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NATIONAL ENDOWMENT FOR THE ARTS OFFICE OF INSPECTOR GENERAL

Performance Audit Report on Selected Awards to Washington State Arts Commission Olympia, WA

Report No. OIG-21-03

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SUMMARY

We conducted a performance audit of two National Endowment for the Arts (Arts Endowment) Partnership awards issued to the Washington State Arts Commission (ArtsWA). Based on our review, we determined ArtsWA generally met the financial and compliance requirements in the award documents. However, we identified some areas requiring improvement. For instance, we found that ArtsWA:

- Included \$31,000 in unallowable cost share on its Federal Financial Reports (FFRs).
- Included \$19,458 in unallowable entertainment costs on its FFRs.
- Did not notify all subrecipients of Federal subaward management requirements.
- Did not verify potential vendors were eligible to receive Federal funds.

We believe the evidence obtained during the audit provides a reasonable basis for our findings and conclusions based on our audit objectives. We are questioning \$50,458 (\$31,000 plus \$19,458) in unallowable costs. We also made six recommendations to address the audit findings -- four to ArtsWA and two to the Arts Endowment.

INTRODUCTION

AUDITEE BACKGROUND

The Washington State Arts Commission (ArtsWA) is a state agency dedicated to advancing the role of the arts in the lives of individuals and communities throughout the state. ArtsWA was established in 1961 with the mission to nurture and support the role of the arts in the lives of all Washingtonians. ArtsWA achieves its mission by maintaining a State Art Collection, providing grant opportunities, supporting K-12 arts education, and supporting communities that connect arts and culture to economic development. ArtsWA is supported by annual appropriations from the state Legislature, funds from the National Endowment for the Arts (Arts Endowment), and corporate sponsorships. These funds are primarily used to maintain the State Art Collection, pay personnel expenses, and issue grants.

OBJECTIVES, SCOPE, AND METHODOLOGY

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 and appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. The objectives of this audit were to determine whether:

- ArtsWA's financial management system and recordkeeping comply with requirements established by the Office of Management and Budget (OMB) and the Arts Endowment's *General Terms and Conditions for Partnership Agreements (General Terms)*;
- ArtsWA fulfilled the financial and compliance requirements in the award documents, including any required cost share/matching; and

- Reported award costs were reasonable, allocable, and allowable.

We limited the scope of our audit to two awards (see table below) closed during the period of May 1, 2017 through April 30, 2020. Both awards were Partnership grants issued to support activities in the Arts Endowment-approved state plan. Approved activities included issuing subawards, running general operations, and managing the Poetry Out Loud and Folk and Traditional Arts programs. The awards each had a one-to-one cost share match, and there were no amendments or de-obligations.

Award No.	Award Period	Award Amount	Reported Costs
17-6100-2024	07/01/17 – 12/31/18	\$820,400	\$2,232,083
1809822-61-18	07/01/18 – 12/31/19	830,800	2,500,871
Total		\$1,651,200	\$4,732,954

We conducted audit work to identify and test the operation and reliability of ArtsWA’s significant internal controls relevant to the audit objectives. As a result, we are not stating an opinion on the effectiveness and efficiency of ArtsWA’s overall internal control system. We identified two significant internal control components that were relevant to our audit objectives - control activities and monitoring. Control activity principles require ArtsWA to design and implement control activities that achieve mission objectives and respond to risks. Monitoring principles require ArtsWA to establish and operate activities to monitor and evaluate the internal control system, addressing deficiencies on a timely basis. Tests of these controls included audit work to verify the reliability of computer-processed data (CPD) provided by ArtsWA. Due to restrictions caused by the COVID-19 pandemic, tests of controls over CPD to ensure data reliability were conducted through virtual meetings and screen-sharing walk-throughs. We determined the data obtained and used for the purposes of this audit was reliable.

Additionally, we conducted reviews of ArtsWA’s financial procedures and performance outcomes to determine compliance with award requirements. This audit work included reviews of procedures and supporting documentation, and interviews with ArtsWA staff.

Finally, we conducted tests of subawards and transactions to determine the allowability of reported costs. We conducted risk assessments to determine subaward and costs transaction selection methods, and the testing levels necessary to support findings and conclusions. Based on the risk assessment results, we judgmentally selected three subawards from each award for compliance testing with subaward requirements. We also judgmentally selected 25 cost items from each award for cost allowability testing. These items included payroll, credit card, procurement, and subaward costs.

PRIOR AUDIT COVERAGE

The Arts Endowment Office of Inspector General had not issued any audit reports on ArtsWA in the past five years. The State of Washington had not issued any audit reports on ArtsWA within our audit scope period. However, ArtsWA was included in the state’s annual Single Audit

reports. As of our review, the most recent Single Audit report was issued by the Office of the Washington State Auditor on November 22, 2019, for fiscal year (FY) 2019. ArtsWA was included in the report's Schedule of Expenditures of Federal Awards (SEFA), though not selected for review as a major program. The report stated that the SEFA was fairly stated, in all material respects, in relation to the basic financial statements as a whole. Additionally, the auditors did not identify any major weaknesses or significant deficiencies in statewide operations that impacted ArtsWA.

However, during our review, we identified several misstatements in ArtsWA information reported on the FY 2019 SEFA. SEFA Partnership costs exceeded the 2018 award amount, though the reporting periods aligned. Additionally, expenditures incurred under an Arts Endowment subaward were misreported as a National Aeronautics and Space Administration award.

We followed up on these discrepancies during our review and determined ArtsWA's practice of recording all Federal award activity under one general account was a contributing factor (see the Unallowable Cost Share finding below).

AUDIT RESULTS

The following sections present a detailed discussion of the audit findings.

UNALLOWABLE COST SHARE

During our review, we determined that both Partnership awards' FFRs included unallowable costs paid by another Federal program. These unallowable costs totaled \$31,000 -- \$25,000 for the 2017 award, and \$6,000 for the 2018 award.

Arts Endowment awards are subject to the following

- **2 CFR 200.306 *Cost Sharing or Matching (b)* states in part:** For all Federal awards, any shared costs or matching funds and all contributions, including cash and third-party in-kind contributions, must be accepted as part of the non-Federal entity's cost sharing or matching when such contributions meet all of the following criteria:
 2. Are not included as contributions for any other Federal award;
 5. Are not paid by the Federal Government under another Federal award, except where the Federal statute authorizing a program specifically provides that Federal funds made available for such program can be applied to matching or cost sharing requirements of other Federal programs.
- **2 CFR 200.403 *Factors Affecting Allowability of Costs (f)* states:** Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards: Not be included as a cost or used to meet cost sharing or matching requirements of any other Federally-financed program in either the current or a prior period. See also 200.305 Cost Sharing or Matching, paragraph (b).
- **General Terms 9. *Financial Management and Internal Controls* states in part:** You must establish and maintain effective internal control over your award that provides

reasonable assurance that you are managing the award in compliance with Federal statutes, regulations, and the terms and conditions of the award. See recommended compliance documentation (2 CFR 200.303).

ArtsWA officials stated they forgot to remove the other program's costs when preparing the reports. We determined ArtsWA did not establish procedures or controls for ensuring Federal award cost requirements were met.

Including unallowable costs on award FFRs could lead to an audit conclusion that ArtsWA did not meet minimum cost sharing/matching requirements, potentially resulting in funds due back to the Arts Endowment. We reduced each award's allowable expenditures by the unallowable costs and determined ArtsWA still met the minimum cost share/match requirements.

We recommend ArtsWA document and implement procedures and controls that ensure that costs associated with other Federal awards funds are not included in Partnership awards' reported costs.

We recommend the Arts Endowment disallow \$31,000 in unallowable cost share/match - \$25,000 for the 2017 award, and \$6,000 for the 2018 award.

ArtsWA concurs with this finding and recommendation (see Appendix B).

UNALLOWABLE ENTERTAINMENT COSTS

The Governor's Arts and Heritage Awards (GAHA) Program issues annual awards to recognize and honor individuals and organizations for their significant contributions to the arts and cultural development of Washington State. ArtsWA was responsible for managing the program, including organizing annual galas to announce and honor award winners. During the 2017 and 2018 award periods, these galas were evening events featuring professional catering and cash bars, and funded in part by ArtsWA.

During our review, we identified \$19,458 in GAHA costs reported on award FFRs - \$8,458 for the 2017 award and \$11,000 for the 2018 award. These costs were related to catering, professional services, rental fees, and advertising. GAHA costs were not included in approved award activities, and ArtsWA did not receive written approval to report the costs under the Partnership awards. As a result, we determined these costs were unallowable entertainment.

Arts Endowment awards are subject to the following

- **General Terms 13. Cost Principles, 13.3.b Entertainment states:** Costs of entertainment, including amusement and social activities such as receptions, parties, galas, dinners, etc., and any associated costs including catering, alcohol, planning, staffing, supplies, etc. are unallowable. However:
 - i. Specific costs that might otherwise be considered entertainment but have a programmatic purpose may be allowable if authorized either in the approved budget for the Federal award or with prior written approval of the Federal awarding agency.

ArtsWA officials stated they did not intend to include GAHA costs on award FFRs; they forgot to remove the costs when preparing the reports. We determined ArtsWA did not establish documented procedures or controls for ensuring GAHA costs were excluded from award FFRs.

Including unallowable entertainment costs on award FFRs could lead to an audit conclusion that ArtsWA did not meet minimum cost sharing/matching requirements, potentially resulting in funds due to the Arts Endowment. We reduced each award's allowable expenditures by the unallowable costs and determined ArtsWA still met the minimum cost share/match requirements.

We recommend ArtsWA document and implement procedures and controls that ensure unallowable entertainment costs are excluded from award FFRs.

We recommend the Arts Endowment disallow \$19,458 in unallowable entertainment costs from award FFRs - \$8,458 for the 2017 award and \$11,000 for the 2018 award.

ArtsWA concurs with this finding and recommendation (see Appendix B).

SUBRECIPIENT NOTIFICATION

During the 2018 award period, ArtsWA initiated a new grant program – SNAP – targeting small and emerging groups and organizations. ArtsWA established policies to exclude the SNAP program from Partnership award activities; however, it did not establish procedures or controls to ensure the costs were excluded from Partnership FFRs. We identified 35 SNAP grants included on the 2018 award FFR. We verified these subrecipients were not notified of Federal award participation, or Federal subaward management requirements.

Arts Endowment awards are subject to the following

- **2 CFR 200.331 Requirements for Pass-Through Entities (a) states in part:** All pass-through entities must ensure that every subaward is clearly identified to the subrecipient as a subaward and includes the following information at the time of the subaward and if any of these data elements change, include the changes in subsequent subaward modification. When some of this information is not available, the pass-through entity must provide the best information available to describe the Federal award and subaward. Required information includes:
 1. Federal award identification;
 2. All requirements imposed by the pass-through entity on the subrecipient so that the Federal award is used in accordance with Federal statutes, regulations, and the terms and conditions of the Federal award; and
 3. Any additional requirements that the pass-through entity imposes on the subrecipient in order for the pass-through entity to meet its own responsibility to the Federal awarding agency including identification of any required financial and performance reports.

ArtsWA officials stated they forgot to remove the costs when preparing its FFR. We determined ArtsWA did not establish documented procedures or controls for ensuring SNAP grants were excluded from award FFRs. Including improper subaward costs on award FFRs could result in overstated final reports and non-compliance with Federal award management requirements.

We recommend ArtsWA document and implement procedures and controls that ensure FFR costs comply with its Federal award management policies.

ArtsWA concurs with this finding and recommendation (see Appendix B).

DEBARMENT AND SUSPENSION

ArtsWA established procedures to ensure potential subrecipients were eligible to receive Federal funds, but did not establish similar procedures for potential contractors. We determined that 12 contractors received most of ArtsWA's reported contractor costs, and verified that all 12 contractors were eligible to receive Federal funds.

Arts Endowment awards are subject to the following

- **2 CFR 180.300 *What must I do before I enter into a covered transaction with a person at the next lower tier? states:*** When you enter into a covered transaction with another person at the next lower tier, you must verify that the person with whom you intend to do business is not excluded or disqualified. You do this by:
 - i. Checking SAM exclusions;
 - ii. Collecting a certification from that person; or
 - iii. Adding a clause or condition to the covered transaction with that person.
- **General Terms 10. General Procurement Standards, 10.1.a states:** You should have written procedures to ensure that contractors or recipients are not debarred or suspended prior to the payment or award of Federal funds.

ArtsWA officials did not realize the debarment and suspension requirements applied to contractors as well as subrecipients; therefore, did not establish procedures or controls to ensure compliance. Without procedures and controls in place to verify that potential contractors are not suspended or debarred, Federal funds could be issued to ineligible recipients.

We recommend ArtsWA document and implement procedures and controls that ensure potential contractors are not debarred or suspended from receiving Federal assistance prior to the payment or award of Federal funds.

ArtsWA concurs with this finding and recommendation (see Appendix B).

RECOMMENDATION SUMMARY

We recommend ArtsWA:

1. Document and implement procedures and controls that ensure that costs associated with other Federal awards funds are not included in Partnership awards' reported costs.
2. Document and implement procedures and controls that ensure unallowable entertainment costs are excluded from award FFRs.
3. Document and implement procedures and controls that ensure FFR costs comply with its Federal award management policies.
4. Document and implement procedures and controls that ensure potential contractors are not debarred or suspended from receiving Federal assistance prior to the payment or award of Federal funds.

We recommend the Arts Endowment:

1. Disallow \$31,000 in unallowable cost share/match - \$25,000 for the 2017 award, and \$6,000 for the 2018 award.
2. Disallow \$19,458 in unallowable entertainment costs from award FFRs - \$8,458 for the 2017 award and \$11,000 for the 2018 award.

BREAKDOWN OF AWARD COSTS

<i>Award No. 17-6100-2024</i>	
Total Reported Costs	\$2,232,083
Less Unallowable Costs	
Subawards	(25,000)
Entertainment	(8,458)
Potential Allowable Reported Costs	<u>2,198,625</u>
Less Arts Endowment Disbursement	<u>(820,400)</u>
Potential Allowable Cost Share/Match	1,378,225
Less Required Cost Share/Match ¹	<u>(820,400)</u>
ArtsWA Cost Share/Match Exceeded	<u><u>\$557,825</u></u>

¹Required Cost Share/Match is equal to the Arts Endowment Disbursement amount

<i>Award No. 1809822-61-18</i>	
Total Reported Costs	\$2,500,871
Less Unallowable Costs	
Subawards	(6,000)
Entertainment	(11,000)
Potential Allowable Reported Costs	<u>2,483,871</u>
Less Arts Endowment Disbursement	<u>(830,800)</u>
Potential Allowable Cost Share/Match	1,653,071
Less Required Cost Share/Match ¹	<u>(830,800)</u>
ArtsWA Cost Share/Match Exceeded	<u><u>\$822,271</u></u>

¹Required Cost Share/Match is equal to the Arts Endowment Disbursement amount



WASHINGTON STATE
ARTS COMMISSION

July 28, 2021

Ron Stith, Inspector General
Office of the Inspector General
National Endowment for the Arts
400 7th Street SW
Washington, DC 20506

Dear Mr. Stith,

Thank you for your transmittal letter and draft audit report dated July 26, 2021. As requested, this letter constitutes our written response.

We recognize and concur with the four findings in the report and the included recommendations. We look forward to receipt of the final report and to working with the NEA assigned staff as we develop and apply appropriate responses and remedies.

Thanks to Katie Weisner and her team for their hard, precise, and patient work, especially during a global pandemic, which certainly exerted its own challenges.

Best regards,

A handwritten signature in black ink, appearing to be "K. Hanan", written in a cursive style.

Karen J. Hanan
Executive Director, ArtsWA (Washington State Arts Commission)

