



APPALACHIAN REGIONAL COMMISSION

**INSPECTOR GENERAL'S
SEMIANNUAL REPORT
TO CONGRESS**

OCTOBER 1, 1990 - MARCH 31, 1991



APPALACHIAN REGIONAL COMMISSION

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INSPECTOR GENERAL
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May 15, 1991

MEMORANDUM FOR THE FEDERAL CO-CHAIRMAN

SUBJECT: Semiannual Report to Congress

In accordance with the requirements of the Inspector General Act Amendments of 1988, Public Law 100-504, I submit the semiannual report of the Office of Inspector General for the period October 1, 1990, through March 31, 1991.

During this reporting period, operational activities included issuance of thirteen individual grant audit reports; three headquarters survey reports, including one dealing with Business Development RLFs; and one investigation report. Recommendations highlighted the potential for more timely use of funds and system/control improvements with respect to general operations. Emphasis was also placed on contracting for audit services; guidance and/or monitoring of contract audit services; coordination with Federal, State, and ARC officials; and strategic audit planning.

Additionally, approval was received to employ a senior auditor to assist the Inspector General in day to day operations, conduct audits, and monitor contract audit staff.

During the reporting period, we also reviewed and commented on proposed changes to the ARC Code, provided a summary of audit results and status for followup by ARC, reviewed audit responses, and updated the status of non-housing RLFs. Also, audit and investigation work, with respect to several entities partially funded by ARC grants was initiated by other OIG offices.

We noted that ARC initiated actions to address some of our programmatic recommendations, including RLF capitalization, use of funds in a timely manner, and control of single audit reports. Although some recommendations remain open, we believe the thrust and intent of ARC decisions were positive and generally in line with audit positions.

TABLE OF CONTENTS

	<u>Page</u>
Executive Summary.ii
I Introduction	1
II Background	1
Appalachian Regional Commission.	1
Office of Inspector General Establishment.	2
III OIG Activity	3
Audits	3
Investigations	8
IV Audit Planning	8
V Legislative and Regulatory Review.	8
VI Other.	9
Appendices	
A. Schedule of Audit Reports Issued October 1, 1990 to March 31, 1991.10
B. Schedule of Audit Reports with Recommendations that Funds Be Put to Better Use.11
C. Schedule of Audit Reports with Questioned or Unsupported Costs.12
D. Definitions of Terms Used.13

EXECUTIVE SUMMARY

During this reporting period, thirteen grant audits, two headquarters surveys, and one program survey and followup were completed; and reports were issued containing recommendations for grantee and/or ARC actions. Additionally, one personnel investigation was completed, six audit survey programs were prepared, comments were provided on proposed ARC code revisions, and recommendations were made for increased assessment of administrative controls under the Federal Managers' Financial Integrity Act (FMFIA) and establishment of an ARC audit followup system.

Emphasis was also placed on contracting for audit services; contract monitoring; participating in PCIE study of single audit work; coordination with Federal, State, and ARC officials; and addressing staffing issues.

Examples include:

- o A survey of ARC activities disclosed that operations were being performed in a generally effective and efficient manner and that internal and compliance controls were generally sufficient to ensure such operations. The survey disclosed several areas and conditions where recommendations for improvement were made, including project coordinator and program evaluation activity, historical data base and management information systems, file documentation, project closing, and audit report control.
- o Thirteen grant audits, twelve conducted by contract staff and one by another OIG office under a reimbursable agreement, were completed and reports issued. These reports contained recommendations with respect to eligibility and documentation of costs incurred approximating \$390,000 and the need for increased revolving loan fund (RLF) activity to ensure timely use of available funds approximating \$1.5 million.
- o A summary report of business development RLFs identified eight grants with limited activity and loan balances of about \$2.9 million that could be put to better use pending RLF identification or development of additional loan activity. Recommendations were made with respect to actions and controls relative to timely use of funds, program monitoring, and identification of need.
- o The Inspector General is participating on a PCIE evaluation of single audit, and work to date included team preparation of questionnaires to pertinent single

I. INTRODUCTION

The Inspector General Act Amendments of 1988 (P.L. 100-504) provided for the establishment of an Office of Inspector General at 33 designated Federal entities, including the Appalachian Regional Commission (ARC). The ARC Office of Inspector General became operational on October 1, 1989, with the appointment of an Inspector General and provision of budgetary authority for contracted audit and/or investigation activities. Prior to the establishment of an Office of Inspector General, audit and investigation activity was carried out primarily by ARC staff, supplemented by financial and compliance audits, required of State and local agencies receiving Federal funds, and contracts with independent public accounting firms.

The Office of Inspector General will supplement these activities in line with the authorities and responsibilities noted in P.L. 100-504 and in the Inspector General Act of 1978 (P.L. 95-452).

II. BACKGROUND

A. APPALACHIAN REGIONAL COMMISSION

The Appalachian Regional Commission (ARC) was established as an independent agency by the Appalachian Regional Development Act of 1965 (P.L. 89-4). The Act authorizes a Federal/State partnership designed to promote long-term economic development on a coordinated regional basis in the 13 Appalachian States. The Commission represents a unique experiment in partnership among the Federal, State, and local levels of Government and between the public and private sectors. It is composed of the Governors of the 13 Appalachian States and a Federal representative who is appointed by the President. The Federal representative serves as the Federal Co-Chairman with the Governors electing one of their number to serve as the States' Co-Chairman.

- o Through joint planning and development of regional priorities, ARC funds are used to assist and encourage other public and private resources to address Appalachia's unique needs. Program direction and policy is established by the Commission (Appalachian Regional Commission Code) by the vote of a majority of the State members and the affirmative vote of the Federal Co-Chairman. Emphasis has been placed on highways, infrastructure development, business enterprise, and human resources programs.
- o Administratively, the Commission consists of three distinct, but interrelated components: the Office of the Federal Co-Chairman with a staff of 10, the Commission staff (56), and the Office of the States' Washington Representative (4). All personnel are located in

inquiries may be in the form of audits, surveys, criminal and other investigations, personnel security checks, or other appropriate methods. The two primary purposes of these inquiries are (1) to assist all levels of ARC management by identifying and reporting problem areas, weaknesses, or deficiencies in procedures, policies, program implementation, and employee conduct and (2) to recommend appropriate corrective actions.

Relationship to Other Principal ARC Offices

The ARC staff have full responsibility for establishing, executing, and ensuring compliance with policies, plans, and procedures; for proper protection and use of Commission resources; and for appropriate action on conditions needing improvement, including those reported by the OIG. The operations of the OIG neither replace established lines of operating authority nor eliminate the need for the Commission offices to take reasonable measures to protect and enhance the integrity and effectiveness of their operations. All Commission offices are responsible for monitoring and evaluating the programs entrusted to them and reporting information or incidences needing further audit and/or investigation to the Inspector General.

Funding and Staffing

FY 1991 funding for OIG operations is \$350,000. Approximately 57 percent was budgeted for contract audit or investigative services; 34 percent, for salaries and benefits; 6 percent, for travel; and 3 percent, for all other activities (training, equipment, supplies, etc.). The OIG funding level represents about 35 percent of the total funds available to the Office of the Federal Co-Chairman.

Initial OIG operations included authorization for an Inspector General and a Confidential Assistant. A senior Auditor has been approved and will be added to the permanent staff in the latter half of FY 1991. Grant review activities will continue to emphasize use of contracted services (e.g., independent public accounting firms or other OIG offices) supplemented by programmatic and performance reviews directed by OIG staff. Ongoing evaluations and determinations will continue with respect to the practicality and efficiency of this approach.

III. OIG ACTIVITY

A. AUDITS

During the reporting period, emphasis was placed on finalizing surveys of ARC operations and programs; completion of the initial round of grant audits by contractors; audit planning and guidance with respect to performance oriented reviews; audit resolution and followup; and continued liaison and communications with ARC, State, and other OIG officials about matters of mutual interest.

were issued. Continued followup is in process to resolve open issues, including planning of additional testing in areas such as automated systems, project monitoring and evaluation, file documentation, grant closings, and fund deobligations, and to provide management with additional information about these activities.

- o A survey of eighteen business development grants for establishment of revolving loan funds, including field audit tests of four grantees, disclosed eight cases where RLF activity was limited resulting in the potential for improved use of ARC RLF fund balances approximating \$2.9 million. Recommendations with respect to ARC actions included:

--RLF capitalizations should be based on need, including project proposals better identifying potential loan activity and grantee ability to utilize requested funds in a reasonable time period.

--ARC regulations and guidelines should include provisions with respect to low activity RLFs, implementation schedules, capitalization limitations, and periodic determinations of potential deobligations where limited activity is apparent, including cases noted in this report.

--Continued monitoring of RLFs to ensure grantee implementation of grant requirements and ARC RLF guidelines, and increased coordination with grantees to improve program operations, including marketing strategies essential for program success.

ARC management, in coordination with State Alternates, reviewed the RLF program, including the audit recommendations, and proposed several actions, including limiting initial RLF capitalizations to \$500,000 and provisions for withdrawing funds from an approved RLF grant if funds remain undisbursed from a grant 36 months after the date of approval.

Although we agree that the noted actions are positive, we also recommended that language and controls with respect to withdrawing funds should be strengthened and that procedures include implementation schedules for use of grant funds throughout the grant period, rather than a one-time withdrawal provision after 36 months.

Additionally, we noted that ARC had notified grantees of intentions to deobligate about \$1,640,000 from two RLFs due to inactivity, deobligated about \$96,000 in one case, and in another case ARC monitoring resulted in collection

practice/work in Appalachia reflected substantial increased activity during the past 2 years and a need for written guidelines, procedures, and controls identifying ARC responsibilities, policies, and activity under this program.

This survey coincided with the Federal Co-Chairman's initiatives to restructure the program, including the preparation of guidance with respect to ARC's role in the program and establishment of an automated data base identifying program activity.

- o Survey audit programs were prepared in conjunction with several planned reviews. These included:
 - Technical assistance grants;
 - Program evaluation;
 - Assessing the reliability of ARC computer processed data;
 - Administrative expenses;
 - Payroll and fringe benefits.
- o Information and recommendations with respect to audit followup responsibilities and a summary of open audits and issues needing ARC followup to facilitate report closing were provided ARC management.
- o Information was provided ARC management about Section 2, Internal Accounting and Administrative Controls, of the FMFIA, including potential internal control assessment methodologies. ARC implements FMFIA and emphasizes assessments of the Commission's accounting systems. Recommendation was made to include assessment of controls in future FMFIA assessments.
- o Emphasis continued to be placed on ascertaining the extent and effectiveness of single audit coverage provided ARC programs, including participation in a quality control review of a statewide single audit. Grant audit work included the review of available audit reports to avoid duplicative efforts. It was noted that most grants were subject to financial audits, either under single audit or in line with ARC, State, or local requirements. However, limited compliance testing of ARC activity was noted. Consequently, action remains necessary with respect to single audit compliance and transaction testing of non-major program activity in order to provide program managers with sufficient

VI. OTHER

The Inspector General is serving on the PCIE Task Force on Single Audit and participated in the development of questionnaires intended to obtain feedback from Federal, State, and local officials, including auditors, and public accounting firms about methods and procedures to improve single audit coverage and creditability.

The Inspector General participated in a meeting of the Association of Federal Investigation Directors and presented an overview of OIG operations in designated agencies.

An ARC management contracted study of various personnel and staffing issues affecting the Commission is continuing.

During the period of operation, ARC management has implemented and emphasized the ARC OIG concept and structure, despite normal apprehension and concern about the role, responsibility, and operational strategies of a mandated oversight office. The degree of general acceptance of the OIG concept is of particular importance due to the Federal/State nature of ARC, which substantially expands the client universe and requires addressing the concerns of 15 major clients including the Office of the Federal Co-Chairman, ARC Executive Director, and Governors of the 13 Appalachian States.

APPENDIX A

SCHEDULE OF AUDIT REPORTS ISSUED OCTOBER 1, 1990 TO MARCH 31, 1991

Audit Report No.	Title	Program Dollars or Contract/Grant Amount	Questioned Costs*	Unsupported Costs**	Funds to Better Use***
	Contract Audits				
91-1(H)	ARC Business Development RLFs	\$13,400,000 ^{1/}			\$2,900,000 ^{1a/}
91-2(H)	Survey of ARC Program Activities and Controls	5,400,000 ^{2/}			
91-3(H)	Survey of J-1 Waiver Program				
91-4(H)	Update of RLF Status	4,260,268			(2,588,292) ^{1b/}
91-1(G)	Georgia Department of Community Affairs (RLF)	1,000,000			(668,524) ^{3/}
91-2(G)	South Carolina Appalachian Council of Governments (RLF)	1,000,000			(877,200) ^{3/}
91-3(G)	Ironton Iron, Inc. RLF (OVRDC), Ironton, Ohio	300,000	\$148,398		
91-4(G)	Regional Service Agency of Appalachian Maryland--Technology Transfer	400,000			
91-5(G)	Tennessee Department of Education, Adult Literacy	1,500,000 ^{4/}	2,562		
91-6(G)	Centre South Riverport and Industrial Park--Hamilton County, Tennessee	4,371,000		82,800	
91-7(G)	Woodlands Mountain Institute--Franklin, West Virginia	333,000		65,633	
91-8(G)	Bluegrass State Skills Corp. Technical Assistance	124,080	16,235		
91-9(G)	Bluegrass State Skills Corp. Training Project	198,500	1,681		
91-10(G)	Wytheville Community College, Wytheville, Virginia	100,000	17,483		
91-11(G)	New River Community College, Dublin, Virginia	59,450	1,441	22,000	
91-12(G)	Macon County Sewer and Water Extension, Franklin, North Carolina	202,642	33,965		
91-13(G)	Northeast Mississippi Planning and Development District	1,075,000 ^{5/}			
TOTALS		\$33,723,940	\$221,765	\$170,433	\$2,900,000

* A cost the Office of Inspector General has questioned because of an alleged violation of law, regulation, contract, or other agreements governing the expenditure of funds; such cost is not supported by adequate documentation; or the expenditure of funds for the intended purpose is unnecessary or unreasonable.

** A cost the Office of Inspector General has questioned because of a lack of adequate documentation at the time of the audit.

*** Funds the Office of Inspector General has identified in an audit recommendation that could be used more efficiently by reducing outlays, deobligating program or operational funds, avoiding unnecessary expenditures, or taking other efficiency measures, such as timely use of funds.

**** Includes \$33,000 in excess cash returned by grantee.

^{1/} \$13.4 million of RLF grants to 18 entities included in the audit universe. The dollars applicable to individual grants audited are also included for each audit. The report was based on field testing of 4 RLFs and headquarters review of grant files for the remaining RLFs.

^{1a/} \$2,900,000 represents approximate balances in eight RLFs highlighted in RLF summary report issued 11/13/90.

^{1b/} \$2,588,292 represents balances of nine RLF's in an updated survey report, including five RLFs that had no loan activity since the initial report with balances of about \$1.4 million. These funds were included in the initial survey report as having potential for better use.

^{2/} Survey of ARC headquarters included all Federal and Commission operations for which administrative costs approximate \$5.4 million annually. No attempt was made to quantify audit results in terms of dollar impacts.

^{3/} Included in summary report totals.

^{4/} Includes \$500,000 grants for 1988, 1989, and 1990.

^{5/} Audit performed by Department of Commerce OIG.

APPENDIX B

SCHEDULE OF AUDIT REPORTS WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE

	<u>No. of Reports*</u>	<u>Dollar Value (\$ in thousands)</u>
A. For which no management decision has been made by the commencement of the reporting period	0	0
B. Which were issued during the reporting period	1	\$2,900
Subtotals (A + B)	1	\$2,900
C. For which a management decision was made during the reporting period	0	0
(i) dollar value of recommendations that were agreed to by management	0	0
--based on proposed management action	0	0
--based on proposed legislative action	0	0
(ii) dollar value of recommendations that were not agreed to by management	0	0
D. For which no management decision has been made by the end of the reporting period	1	\$2,900**
E. Reports for which no management decision was made within 6 months of issuance	0	0

* There were no instances of significant revised management decisions or information concerning significant management decisions with which the Inspector General is in disagreement during the reporting period.

** This includes an overall summary report and individual reports contributing to the summary report. Action is in process and, as of the end of the reporting period, ARC management had initiated various actions including proposals to deobligate \$1.6 million, collection of \$600 thousand in excess cash based on grant monitoring, and initiation of controls to better ensure timely use of funds. Final decisions on multiple audit recommendations and grants noted in the summary report (91-1-H, Business Development Revolving Loan Funds) will be made in the April 1 to September 30, 1991 reporting period.

APPENDIX C

**SCHEDULE OF AUDIT REPORTS WITH
QUESTIONED OR UNSUPPORTED COSTS**
(\$ in thousands)

	<u>No. of Reports*</u>	<u>Questioned Costs</u>	<u>Unsupported Costs</u>
A. For which no management decision has been made by the commencement of the reporting period	3	\$137	\$260
B. Which were issued during the reporting period	9	\$222	\$170
Subtotals (A + B)	12	\$359	\$430
C. For which a management decision was made during the reporting period	10	\$325	\$170
(i) dollar value of disallowed costs	4	\$141	0
(ii) dollar value of costs not disallowed	6	\$184	\$170
D. For which no management decision has been made by the end of the reporting period	2	\$ 34	\$260
E. Reports for which no management decision was made within 6 months of issuance	1	0	\$260**

* There were no instances of significant revised management decisions or information concerning significant management decisions with which the Inspector General is in disagreement during the reporting period.

** This involves one grant report from prior audit period where a management decision was made to pursue the open issue, but a final decision is not possible with respect to unsupported costs of \$26,000 pending receipt of additional documentation to support the claim that has been requested by OIG from the grantee. Final decisions are expected by June 30, 1991, for this audit--West Virginia Economic and Development Authority 90-7-6.

DEFINITIONS OF TERMS USED

The following definitions apply to terms used in reporting audit statistics:

Questioned Cost

A cost which the Office of Inspector General (OIG) questioned because of an alleged violation of a provision of a law, regulation, contract, or other agreement or document governing the expenditure of funds; such cost is not supported by adequate documentation; or the expenditure of funds for the intended purpose is unnecessary or unreasonable.

Unsupported Cost

A cost which the OIG questioned because the cost was not supported by adequate documentation at the time of the audit.

Disallowed Cost

A questioned cost that management, in a management decision, has sustained or agreed should not be charged to the Commission.

Funds Be Put To Better Use

A recommendation made by the OIG that funds could be used more efficiently if management took actions to implement and complete the recommendation.

Management Decision

Management's evaluation of the findings and recommendations included in the audit report and the issuance of a final decision by management concerning its response to such findings and recommendations, including actions concluded to be necessary. Interim decisions and actions are not considered final management decisions for the purpose of the tables in this report.

Final Action

The completion of all management actions that are described in a management decision with respect to audit findings and recommendations. If management concluded that no actions were necessary, final action occurs when a management decision is issued.