 uncovered questioned costs of approximately $ 3.6 million. Experience suggests that similar problems exist elsewhere in the portfolio, making improper payments more prevalent than the Corporation acknowledges. Despite this, the Corporation's FY 2012 Agency Financial Report (AFR) does not contain an estimate of improper payments, does not describe the actions taken or to be taken to prevent and recover improper payments, and does not address the adequacy of its internal controls.

The Corporation's approach to identifying and reducing improper payments requires further development. The assessment that the Corporation obtained from a consultant was poorly designed and not likely to yield useful information. First, the Corporation selected FY 2010 as the period to be reviewed, making the results untimely when they were delivered in FY 2012. The Corporation has not attempted to estimate or evaluate its improper payments for FY 2011 or FY 2012. Second, with the Corporation's consent, virtually all of the testing undertaken by the consultant occurred at the grant level. There was no review of individual disbursements, eligibility of members for stipends and education awards, or allowability of costs paid by grantees, although a long history of OIG audits demonstrates that deficiencies in these areas give rise to millions of dollar of improper payments. Third, both the Corporation's risk assessment and its estimate disregarded specific findings from OIG audit reports and investigations. Without acknowledging known risks and a reliable estimate of improper payments, the Corporation cannot strengthen its internal controls to prevent their recurrence.

One important opportunity to reduce improper payments lies in appropriate utilization of the Department of Treasury's (Treasury's) Do Not Pay solution to verify the eligibility of potential recipients of Federal funds. The Corporation has not yet taken advantage of this resource, which exists to prevent improper payments. We believe that the Corporation should develop a plan for doing so, including the use of data analytic services offered as part of the Do Not Pay solution.

RESULTS OF EVALUATION

Finding 1. The Corporation has not complied with the reporting requirements of IPERA.

IPERA requires the Corporation to include in its AFR:

a. A statistically valid estimate of improper payments in every program or activity determined to be susceptible to significant improper payments, defined as (i) more than $10 million in amount and (ii) more than 2.5 % of program outlays;
b. A report on actions by the Corporation to reduce and recover improper payments; and
c. A statement as to whether the Corporation has sufficient resources—including internal controls, human capital, information systems and other infrastructure—to prevent improper payments, and, if it does not, a description of the additional resources needed to do so.

The Corporation's FY 2012 AFR relies upon a determination made the prior year that none of its programs were susceptible to significant improper payments under IPERA criteria. FY 2012 AFR at page 86. Accordingly, the FY 2012 AFR contains no estimate of improper payments in any program, does not describe actions to reduce improper payments or recover them after the fact, and does not address the adequacy of the Corporation's internal controls.

The FY 2012 AFR does not explain the basis for the Corporation's determination that none of its programs is susceptible to significant levels of improper payment and contains no description of the assessment procedures that led to this conclusion. The OMB Circular A-136, *Financial Reporting Requirements*, Section II.5.8, IPIA [Improper Payments Information Act of 2002] (as amended by IPERA) Reporting Details, describes the format that agencies should use for improper payment reporting in their annual AFRs, including: risk assessment, statistical sampling, corrective actions, and improper payment reduction outlook table. The Corporation did not follow this reporting format.

The OIG believes that one or more of the Corporation's programs are in fact susceptible to significant improper payments. A mere six audits of AmeriCorps State and National programs conducted by the OIG in FY 2012 identified more than $3.6 million questioned costs.[1] Those audits covered only a small fraction of the approximately 368 AmeriCorps State and National active grants overseen by the Corporation. However, our experience suggests that the problems that gave rise to these questioned costs are widespread and result in a greater incidence of improper payments than the Corporation has acknowledged.[2] Because the Corporation has underestimated the extent of its improper

[1] A questioned cost is an alleged violation of a provision of law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds or a finding that, at the time of testing, includes costs not supported by adequate documentation.

[2] In addition to the six OIG audits referenced above, a recent OMB Circular A-133 audit of a state service commission identified improper costs of more than $91,000 and estimated another $517,000 in questioned costs. Similarly, a search warrant affidavit recently made public contained detailed information concerning a $4 million theft and fraud investigation of a grantee. Although the Corporation was not on notice of these particular improper payments in FY 2012, we offer them as examples that tend to confirm our view that significant improper payments are occurring.

payments, the IPERA section of the Corporation's FY 2012 AFR was incomplete and not adequately presented.

Recommendations

We recommend that the Corporation:

1a. Re-evaluate the susceptibility of its programs to improper payments, taking into account all available information;

1b. Include in future AFRs detailed descriptions of the procedures performed in connection with its evaluation of improper payments (to include risk assessment, sample methodology, and testing), and provide well founded estimates; and

1c. Specify what actions the Corporation has taken or plans to take to reduce improper payments and describe whatever additional resources it needs to make meaningful progress in this area.

Finding 2. The Corporation's methodology used to assess and estimate improper payments was insufficient and ineffective (a modified repeat finding from prior year).

As in the prior year, the Corporation could not prepare a reasonable and reliable estimate of its improper payments because its methodology was fundamentally flawed. In our FY 2011 assessment, we found that the Corporation had directed its IPERA consultant not to test whether payments were made for their intended purpose, i.e., whether payments were being used to support unallowable activities. Our FY 2012 assessment likewise found a basic inadequacy in the Corporation's methodology, in that the tested attributes were limited to the grant level, and did not address the permissibility of disbursements from those grants. The attributes tested by the Corporation for AmeriCorps State and National and Senior Corps grants included:

- Verifying that the grant application was complete
- Verifying that the grant application was certified/approved
- Searching the List of Parties Excluded from Federal procurement or non-procurement programs to ensure recipient does not appear on the list
- Confirming whether the grant was subject to a hold, and, if so, verifying that there were no unauthorized drawdowns of funds
- Verifying that drawdowns did not exceed the awarded amount
- Verifying that the grantee completed a Federal Financial Report (FFR)
- Verifying that Program Officers performed monitoring and reviewed progress reports for eligible grant program activities as evidenced in eGrants

None of these attributes would detect whether disbursements from these grants were improper, as OIG frequently discovers when auditing grantees. Although the total value of the sampled transactions was high—$45,776,943 for AmeriCorps State and National programs, and $7,559,611 for Senior Corps programs—all but three of the individual transactions sampled by the consultant represented the entire grant amount, without any testing of downstream disbursements from the grants, allowability of costs incurred by the grantee, or member eligibility. The sheer size of the sample—411 grants, split between Senior Corps and AmeriCorps—precluded meaningful testing of disbursements. Without testing the use of the grant proceeds, treating the entire grant amount as “proper” presents a misleading picture.

Certain of the attributes were not properly designed, even if the only objective was testing at the grant level. For example, verifying that a grantee has completed an FFR is important, but the review is incomplete unless that FFR reconciles to the grantee’s internal financial records and the drawdown records maintained by the Department of Health and Human Service’s Payment Management System. By failing to conduct a more thorough FFR review, the Corporation missed key opportunities to detect potential improper payments.

Further, we noted that the Corporation conducted its FY 2012 improper payment review and testing based on transactions in FY 2010, yielding outdated results. In response to our inquiry as to why a more recent period was not selected, the consultant stated that this was the only data provided by the Corporation, and that the testing scope was determined by the Corporation on the basis of document availability, time limitation, and resource constraints. The sample coverage was also inadequate in that it included only two contracts and one credit card payment.

We believe it is likely that the Corporation has understated the magnitude of improper payments in its programs. Overall, we consider the attributes tested, the sample size, coverage, and period tested by the Corporation were insufficient to properly assess and/or detect instances of improper payments. Without a sound methodology, the Corporation cannot obtain a meaningful estimate of its improper payments or determine what measures would be most effective to prevent them from recurring.

Recommendations

We recommend that the Corporation:

2a. Develop a comprehensive testing plan to include attributes to verify that the Corporation did not make payments or undertake obligations to ineligible members, for unallowable or prohibited activities or based on inadequate documentary support. It is efficient to incorporate this type of testing in the internal control structure used to manage high-risk programs; and

2b. Ensure that the sample size, coverage, and period utilized to analyze improper payments will enable sufficient, comprehensive, and timely testing.

Finding 3. The Corporation's efforts to estimate improper payments did not address all known weaknesses (a repeat finding from prior year).

Again this year, the Corporation's efforts to estimate improper payments overlooked improper payments identified in OIG audits and investigations and OMB Circular A-133[3] audit reports. The consultant confirmed that these sources had not been incorporated into its analysis, citing "funding restrictions and limited scope" as the reasons. As a result, the Corporation has understated its improper payments although the relevant information was readily available; as previously noted, for FY 2012, OIG audits alone identified questioned costs totaling more than $3.6 million. Ignoring these tools for the second year in a row calls into question the rigor of the Corporation's efforts in the realm of improper payments.

Quite apart from the specific questioned costs quantified in audits conducted by the OIG, the repetitive nature of the audit findings that lead to questioned costs suggests that many improper payments are going undetected by the Corporation's own monitoring and prevention efforts. Under the circumstances, a more robust assessment of improper payments is needed, together with a rigorous review of root causes and internal control weaknesses.

Recommendations

We recommend that the Corporation:

3a. Implement effective testing procedures to completely and accurately identify the full extent of improper payments by capturing improper payments identified in OIG audits and investigations as well as OMB Circular A-133 reports;

3b. Utilize existing Corporation monitoring tools, including quarterly reviews, internal control reviews, and grantee/subgrantee monitoring reviews, to enhance the process of identifying and recovering improper payments; and

3c. Conduct a thorough review of the root causes of improper payments in order to determine how best to strengthen its internal controls to prevent such payments in the future.

Finding 4. The Corporation does not make use of the Treasury's Do Not Pay solution and did not establish a plan to do so, as required by OMB Memorandum M-12-11.

In June 2010, the President directed the establishment of a Do Not Pay List, a single-point-of-entry network of databases to be consulted before determining eligibility for any Federal funding. Its purpose was to prevent improper payments by centralizing resources that could be used to identify ineligible recipients. The mechanism developed by OMB and the Treasury, known as the Do Not Pay solution, consists of two components:

[3] OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, Subpart B -- Audits, §___.200, Audit requirements., (b), states "[n]on-Federal entities that expend $300,000 ($500,000 for fiscal years ending after December 31, 2003) or more in a year in Federal awards shall have a single audit conducted."

- A web-based, single-entry access portal that enables agencies to verify the eligibility of potential recipients of Federal funds; and
- Data Analytics Services that utilize additional resources to identify trends, anomalies, risks and patterns of behavior associated with improper payments.

In April 2012, OMB issued instructions that "Federal agencies must take immediate steps to use the centralized solutions that are already in place for pre-payment eligibility reviews." OMB Memorandum M-12-11, *Reducing Improper Payments through the "Do Not Pay List*" at page 2. To that end, each agency was required to submit a plan for using the Do Not Pay solution. *Id*. The Corporation did not respond, nor has it made use of this resource to date.

The OIG has introduced the Corporation's Office of Accountability and Oversight to representatives of the Do Not Pay solution, to explore how the Corporation might best make use of this resource. The OIG hopes that the Corporation will take full advantage of the Do Not Pay solution as an efficient means to prevent improper payments, including disbursements from Corporation grants.

Recommendations

We recommend that the Corporation:

4a. Work with the Treasury Department to develop a detailed plan for using the Do Not Pay solution, including its data analytic capability;

4b. Integrate use of the Do Not Pay solution into the Corporation's operations; and

4c. Measure the results of using the Do Not Pay solution by tracking the improper payments avoided.

OBJECTIVE, SCOPE, AND METHODOLOGY

Our evaluation objective was to determine whether the Corporation performed its improper payment assessment in compliance with IPERA, applicable Executive Orders, and OMB guidance.

We conducted this evaluation in accordance with the Quality Standards for Inspection and Evaluation issued by the Council of the Inspectors General on Integrity and Efficiency.

We performed our evaluation from October 2012 to February 2013 at the Corporation's Headquarters in Washington, DC. Our evaluation entailed a review and assessment of the Corporation's efforts in determining and reporting improper payments. We conferred with Corporation personnel regarding their work in assessing improper payments and to reiterate the concerns expressed in last year's IPERA review regarding design of the testing attributes and omission of OIG's audit results from the Corporation's overall improper payment assessment. We conducted interviews with the consultants who were retained by the Corporation to obtain an understanding of the work they performed, including methodology, results of risk assessments, and testing procedures and results.

We reviewed their reports and supporting documentation to determine whether the methodology and testing procedures used to assess improper payments were reasonable, sound, and reliable. The Corporation reviewed and tested payments made between October 1, 2009 and September 30, 2010.

In addition, we reviewed prior audit reports to identify questioned costs that should have been incorporated into the Corporation's overall improper payment assessments. We also reviewed applicable laws and regulations (such as OMB Circular A-123, Appendix C; the IPERA [Public Law 111-204]; the OMB Memorandums M-11-04, M-11-16, M-12-11; and Executive Order 13520), and the Corporation's FY 2012 AFR.

BACKGROUND

An improper payment is defined as any payment that should not have been made or that was made in an incorrect amount, to an ineligible recipient or for ineligible goods or services or for goods and services that were not received, any duplicate payment, or any payment that does not account for credit for applicable discounts.[4] Improper payments may result from inadequate recordkeeping, inaccurate eligibility determinations, inadvertent processing errors, the lack of timely and reliable information to confirm payment accuracy, or fraud. OMB guidance instructs agencies to report as improper payments of any payments for which insufficient or no documentation was found.

To implement the goal of reducing wasteful improper payments, the President signed IPERA into law in July 2010.[5] IPERA requires agencies to identify programs or activities that are susceptible to significant improper payments, conduct a risk assessment, perform testing of programs considered high risk, test a sample of transactions, determine the estimated amount of improper payments, and develop and implement corrective actions plans for high risk programs.

OMB Circular A-123, Appendix C, provides guidance to Federal agencies on implementing IPERA which reinforces significant reliance on internal controls. As stated in the Government Accountability Office's testimony before the "Subcommittee on Government Organization, Efficiency, and Financial Management, Committee on Oversight and Government Reform, House of Representatives" on February 7, 2012, implementing strong preventive controls can help defend against improper payments, increasing public confidence and avoiding the difficult "pay and chase" aspects of recovering improper payments. Preventive controls involve activities such as upfront validation of eligibility using electronic data matching, predictive analytic tests, and training programs.

In recent years, the Federal government has made eliminating improper payments a focal point targeting reduction in fraud, waste, and abuse. IPERA requires the following:

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[4] OMB Circular A-123, *Management's Responsibility for Internal Control*, Appendix C. *Requirements for Effective Measurement and Remediation of Improper Payments*, April 14, 2011.

[5] In additions to the existing IPERA legislation, the President signed the Improper Payments Elimination and Recovery Act of 2012 in December 2012, which requires OMB to issue additional rules to agencies requiring more consistent and complete estimates of overpayments. The law also codifies the executive order regarding the establishment of a government-wide "Do Not Pay List." This new Act becomes effective from FY 2013.

- Increased transparency and intensified agency efforts in preventing, identifying, and recovering payment errors within Federal spending;

- Agencies annually identify programs and activities susceptible to improper payments, estimate the annual amount of improper payments and submit the estimate to the President and Congress. Agencies are to include the estimates in their AFR; and

- Inspector General reviews of agency's improper payment reporting in the AFR and report on the agency's compliance.

The Corporation's Office of Accountability and Oversight was established in FY 2012 and is responsible for reporting on the Corporation's compliance with IPERA. The Corporation contracted with a consulting firm to conduct improper payment testing on programs deemed to be of the highest risk. The Corporation selected payments from the AmeriCorps State and National as well as payments from the Senior Corps programs for the FY 2012 IPERA reporting. The scope of the payments was made between October 1, 2009 and September 30, 2010. The consultants tested a total of 414 payment samples. For FY 2010, the AmeriCorps State and National and the Senior Corps reported outlays of approximately $526 million. The Corporation reported no improper payment based on the testing procedures it performed.

EXIT CONFERENCE

We discussed the contents of this draft report with Corporation representatives at an exit conference held on February 27, 2013. We summarized the Corporation's response to the draft report below and included its response, in its entirety, as Appendix A.

CORPORATION RESPONSE

Corporation management generally concurred with our determination that it needs to make substantial improvements to is analysis and estimation of improper payments. The Corporation stated that it intends to undertake a comprehensive review of its programs to determine their susceptibility to significant levels of improper payments, and its preliminary analysis indicates that the AmeriCorps State and National program is most likely to reach that threshold. The Corporation plans to work with us on how our findings can be used in planning a comprehensive, statistically-projectable review of unallowable grant costs and developing means of using the Do Not Pay solution as part of the Corporation's internal controls.

OIG COMMENT

We look forward to working with the Corporation to reduce and eliminate improper payments, including integrating Do Not Pay solution capabilities into its internal control and implementing a reliable methodology for estimating unallowable grant costs. Compliance with these OMB requirements should go a long way towards reducing waste and fraud and ensuring that public resources are spent efficiently and effectively. We welcome the Corporation's acknowledgement that its prior efforts have been insufficiently rigorous, and that the high questioned costs identified in recent audits cast doubt on the Corporation's past determination that none of its programs presents a significant risk of improper payments. We will continue to assess the Corporation's progress in complying with IPERA and its efforts to estimate and reduce improper payments.

Stuart Axenfeld, Assistant Inspector General for Audit
Office of Inspector General
Corporation for National and Community Service

Appendix A

Corporation's Response to Draft Report

Corporation for
NATIONAL & COMMUNITY SERVICE

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To: Stuart Axenfeld, Assistant Inspector General for Audit

From: Douglas Hilton, Director of Accountability and Oversight

Date: March 12, 2013

Subject: Comments on the Office of the Inspector General's (OIG) Draft Report Fiscal Year 2012 Evaluation of the Corporation's Compliance with the Improper Payments Elimination and Recovery Act (IPERA)

Thank you for the opportunity to review the draft OIG report on the Corporation for National and Community Service's (CNCS) compliance with IPERA. Rather than respond to each of the findings in the draft report individually, CNCS will respond to the findings generally and to the overall results of the OIG's evaluation. Those overall results are that CNCS needs to do far more than it has in the past in regard to analyzing the potential for and calculating estimates of improper payments made within its programs. With this criticism, CNCS concurs. CNCS' approach to its IPERA analysis is being led by a different management structure, including a new Chief Financial Officer and the recently established Office of Accountability and Oversight. CNCS is committed to a comprehensive assessment under IPERA and its implementing guidance, and appreciates the constructive feedback of the OIG.

As we reported in our fiscal year 2012 Agency Financial Report, in 2013 CNCS is undertaking a new review of whether its programs are susceptible to significant levels of improper payments as defined in IPERA and all the relevant implementing guidance. Preliminary analysis indicates that the AmeriCorps State and National (ASN) grant program would be most the likely CNCS program to reach the IPERA threshold of being subject to significant levels of improper payments.[1]

As the OIG points out, there are a number of OIG and A-133 audits that call significant amounts of claimed AmeriCorps grantee costs into question. Having considered various accepted methods for estimating improper payments, CNCS has concluded that assessments of improper payments within its grant programs should be based upon assessing unallowable costs charged to grant funds by grantees. However, relying on ASN grant costs which are disallowed after being questioned in audits is not a sufficient basis for conducting an analysis IPERA. This is because those audits are not undertaken on a basis that allows for statistically valid projections of disallowed costs across an entire grant program as required under OMB Circular A-123, Appendix C. Many of the OIG's most recent audits (some of which have identified the highest levels of questioned costs) have been conducted at the request of CNCS because of concerns that

[1] CNCS' evaluation will include all of its programs. However, because the balance of its programs are significantly smaller than AmeriCorps grants, CNCS considers it highly unlikely that any other program will have improper payments which approach the $10 million IPERA threshold.

arose in the context of the comprehensive ongoing grantee monitoring that CNCS conducts. These audits occur when CNCS identifies an anomalously high level of risk in certain programs, rather than when an average or low level of risk is present. This has been especially true in FY 2012 and 2013. As the OIG's funding has been severely reduced, more of its audit work has been occurring in programs specifically identified by CNCS as higher risk as part of its ongoing oversight and monitoring. While ongoing grantee monitoring and resultant audits are vital components of CNCS' overall system of accountability, they do not meet the specific objectives of improper payment testing under IPERA and its implementing guidance because the skewing of audit work toward higher risk grantees severely erodes the value of those audit results as an overall assessment of the susceptibility of the ASN grant program to significant improper payments.

For these reasons, CNCS is planning a comprehensive, statistically-projectable review of costs incurred by ASN grants to develop a basis on which to assess the level of costs that are improper on the basis of not conforming to the terms and conditions of CNCS' awards (including the associated Office of Management and Budget cost principles). We anticipate that this analysis will give CNCS a proper basis on which to pursue further activities designed to ensure compliance with IPERA. We look forward to discussing with OIG how its findings can be used as part of planning that work.

In addition, CNCS concurs with OIG's specific recommendation to consider using the Treasury Department's Do Not Pay solution as part of CNCS' grant award and oversight processes, as well as other appropriate programs and operations. CNCS' CFO and Director of Accountability and Oversight recently met with OIG and Treasury officials to receive a briefing on the functionality of the various Do Not Pay databases, as well as the data analytics which are available. CNCS looks forward to working with the OIG in developing means of using Do Not Pay resources as part of our system of internal controls.