

**MEMORANDUM REVIEW REPORT ON THE
NATIONAL INSTITUTE OF FLEXIBLE MANUFACTURING**

Accelerated Grinder Trainer Program

**ARC Grant No.: CO-11485-94-I-302-0204
ARC Contract No.: 94-48
For the Period March 1, 1994 through April 30, 1996**

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Report Number: 96-36(H)

Date: September 30, 1996

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ARC Contract No.: 94-48
For the Period March 1, 1994 through April 30, 1996**

Prepared by:

**Tichenor & Associates
Certified Public Accountants
Woodbridge, Virginia**

**Under Contract Number J-9-G-5-0010 with the
U.S. Department of Labor
Office of the Inspector General
Office of Audit**

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TO: Appalachian Regional Commission (ARC)
Office of Inspector General (OIG)

FROM: Tichenor & Associates
Woodbridge, Virginia

REPORT FOR: The Federal Co-Chairman
ARC Executive Director
OIG Report No. 96-36(H)

SUBJECT TO: Memorandum Review Report on National Institute of Flexible
Manufacturing, Accelerated Grinder Trainer Program, Meadville,
Pennsylvania. Grant No: CO-11485-94-I-302-0204: ARC Contract No.
94-48.

PURPOSE: The purpose of our review was to determine if (a) the total funds claimed for reimbursement by the National Institute of Flexible Manufacturing (NIFM) were expended in accordance with the ARC approved grant budget and did not violate any restrictions imposed by the terms and conditions of the grant; (b) the accounting, reporting and internal control systems provided for disclosure of pertinent financial and operating information; and (c) the objectives of the grant had been met.

BACKGROUND: ARC awarded Grant Number CO-11485-94-I-302-0204, with maximum ARC funding of \$200,000, to NIFM for the period March 1, 1994 through April 30, 1996. ARC required that the ARC grant funding be matched with cash and in-kind of, at least, \$374,723. ARC made one advance payment of \$60,000 and one progress payment of \$106,548 to NIFM. The last payment by ARC was made on November 8, 1995. No final payment had been requested by NIFM as of the date of our review.

The purpose of the grant was to provide financial support to assist Appalachian metal working manufacturers and workers by designing and testing a training program that would accelerate the learning process for entry-level grinding workers. The specific tasks of the grant program were:

- To train a minimum of 35 individuals to the skill-level of a two year experience in grinding over a series of 13-week training periods. (approximately 11 individuals in year 1; and 24 in year 2). Approximately three of these individuals are to be recruited from firms located in the Southern Tier portion of Appalachian New York;
- To train an application engineer as a second grinder trainer;
- To evaluate the effectiveness of the training project from the perspective of firms, workers, service providers, and other project partners. This is to be done in accordance with a written plan submitted to ARC by June 1, 1994, and approved by ARC;
- To conduct a minimum of six seminars for disseminating the results of the demonstration project to other training institutions, business or technical assistance providers, and interested firms throughout the Appalachian Region.

SCOPE: We performed a review of the grant as described in the Purpose section of this report. Our review was based on the terms of the grant agreement and on the application of certain agreed-upon procedures previously discussed with the ARC OIG. We determined if the specific tasks of the grant had been met, if the accountability over ARC funds was sufficient as required by the applicable Office of Management and Budget (OMB) Circulars, and if NIFM had complied with the requirements of the grant agreement. In addition, we discussed the program objectives and performance with NIFM's personnel. Our results and recommendations are based on those procedures.

RESULTS: The following results were based on our review performed at NIFM's offices in Meadville, Pennsylvania:

A. Incurred Costs

NIFM claimed total reimbursable costs from March 1, 1994 through August 31, 1995 of \$166,058 for the grant. We reviewed the costs claimed for reimbursement and determined that, in general the funds had been expended as reported by NIFM. However, we noted several conditions that affect the allowability of some of the claimed costs.

1. Costs Not Incurred

NIFM claimed \$10,874 which was not incurred, and is therefore not reimbursable by ARC or eligible as in-kind costs. NIFM mistakenly claimed an equipment invoice for \$9,638 twice. In addition, NIFM did not credit the equipment expenses for a vendor credit of \$1,236. These costs are unallowable under the grant in accordance with OMB Circular A-122, Attachment A, Paragraph A.1., which states:

"Composition of total costs. The total cost of an award is the sum of the allowable direct and allocable indirect costs less any applicable credits."

We recommend that NIFM implement controls to assure that costs are properly recorded, accumulated and reported.

NIFM's Comments:

NIFM concurred with our finding. NIFM stated that the cost not incurred was the result of an error in recapping the cost incurred. An invoice was listed twice and a credit was not listed. Both of the errors would have been corrected in the final billing as the accounts were reconciled to the ledgers. NIFM stated that the errors have been corrected. ✓

2. Trainee's Labor and Fringe Benefit Costs Not Properly Supported

NIFM claimed in-kind costs through August 31, 1995 of \$293,930 as follows:

Direct Labor	\$ 37,882
Trainee Wages	70,200
Fringe Benefits (Trainees and teachers)	44,412
Other Direct Costs	119,708
Overhead	<u>21,728</u>
TOTAL	<u>\$293,930</u>

NIFM provided a hand written memo with the following calculation to support the number of trainees, the hours attended, the in-kind wages and the in-kind fringe benefits:

Class	Trainees	Dollars	Hours
1	4	\$ 24,000	2,080
2	5	30,000	2,600
3	5	30,000	2,600
4	4	24,000	2,080
			9,360
Hourly Rate			\$ 7.50
Total Wages			\$ 70,200
Fringe Rate			30%
Total Fringes			\$ 21,060

Trainee's Labor:

Trainee's labor costs should be supported by attendance records such as sign-in sheets or employer timesheets indicating the person attending the class and the number of hours attended. The class hours should then be multiplied by the trainee's hourly labor rate in order to determine the value of the in-kind labor. As discussed in the Internal Control section below, these records are required in accordance with the applicable OMB Circulars.

NIFM's Comments:

NIFM indicated trainees were employed by various companies and thus were subject to their own firm's timekeeping requirements and wage and benefits structure. NIFM felt due to the sensitivity of wage information, it would not be feasible to record each trainee's actual pay rate. NIFM also stated the time involved in the classes usually exceeded what had been reported.

Trainee's Fringe Benefits

NIFM claimed both the trainee's fringe benefits, as shown in the above trainee's table, and the teacher's fringe benefits as in-kind costs by applying a 30 percent rate to wages and a constant rate to teacher's wages. There was, however, no support for the 30 percent fringe benefit rate used.

NIFM's Comments:

NIFM felt due to the sensitivity of wage and benefit information divulged from competing firms, an industry average of 30% would be adequate.

Additional Comments:

We do not disagree that the training program was performed. However, NIFM as the grantee is responsible for keeping adequate supporting documentation as required by the OMB Circulars. The submission of an application with budgeted or projected costs is not considered adequate. Also, the provision of wage and fringe benefit information from the various companies to NIFM does not need to be shared with the trainee's, but must be recorded by NIFM's management.

3. Administrative Staff Labor and Fringe Benefit Costs Not Properly Calculated

The remaining in-kind costs were for the wages and benefits for the president and the administrative staff. We traced the reported hours to timesheets or time estimates, determined the actual rates of pay for each employee, and recalculated the wages and actual fringe benefits. We determined that NIFM had overstated the in-kind costs for the president and administrative staff by \$1,430. The difference between NIFM's claimed amount of \$21,728 and our recalculated amount of \$20,298 was due to NIFM's use of estimated hours and an estimated fringe benefit rate.

Although it appears that the estimates made by NIFM in claiming trainee's labor and fringe benefit costs, as well as its estimates used to claim administrative wages and fringe benefits appears reasonable, the lack of supporting accounting records could result in:

- The recovery of costs not incurred by NIFM or the trainee's employers.
- The recovery of the same costs under one or more other grants or programs.
- The use of the same costs as match on one or more other grants or programs.

We recommend that NIFM review the requirements of OMB A-110, Attachment E and implement procedures to assure all in-kind costs are properly documented and supported.

NIFM's Comments:

NIFM stated that it is possible that the interim audit would reflect a discrepancy as they expected to exceed the budgeted amount by the end of the project and made only a reasonable effort to assure accuracy knowing that they would reconcile their accounts at the time of final billing. They also stated that NIFM has no other grants or programs that would enable them to recover the same costs or use as match. ✓

B. Internal Controls

In addition to the internal control weaknesses which resulted in the questioned costs above, we identified several other internal control weaknesses with respect to the accounting system and its ability to properly accumulate and report pertinent financial and operating information.

1. Timekeeping

Timesheets are not required to be completed and submitted by all personnel. Timesheets were prepared by only one part-time teacher and some administrative staff. Full-time teachers, other administrative staff and the president are not required to prepare and submit timesheets to support labor hours worked. These teacher's labor hours and costs were charged directly, in full, to the ARC grant program. The president's labor costs were allocated to the ARC grant based on quarterly estimates, and claimed as in-kind labor. The amount of the President's salary charged to ARC in-kind was \$11,102.

Our review of the part-time teacher's timesheets also indicated several internal control weaknesses.

- Each timesheet did not have the signature of the employee or the approval of a supervisor;
- The part-time teacher was not required to prepare and submit timesheets for two months, July and August, 1995. The president of NIFM estimated the number of hours for these months and calculated personnel costs based on the estimate.

Timesheets should be completed and maintained for all personnel to support that labor hours were allocable to the program being charged and that personnel costs are accurately based on work performed. Such records are required in accordance with OMB A-110, Attachment F, Paragraph 2.f. and 2.g., which states:

"Recipient's financial management systems shall provide for:...f. Procedures for determining the reasonableness, allowability and allocability of costs...g. Accounting records that are supported by source documentation."

In addition, in-kind labor costs must be supported by timesheets to satisfy the documentation criteria established in OMB A-110, Attachment E, Paragraph 3.b., which states, in part:

"All contributions, both cash and in-kind, shall be accepted as part of the recipients' cost sharing and matching when such contributions meet all of the following criteria:

- (1) Are verifiable from the recipient's records;
- (2) Are not included as contributions for other federally-assisted program;
- (3) Are necessary and reasonable for proper and efficient accomplishment of project objectives;..."

NIFM's Comments:

NIFM stated that all employees are salaried and are not required to clock in or out or to make out timesheets. They stated that full-time instructors do not complete timesheets, the part-time applications engineer prepares a timesheet for the estimated hours he worked on the project, the president's time is based on a fair and conservative estimate and that all administrative staff reported the actual time utilized when performing duties related to the project. NIFM concluded that this reporting is reasonable and fair to the program.

Additional Comments:

Based on the sample tested, we determined that not all administrative staff and that part-time teachers for the period indicated did not maintain timesheets. Our finding and recommendation are to aid NIFM in strengthening its system and to avoid unallowable costs on future government contracts.

2. Fringe Benefits

NIFM claimed fringe benefits for teachers, administrative staff and trainees as in-kind costs. In determining fringe benefits expenses for NIFM personnel, NIFM calculated a fringe benefit rate for each person using an estimated annual salary and actual fringe benefit component rates applied to that salary. NIFM's calculated fringe benefits included:

Benefit	Amount
Worker's Comp	\$1.09/\$100
FICA	6.65%
State Unemployment	2.5767%
Pension	5%
Health & Life Insurance	Actual Cost

We noted that the base used to calculate the fringe benefit costs was incorrect for three of the seven NIFM employees. The base salary used to calculate the fringe benefit rate for the president, one administrative person, and one teacher were overstated. In addition, NIFM did not recalculate the individual fringe benefit rates to take into consideration salary increases during the grant's period of performance, which would reduce the effective fringe benefit rate.

Fringe benefit costs must be based on actual costs in accordance with OMB Circular A-122, Attachment A, Paragraph A.1.. In addition, OMB A-122, Attachment B, Paragraph 6.f.(2), states, in part:

"Fringe benefits in the form of employer contributions or expenses for social security, employee insurance, workmen's compensation insurance, pension plan costs...are allowable provided such benefits are granted in accordance with established written organization policies. Such benefits whether treated as indirect costs or as direct costs, shall be distributed to particular awards and other activities in a manner consistent with the pattern of benefits accruing to the individuals..."

NIFM's Comments:

NIFM stated that the base salaries used for interim invoicing was the rate being paid at the time of billing. They stated that the final invoicing reflects the actual wages and benefits paid each individual involved in the program. ✓

Additional Comments:

Based on our review of the personnel files, the invoicing did not reflect actual wages and benefits paid each individual in the program.

3. Segregation of Duties

The independent public accountant (IPA) who conducted the Single Audit of NIFM for the fiscal year ended June 30, 1995 reported in the "Single Audit Report on the Internal Control Structure used in Administering Federal Awards" that there are not sufficient accounting employees at NIFM to permit an adequate segregation of duties. We concur with the IPA's conclusion. However, we also concurred that the costs to improve the system would not outweigh the benefits.

We noted that NIFM does not have written accounting policies and procedures to assure that costs are properly and consistently recorded. We recommend that NIFM develop, document and implement accounting policies and procedures which will address the internal control weaknesses discussed, as well as assure the proper accumulation and reporting of all other costs.

NIFM's Comments:

NIFM indicated it relies on the independent audit to ensure compliance with generally accepted accounting practices. They also indicated their utilization of a standard computer accounting software.

Additional Comments:

We saw no evidence of an automated system in place during our on-site visit. However, NIFM had mentioned its desire to automate its accounting functions.

C. Compliance and Program Results

NIFM has substantially accomplished the specific tasks required by the grant agreement. However, NIFM did not recruit any individuals from the Southern Tier portion of Appalachian New York. NIFM has contacted the Jamestown Community College in Jamestown, New York in an attempt to recruit individuals from the Southern Tier region, but has been unsuccessful in attracting any participants.

NIFM's Comments:

NIFM is still meeting with agencies from Chautauqua County, New York and are hopeful in attracting participants from that region.

RECOMMENDATIONS: We recommend that NIFM calculate and claim fringe benefits based on actual salaries, and adjust the fringe benefit rates to reflect salary increases. We also recommend NIFM adjust its final financial status report to delete the costs which are not reimbursable under the grant including costs which were not incurred or claimed in error and costs based on estimates which are not supported by adequate accounting documentation. In addition, we recommend NIFM establish written accounting policies and procedures, including timekeeping and attendance procedures. Lastly, we recommend ARC make a final determination on NIFM's compliance to the grants matching requirements.

Tichenor & Associates
TICHENOR & ASSOCIATES
Woodbridge, Virginia
April 17, 1996



Hubert N. Sparks, Inspector General
APPALACHIAN REGIONAL COMMISSION
1666 Connecticut Avenue, N. W.
Washington, DC 20235

Re: OIG Report 96-36 (H), ARC Contract 94-48
Grant CO-11485

Dear Mr. Sparks:

I apologize for taking so much time to reply to the draft copy of Tichenor & Associates audit report. It seems as if this is the time of the year that everything is due and as you know from the audit we are very limited on staff.

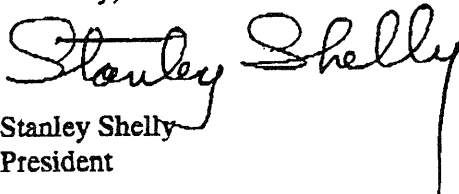
In reviewing our comments to the auditors report we ask that you consider:

1. That we are a small company with a limited, overworked staff.
2. That this is the first government contract that we have had.
3. That we were unaware that an In-Process Audit might be performed and relied on our Independent Certified Audit to pick up any discrepancies.
4. That we knew that our cash and in-kind match requirement of \$374,723 would be exceed by a large amount of dollars. The amount of cash and in-kind calculated by NIFM for the contract period is \$483,156, which is \$108,433 or 28.9% more than required.
5. That we have met or exceeded all performance provisions of the contract with the exception of training 3 individuals recruited from firms located in the Southern Tier portion of Appalachian New York. We are still having conversation with them and there is a good possibility that this will still happen.

For convenience of reading, I will repeat each of the auditors findings and state our comments directly below.

Please do not hesitate to call me if further clarification is required. My phone number is 814-333-2415.

Sincerely,


Stanley Shelly
President

Enclosure



To: Appalachian Regional Commission (ARC)
Office of Inspector General (OIG)

From: The National Institute of Flexible Manufacturing (NIFM)

Subject: NIFM's Comments to Tichenor & Associates Draft Report on the
Accelerated Grinder Training Program in Meadville, Pennsylvania
Grant No. CO-11485-94-I302-0204
ARC Contract No. 94-48

TICHENOR & ASSOCIATES REPORT AND NIFM'S COMMENTS:

Item A. Incurred Costs

NIFM claimed total reimbursable costs from March 1, 1994 through August 31, 1995 of \$166,058 for the grant. We reviewed the costs claimed for reimbursement and determined that in general the funds had been expended as reported by NIFM. However, we noted several conditions that effect the allowability of some of the claimed costs.

1. **Costs Not Incurred**

NIFM claimed \$10,874 which was not incurred, and is therefore not reimbursable by ARC or eligible as in-kind costs. NIFM mistakenly claimed an equipment invoice for \$9,638 twice. These costs are unallowable under the grant in accordance with OMB Circular A-122, Attachment A, Paragraph A.1., which states:

"Composition of total costs. The total cost of an award is the sum of the allowable direct and allocable indirect costs less any applicable credits."

We recommend that NIFM implement controls to assure that costs are properly recorded, accumulated and reported.

NIFM Comments: The above "cost not incurred" was the result of an error in recapping the cost incurred. An invoice was listed twice and a credit was not listed. Both of these errors would have been corrected in our final billing as our accounts were reconciled to our ledgers. Also our outside auditors would have caught the errors in their annual certified audit.

Obviously, the errors have been corrected.

2. Trainee's Labor and Fringe Benefits Costs not Properly Supported

NIFM claimed in-kind costs through August 31, 1995 of \$293,930 as follows:

Direct Labor	\$37,882
Trainee Wages	70,200
Fringe Benefits (Trainees and teachers)	44,412
Other Direct Costs	119,708
Overhead	<u>21,728</u>
TOTAL	\$293,950

NIFM provided a hand written memo with the following calculation to support the number of trainees, the hours attended, the in-kind wages and the in-kind fringe benefits:

<u>Class</u>	<u>Trainees</u>	<u>Dollars</u>	<u>Hours</u>
1	4	\$ 24,000	2,080
2	5	30,000	2,600
3	5	30,000	2,600
4	4	24,000	<u>2,080</u>
			9,360
Hourly Rate		\$	<u>7.50</u>
Total Wages		\$	70,200
Fringe Rate			30%
Total Fringes		\$	21,060

Trainee's Labor:

Trainee's labor costs should be supported by attendance records such as sign-in sheets or employer timesheets indicating the person attending the class and the number of hours attended. The class hours should then be multiplied by the trainee's hourly labor rate in order to determine the value of the in-kind labor. As discussed in the Internal Control section below, these records are required in accordance with the applicable OMB Circulars.

NIFM Comments: The trainees involved are some company's employees and as such are subject to their rules of timekeeping. Our rule is that the trainee can miss only 3 days out of the 65 days of training, and the projects missed must be made up.

Additionally, trainees often stay after hours to perfect their methods and none of these hours are reflected in the total hours of training. The \$7.50 per hour rate came from a sampling of the industry and was used in compiling our application to the ARC and we have consistently used this rate. Because we are training employees of several different companies at one time there is great reluctance for them to reveal the wages and benefits being paid for fear of losing their employee -- so wage rates are not given to us nor are they normally requested.

It should be noted that each class in this program required from 3 days to 8 days of additional training to complete their projects --- none of this additional time is reflected in any of the reports. We consider the training to be complete when the projects are complete not when the calendar tells us that the 65 days has elapsed.

Trainee's Fringe Benefits

NIFM claimed both the trainee's fringe benefits, as shown in the above trainee's table and the teacher's fringe benefits as in-kind costs by applying a 30 percent rate to wages and a constant rate to teacher's wages. There was, however, no support for the 30 percent fringe benefit rate used.

NIFM Comments: The 30% fringe benefit rate is again the reflection of the industry and was used in preparing our application to the ARC for funding and we have consistently used this rate for billing purposes. The trainees companies are reluctant to divulge the actual benefits because they may lose their employee or their competitive advantage.

3. Administrative Staff Labor and Fringe Benefits Costs Not Properly Calculated:

The remaining in-kind costs were for wages and benefits for the president and the administrative staff. We traced the reported hours to timesheets or time estimates, determined the actual rates of pay for each employee, and recalculated the wages and actual fringe benefits. We determine that NIFM had overstated the in-kind costs for the president and administrative staff by \$1,430. The difference between NIFM's claimed amount of \$21,728 and our recalculated amount of \$20,298 was due to NIFM's use of estimated hours and an estimated fringe benefit rate.

Although it appears that the estimates made by NIFM in claiming trainee's labor and fringe benefit costs, as well as its estimates used to claim administrative wages and fringe benefits appears reasonable, the lack of supporting accounting records could result in:

- * The recovery of costs not incurred by NIFM or the trainee's employers.

- * The recovery of the same costs under one or more other grants or programs.
- * The use of the same costs as match on one or more other grants or programs.

We recommend that NIFM review the requirements of OMB A-110, Attachment E and implement procedures to assure all in-kind costs are properly documented and supported.

NIFM Comments: It is very possible that the interim audit would reflect a discrepancy as we expected to exceed the budgeted amount by the end of the project and made only a reasonable effort to assure accuracy knowing that we would reconcile our accounts at the time of final billing. Also our Independent Certified Audit would disclose any errors.

NIFM has no other grants or programs that would enable us to "recover the same costs or use as match" against them.

Item B. Internal Controls

In addition to the internal control weaknesses which resulted in the questioned costs above, we identified several other control weaknesses with respect to the accounting system and its ability to properly accumulate and report pertinent financial and operating information.

1. Timekeeping

Timesheets are required to be completed and submitted by all personnel. Timesheets were prepared by only one part-time teacher and some administrative staff. Full-time teachers, other administrative staff and the president are not required to prepare and submit timesheets to support labor hours worked. These teacher's labor hours and costs were allocated to the ARC grant based on quarterly estimates, and claimed as in-kind labor. The amount of the President's salary charged to ARC in-kind was \$11,102.

Our review of the part-time teacher's timesheets also indicated several internal control weaknesses.

- * Each timesheet did not have the signature of employee or the approval of a supervisor.
- * The part-time teacher was not required to prepare and submit timesheets for two months, July and August, 1995. The president of NIFM estimated the number of hours for these months and calculated personnel costs based on the estimate.

Timesheets should be completed and maintained for all personnel to support that labor hours were allocable to the program being charged and that personnel costs are accurately based on work performed. Such records required in accordance with OMB A-110, Attachment F, Paragraph 2.f. and 2.g., which states:

“Recipient’s financial management systems shall provide for :....f. Procedures for determining the reasonableness, allowability and allocability of costs...g. Accounting records that are supported by source documentation.”

In addition, in-kind labor costs must be supported by timesheets to satisfy the documentation criteria established in OMB A-110, Attachment E, Paragraph 3.b., which states, in part:

“All contributions, both cash and in-kind, shall be accepted as part of the recipients’ cost sharing and matching when such contributions meet all of the following criteria:

- (1). Are verifiable from the recipient’s records;
- (2). Are not included as contributions for other federally-assisted program;
- (3). Are necessary and reasonable for proper and efficient accomplishment of project objectives;...”

NIFM Comments: All employees at NIFM are salaried employees and are not required to clock in or out or to make out timesheets. They are required to do-the-job and their jobs are specific, i.e. the full time instructors solicit, interview, train and follow the progress of the trainees. They also maintain/repair equipment and order parts and supplies needed for the program. The part time applications engineer is required to lend assistance to the instructor in any of the above endeavors as requested and thus turned in a timesheet for the estimated hours he assisted.

The President’s time was based on what I did for the program and I believe it to be a fair and conservative estimate.

The administrative staff reported the actual time utilized when performing duties related to this program.

In summary to the time keeping question:

1. Full-time instructors did not turn in a timesheet. Their full time was charged to the program.
2. Part-time teacher/applications engineer did turn in weekly time sheets
3. The President turned in quarterly time sheets based on what he did

4. **The administrative staff turned in time sheets for everything they did. I believe the above reporting to be reasonable and fair to the program.**

2. Fringe Benefits

NIFM claimed fringe benefits for teachers, administrative staff and trainees as in-kind costs. In determining fringe benefits expenses for NIFM personnel, NIFM calculated a fringe benefit rate for each person using an estimated annual salary and actual fringe benefit component rates applied to that salary. NIFM's calculated fringe benefits included:

<u>Benefit</u>	<u>Amount</u>
Worker's Comp.	\$1.09/\$100
FICA	6.65%
State Unemployment	2.5767%
Pension	5%
Health & Life Insurance	Actual Cost

We noted that the base used to calculate the fringe benefit costs was incorrect for three of the seven NIFM employees. The base salary used to calculate the fringe benefit rate for the president, one administrative person, and one teacher were overstated. In addition, NIFM did not recalculate the individual fringe benefit rates to take into consideration salary increases during the grant's period of performance, which would reduce the effective fringe benefit rate.

Fringe benefit costs must be based on actual costs in accordance with OMB Circular A-122, Attachment A, Paragraph A.1.. In addition, OMB A-122, Attachment B, Paragraph 6.f.(2), states in part:

"Fringe benefits in the form of employer contributions or expenses for social security, employee insurance, workmen's compensation insurance, pension plan costs...are allowable provided such benefits are granted in accordance with established written organization policies. Such benefits whether treated as indirect costs or as direct costs, shall be distributed to particular awards and other activities in a manner consistent with the pattern of benefits accruing to the individuals..."

NIFM Comments: The base salaries used for interim invoicing was the rate being paid at the time of billing. However, the final invoicing reflects the actual wages and benefits paid each individual involved in the program.

3. Segregation of Duties

The independent public accountant (IPA) who conducted the Single Audit of NIFM for the fiscal year ended June 30, 1995 reported in the "Single Audit Report on the Internal Control Structure used in Administering Federal Awards" that there are not sufficient accounting employees at NIFM to permit adequate segregation of duties. We concur the IPA's conclusion. However, we also concurred that the costs to improve the system would not outweigh the benefits.

We noted that NIFM does not have written accounting policies and procedures to assure that costs are properly and consistently recorded. We recommend that NIFM develop, document and implement accounting policies and procedures which will address the internal control weaknesses discussed, as well as assure the proper accumulation and reporting of all other costs.

NIFM Comments: Being a 501 (C)(3) Not-for-Profit Corporation and always being short on operating capital we have as many like corporations chosen to depend on the annual Independent Certified Audit to keep us from straying from generally accepted accounting practices. Also in addition to my being an accountant involved in the manufacturing field for nearly 40 years; we utilize a standard computer accounting software program.

Item C. Compliance and Program Results

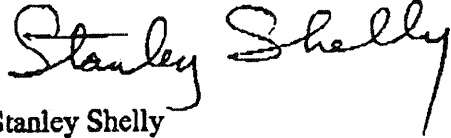
NIFM has substantially accomplished the specific tasks required by the grant agreement. However, NIFM did not recruit any individuals from the Southern Tier portion of Appalachian New York. NIFM has contacted the Jamestown Community College in Jamestown, New York in an attempt to recruit individuals from the Southern Tier region, but has been unsuccessful in attracting any participants.

NIFM Comments: We have been unsuccessful in attracting trainees from the Southern Tier Region thus far. But we are still hopeful and periodically have met with agencies from Chautauqua County, New York and we will eventually have participants from the Southern Tier. There is a very good possibility that Chautauqua County may find funding to establish their own "Teaching Factory" based on what they have learned in conversations with NIFM.

CONCLUSIONS:

In conclusion to our comments I feel that NIFM has been fair and reasonable in complying with the terms and the spirit of the contract. And, as such we respectfully request that your final determination is that NIFM is in compliance to the grants matching requirements.

Sincerely,

A handwritten signature in cursive script that reads "Stanley Shelly". The signature is written in black ink and is positioned above the typed name and title.

Stanley Shelly
President



October 16, 1996

MEMORANDUM FOR THE FEDERAL CO-CHAIRMAN

SUBJECT: OIG Reports 96-31(H), 96-36(H), and 96-37(H); Northern Tier Planning and Development Commission, National Institute of Flexible Manufacturing, and Southwestern Pennsylvania Regional Development Council

Enclosed is a copy of reports dealing with grants to three Pennsylvania organizations. Issues noted in the reports deal with consistent application of costs, division of costs among benefitting programs, sufficiency and documentation of match, costs incurred under prior programs or not incurred, and eligibility of costs to organizations whose mission includes lobbying activities.

In most cases, the issues and recommendations can be resolved between ARC and the grantee in accordance with applicable regulations. However, for several issues, it appears there is a need for ARC review of the reports and grantee responses to determine the need for action or clarifying guidance.

Report 96-31(H), Northern Tier Planning and Development Commission, questions a portion of the grantee's 1995 membership dues to the Economic Planning and Development Council of Pennsylvania (EPDC). The report notes the grantee concurred that this cost was generally charged to unrestricted sources rather than project costs and considered this claim to be an isolated error.

Draft report 96-37(H), Southwestern Pennsylvania Regional Development Council had included a questioned travel cost related to travel to a meeting of the EPDC. The grantee response to the draft report noted that EPDC is permitted to do a wide variety of not-for-profit activities including lobbying; and thus, the related costs should be considered eligible. We removed the specific questioned cost from the final report pending ARC review of this issue.

Contact with a third Pennsylvania LDD disclosed that EPDC dues were also paid out of unrestricted funds. It is possible LDDs were previously informed that membership dues were not eligible as a direct grant cost. Also, there appears to be a difference between the eligibility of dues to an organization that engages in lobbying activities and travel costs for a program related function sponsored by that agency.


ARC should determine if costs incurred for participation in EPDC activities are eligible for reimbursement in whole or in part. Although we did not pursue this issue to determine the primary EPDC activities nor the applicability of current lobbying related statutes, it appears there is some difference among grantees about the treatment of costs for EPDC activities.

Report 96-31(H), Northern Tier Planning and Development Commission, questions the treatment of some costs as direct charges to ARC rather than indirect charges allocable to all benefitting programs, including JTPA. The grantee disagreed and noted that ARC administrative grants are intended to support the administrative activities of the LDD; and thus, the expenses (computer software, typewriter, and training) are allowable under the ARC grant.

We recognize the overall purpose of LDD administrative grants but believe various activities and expenditures that benefit all programs should be treated as indirect costs. However, we believe the issue merits ARC review.

Report 96-31(H) also questions the extent of \$30,000 in matching costs related to a grant from the Pennsylvania Department of Transportation. The report indicates this grant was not received; and therefore, the required match was not provided. The grantee response to the matching cost issue notes that the state grant was received. However, in response to the report conclusion that some studies were not performed, the grantee responded that the five special transportation studies were not conducted due to a lack of funding from the Pennsylvania Department of Transportation. Followup on the status and applicability of this grant is needed.

The above issues and the other recommendations noted in the reports should be resolved between the grantee and ARC program staff. We will followup within 60 days to determine the status of actions.


Hubert N. Sparks
Inspector General

Enclosures



A Shared Use Teaching Factory

(814) 333-2415 FAX (814) 337-8172

Hubert N. Sparks, Inspector General
APPALACHIAN REGIONAL COMMISSION
1666 Connecticut Avenue, N. W.
Washington, DC 20235

Re: OIG Report 96-36 (H), ARC Contract 94-48
Grant CO-11485

Dear Mr. Sparks:

I apologize for taking so much time to reply to the draft copy of Tichenor & Associates audit report. It seems as if this is the time of the year that everything is due and as you know from the audit we are very limited on staff.

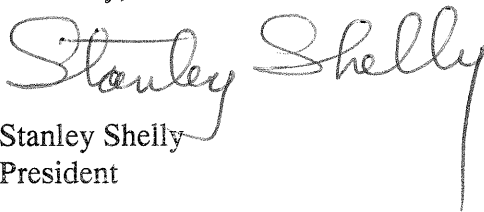
In reviewing our comments to the auditors report we ask that you consider:

1. That we are a small company with a limited, overworked staff.
2. That this is the first government contract that we have had.
3. That we were unaware that an In-Process Audit might be performed and relied on our Independent Certified Audit to pick up any discrepancies.
4. That we knew that our cash and in-kind match requirement of \$374,723 would be exceed by a large amount of dollars. The amount of cash and in-kind calculated by NIFM for the contract period is \$483,156, which is \$108,433 or 28.9% more than required.
5. That we have met or exceeded all performance provisions of the contract with the exception of training 3 individuals recruited from firms located in the Southern Tier portion of Appalachian New York. We are still having conversation with them and there is a good possibilityt that this will still happen.

For convenience of reading, I will repeat each of the auditors findings and state our comments directly below.

Please do not hesitate to call me if further clarification is required. My phone number is 814-333-2415.

Sincerely,



Stanley Shelly
President

Enclosure



To: Appalachian Regional Commission (ARC)
Office of Inspector General (OIG)

From: The National Institute of *Flexible* Manufacturing (NIFM)

Subject: NIFM's Comments to Tichenor & Associates Draft Report on the
Accelerated Grinder Training Program in Meadville, Pennsylvania
Grant No. CO-11485-94-I302-0204
ARC Contract No. 94-48

TICHENOR & ASSOCIATES REPORT AND NIFM'S COMMENTS:

Item A. Incurred Costs

NIFM claimed total reimbursable costs from March 1, 1994 through August 31, 1995 of \$166,058 for the grant. We reviewed the costs claimed for reimbursement and determined that in general the funds had been expended as reported by NIFM. However, we noted several conditions that effect the allowability of some of the claimed costs.

1. Costs Not Incurred

NIFM claimed \$10,874 which was not incurred, and is therefore not reimbursable by ARC or eligible as in-kind costs. NIFM mistakenly claimed an equipment invoice for \$9,638 twice. These costs are unallowable under the grant in accordance with OMB Circular A-122, Attachment A, Paragraph A.1., which states:

"Composition of total costs. The total cost of an award is the sum of the allowable direct and allocable indirect costs less any applicable credits."

We recommend that NIFM implement controls to assure that costs are properly recorded, accumulated and reported.

NIFM Comments: The above "cost not incurred" was the result of an error in recapping the cost incurred. An invoice was listed twice and a credit was not listed. Both of these errors would have been corrected in our final billing as our accounts were reconciled to our ledgers. Also our outside auditors would have caught the errors in their annual certified audit.

Obviously, the errors have been corrected.

2. Trainee's Labor and Fringe Benefits Costs not Properly Supported

NIFM claimed in-kind costs through August 31, 1995 of \$293,930 as follows:

Direct Labor	\$37,882
Trainee Wages	70,200
Fringe Benefits (Trainees and teachers)	44,412
Other Direct Costs	119,708
Overhead	<u>21,728</u>
TOTAL	\$293,950

NIFM provided a hand written memo with the following calculation to support the number of trainees, the hours attended, the in-kind wages and the in-kind fringe benefits:

<u>Class</u>	<u>Trainees</u>	<u>Dollars</u>	<u>Hours</u>
1	4	\$ 24,000	2,080
2	5	30,000	2,600
3	5	30,000	2,600
4	4	24,000	<u>2,080</u>
			9,360
Hourly Rate		\$	<u>7.50</u>
Total Wages		\$	70,200
Fringe Rate			30%
Total Fringes		\$	21,060

Trainee's Labor:

Trainee's labor costs should be supported by attendance records such as sign-in sheets or employer timesheets indicating the person attending the class and the number of hours attended. The class hours should then be multiplied by the trainee's hourly labor rate in order to determine the value of the in-kind labor. As discussed in the Internal Control section below, these records are required in accordance with the applicable OMB Circulars.

NIFM Comments: The trainees involved are some company's employees and as such are subject to their rules of timekeeping. Our rule is that the trainee can miss only 3 days out of the 65 days of training, and the projects missed must be made up.

Additionally, trainees often stay after hours to perfect their methods and none of these hours are reflected in the total hours of training. The \$7.50 per hour rate came from a sampling of the industry and was used in compiling our application to the ARC and we have consistently used this rate. Because we are training employees of several different companies at one time there is great reluctance for them to reveal the wages and benefits being paid for fear of losing their employee -- so wage rates are not given to us nor are they normally requested.

It should be noted that each class in this program required from 3 days to 8 days of additional training to complete their projects --- none of this additional time is reflected in any of the reports. We consider the training to be complete when the projects are complete not when the calendar tells us that the 65 days has elapsed.

Trainee's Fringe Benefits

NIFM claimed both the trainee's fringe benefits, as shown in the above trainee's table and the teacher's fringe benefits as in-kind costs by applying a 30 percent rate to wages and a constant rate to teacher's wages. There was, however, no support for the 30 percent fringe benefit rate used.

NIFM Comments: The 30% fringe benefit rate is again the reflection of the industry and was used in preparing our application to the ARC for funding and we have consistently used this rate for billing purposes. The trainees companies are reluctant to divulge the actual benefits because they may lose their employee or their competitive advantage.

3. Administrative Staff Labor and Fringe Benefits Costs Not Properly Calculated:

The remaining in-kind costs were for wages and benefits for the president and the administrative staff. We traced the reported hours to timesheets or time estimates, determined the actual rates of pay for each employee, and recalculated the wages and actual fringe benefits. We determine that NIFM had overstated the in-kind costs for the president and administrative staff by \$1,430. The difference between NIFM's claimed amount of \$21,728 and our recalculated amount of \$20,298 was due to NIFM's use of estimated hours and an estimated fringe benefit rate.

Although it appears that the estimates made by NIFM in claiming trainee's labor and fringe benefit costs, as well as its estimates used to claim administrative wages and fringe benefits appears reasonable, the lack of supporting accounting records could result in:

- * The recovery of costs not incurred by NIFM or the trainee's employers.

- * The recovery of the same costs under one or more other grants or programs.
- * The use of the same costs as match on one or more other grants or programs.

We recommend that NIFM review the requirements of OMB A-110, Attachment E and implement procedures to assure all in-kind costs are properly documented and supported.

NIFM Comments: It is very possible that the interim audit would reflect a discrepancy as we expected to exceed the budgeted amount by the end of the project and made only a reasonable effort to assure accuracy knowing that we would reconcile our accounts at the time of final billing. Also our Independent Certified Audit would disclose any errors.

NIFM has no other grants or programs that would enable us to "recover the same costs or use as match" against them.

Item B. Internal Controls

In addition to the internal control weaknesses which resulted in the questioned costs above, we identified several other control weaknesses with respect to the accounting system and its ability to properly accumulate and report pertinent financial and operating information.

1. Timekeeping

Timesheets are required to be completed and submitted by all personnel. Timesheets were prepared by only one part-time teacher and some administrative staff. Full-time teachers, other administrative staff and the president are not required to prepare and submit timesheets to support labor hours worked. These teacher's labor hours and costs were allocated to the ARC grant based on quarterly estimates, and claimed as in-kind labor. The amount of the President's salary charged to ARC in-kind was \$11,102.

Our review of the part-time teacher's timesheets also indicated several internal control weaknesses.

- * Each timesheet did not have the signature of employee or the approval of a supervisor.
- * The part-time teacher was not required to prepare and submit timesheets for two months, July and August, 1995. The president of NIFM estimated the number of hours for these months and calculated personnel costs based on the estimate.

Timesheets should be completed and maintained for all personnel to support that labor hours were allocable to the program being charged and that personnel costs are accurately based on work performed. Such records required in accordance with OMB A-110, Attachment F, Paragraph 2.f. and 2.g., which states:

“Recipient’s financial management systems shall provide for :....f. Procedures for determining the reasonableness, allowability and allocability of coats...g. Accounting records that are supported by source documentation.”

In addition, in-kind labor costs must be supported by timesheets to satisfy the documentation criteria established in OMB A-110, Attachment E, Paragraph 3.b., which states, in part:

“All contributions, both cash and in-kind, shall be accepted as part of the recipients’ cost sharing and matching when such contributions meet all of the following criteria:

- (1). Are verifiable from the recipient’s records;
- (2). Are not included as contributions for other federally-assisted program;
- (3). Are necessary and reasonable for proper and efficient accomplishment of project objectives;...”

NIFM Comments: All employees at NIFM are salaried employees and are not required to clock in or out or to make out timesheets. They are required to do-the-job and their jobs are specific, i.e. the full time instructors solicit, interview, train and follow the progress of the trainees. They also maintain/repair equipment and order parts and supplies needed for the program. The part time applications engineer is required to lend assistance to the instructor in any of the above endeavors as requested and thus turned in a timesheet for the estimated hours he assisted.

The President’s time was based on what I did for the program and I believe it to be a fair and conservative estimate.

The administrative staff reported the actual time utilized when performing duties related to this program.

In summary to the time keeping question:

- 1. Full-time instructors did not turn in a timesheet. Their full time was charged to the program.**
- 2. Part-time teacher/applications engineer did turn in weekly time sheets**
- 3. The President turned in quarterly time sheets based on what he did**

4. **The administrative staff turned in time sheets for everything they did. I believe the above reporting to be reasonable and fair to the program.**

2. Fringe Benefits

NIFM claimed fringe benefits for teachers, administrative staff and trainees as in-kind costs. In determining fringe benefits expenses for NIFM personnel, NIFM calculated a fringe benefit rate for each person using an estimated annual salary and actual fringe benefit component rates applied to that salary. NIFM's calculated fringe benefits included:

<u>Benefit</u>	<u>Amount</u>
Worker's Comp.	\$1.09/\$100
FICA	6.65%
State Unemployment	2.5767%
Pension	5%
Health & Life Insurance	Actual Cost

We noted that the base used to calculate the fringe benefit costs was incorrect for three of the seven NIFM employees. The base salary used to calculate the fringe benefit rate for the president, one administrative person, and one teacher were overstated. In addition, NIFM did not recalculate the individual fringe benefit rates to take into consideration salary increases during the grant's period of performance, which would reduce the effective fringe benefit rate.

Fringe benefit costs must be based on actual costs in accordance with OMB Circular A-122, Attachment A, Paragraph A.1.. In addition, OMB A-122, Attachment B, Paragraph 6.f.(2), states in part:

“Fringe benefits in the form of employer contributions or expenses for social security, employee insurance, workmen's compensation insurance, pension plan costs...are allowable provided such benefits are granted in accordance with established written organization policies. Such benefits whether treated as indirect costs or as direct costs, shall be distributed to particular awards and other activities in a manner consistent with the pattern of benefits accruing to the individuals...”

NIFM Comments: The base salaries used for interim invoicing was the rate being paid at the time of billing. However, the final invoicing reflects the actual wages and benefits paid each individual involved in the program.

3. Segregation of Duties

The independent public accountant (IPA) who conducted the Single Audit of NIFM for the fiscal year ended June 30, 1995 reported in the "Single Audit Report on the Internal Control Structure used in Administering Federal Awards" that there are not sufficient accounting employees at NIFM to permit adequate segregation of duties. We concur the IPA's conclusion. However, we also concurred that the costs to improve the system would not outweigh the benefits.

We noted that NIFM does not have written accounting policies and procedures to assure that costs are properly and consistently recorded. We recommend that NIFM develop, document and implement accounting policies and procedures which will address the internal control weaknesses discussed, as well as assure the proper accumulation and reporting of all other costs.

NIFM Comments: Being a 501 (C)(3) Not-for-Profit Corporation and always being short on operating capital we have as many like corporations chosen to depend on the annual Independent Certified Audit to keep us from straying from generally accepted accounting practices. Also in addition to my being an accountant involved in the manufacturing field for nearly 40 years; we utilize a standard computer accounting software program.

Item C. Compliance and Program Results

NIFM has substantially accomplished the specific tasks required by the grant agreement. However, NIFM did not recruit any individuals from the Southern Tier portion of Appalachian New York. NIFM has contacted the Jamestown Community College in Jamestown, New York in an attempt to recruit individuals from the Southern Tier region, but has been unsuccessful in attracting any participants.

NIFM Comments: We have been unsuccessful in attracting trainees from the Southern Tier Region thus far. But we are still hopeful and periodically have met with agencies from Chautauqua County, New York and we will eventually have participants from the Southern Tier. There is a very good possibility that Chautauqua County may find funding to establish their own "Teaching Factory" based on what they have learned in conversations with NIFM.

CONCLUSIONS:

In conclusion to our comments I feel that NIFM has been fair and reasonable in complying with the terms and the spirit of the contract. And, as such we respectfully request that your final determination is that NIFM is in compliance to the grants matching requirements.

Sincerely,

A handwritten signature in cursive script that reads "Stanley Shelly". The signature is written in dark ink and is positioned above the printed name and title.

Stanley Shelly
President