



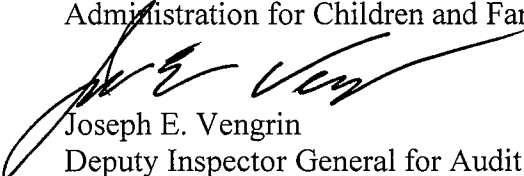
DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Washington, D.C. 20201

**AUG 18 2008**

**TO:** Daniel C. Schneider  
Acting Assistant Secretary  
Administration for Children and Families

**FROM:**   
Joseph E. Vengrin  
Deputy Inspector General for Audit Services

**SUBJECT:** Review of Unexpended Infant and Toddler Targeted Funds and Quality Targeted Funds Claimed by the Iowa Department of Human Services for Fiscal Years 1998–2003 (A-07-07-00231)

Attached is an advance copy of our final report on unexpended infant and toddler targeted funds and quality targeted funds claimed by the Iowa Department of Human Services (the State agency). We will issue this report to the State agency within 5 business days. We undertook this review of Iowa's Child Care and Development Fund (CCDF) program in response to information provided by the Administration for Children and Families regional office.

The CCDF provides targeted discretionary Federal funding for certain activities, such as Infant and Toddler activities and Quality activities, to improve the availability, quality, and affordability of childcare and to support the administration of these activities. The State agency contracted with the Iowa Child Care and Early Education Network (the Network), a private entity, to act as its fiscal agent in disbursing Infant and Toddler targeted funds and Quality targeted funds to subgrantees for Federal fiscal years (FY) 1998–2003.

Our objectives were to determine, for FYs 1998–2003, whether the State agency complied with Federal requirements for (1) claiming CCDF targeted funds and (2) remitting interest earned by the Network on those funds.

The State agency did not comply with Federal requirements when claiming \$3,156,226 of CCDF targeted funds for FYs 1998–2003. Specifically, the State agency (1) did not refund to the Federal Government the targeted funds that remained unliquidated after the timeframe specified in Federal regulations, (2) did not return the funds to the Federal Government when it terminated the Network's contract and transferred funds to a successor contractor after the obligation period for the funds had expired, and (3) did not limit cash advances to the Network to the minimum amounts needed to carry out the purposes of the program. The State agency did not comply with Federal requirements because it relied on a State statute governing the use of State funds and incorrectly applied that statute to Federal funds.

In addition, the State agency did not remit \$155,032 of interest earned by the Network on advanced CCDF targeted funds as required.

We recommend that the State agency:

- refund to the Federal Government \$3,156,226 of unexpended CCDF targeted funds allotted during FYs 1998–2003,
- remit to the Federal Government \$155,032 of interest earned on the CCDF targeted funds held by the Network for FYs 1998–2003,
- ensure that CCDF targeted funds are disbursed in accordance with Federal requirements in the future, and
- review CCDF targeted funds claimed for Federal reimbursement after the audit period and refund any unallowable amounts.

In written comments on our draft report, the State agency did not concur with our first recommendation, concurred with our second and fourth recommendations, and acknowledged but did not concur with our third recommendation. After reviewing the State agency's comments, we continue to support all of our findings and recommendations.

If you have any questions or comments about this report, please do not hesitate to call me, or your staff may contact Lori S. Pilcher, Assistant Inspector General for Grants, Internal Activities, and Information Technology Audits, at (202) 619-1175 or through e-mail at [Lori.Pilcher@oig.hhs.gov](mailto:Lori.Pilcher@oig.hhs.gov) or Patrick J. Cogley, Regional Inspector General for Audit Services, at (816) 426-3591 or through e-mail at [Patrick.Cogley@oig.hhs.gov](mailto:Patrick.Cogley@oig.hhs.gov). Please refer to report number A-07-07-00231.

Attachment



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General  
Offices of Audit Services

Region VII  
601 East 12th Street  
Room 284A  
Kansas City, Missouri 64106

AUG 21 2008

Report Number: A-07-07-00231

Mr. Kevin Concannon  
Director  
Iowa Department of Human Services  
Hoover State Office Building  
1305 East Walnut Street  
Des Moines, Iowa 50319-0114

Dear Mr. Concannon:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), final report entitled "Review of Unexpended Infant and Toddler Targeted Funds and Quality Targeted Funds Claimed by the Iowa Department of Human Services for Fiscal Years 1998-2003." We will forward a copy of this report to the HHS action official noted on the following page for review and any action deemed necessary.

The HHS action official will make final determination as to actions taken on all matters reported. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

Pursuant to the principles of the Freedom of Information Act, 5 U.S.C. § 552, as amended by Public Law 104-231, OIG reports generally are made available to the public to the extent the information is not subject to exemptions in the Act (45 CFR part 5). Accordingly, this report will be posted on the Internet at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at (816) 426-3591, or contact Jenenne Tambke, Audit Manager, at (573) 893-8338, extension 21, or through e-mail at [Jenenne.Tambke@oig.hhs.gov](mailto:Jenenne.Tambke@oig.hhs.gov). Please refer to report number A-07-07-00231 in all correspondence.

Sincerely,

A handwritten signature in black ink, appearing to read "Patrick J. Cogley".

Patrick J. Cogley  
Regional Inspector General  
for Audit Services

Enclosure

**Direct Reply to HHS Action Official:**

Ms. Moniquin Huggins  
Acting Associate Director  
Child Care Bureau  
Administration for Children and Families  
901 D Street SW.  
Washington, DC 20447

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF UNEXPENDED  
INFANT AND TODDLER  
TARGETED FUNDS AND  
QUALITY TARGETED FUNDS  
CLAIMED BY THE  
IOWA DEPARTMENT OF  
HUMAN SERVICES  
FOR FISCAL YEARS  
1998–2003**



Daniel R. Levinson  
Inspector General

August 2008  
A-07-07-00231

# *Office of Inspector General*

<http://oig.hhs.gov>

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The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

## *Office of Audit Services*

The Office of Audit Services (OAS) provides auditing services for HHS, either by conducting audits with its own audit resources or by overseeing audit work done by others. Audits examine the performance of HHS programs and/or its grantees and contractors in carrying out their respective responsibilities and are intended to provide independent assessments of HHS programs and operations. These assessments help reduce waste, abuse, and mismanagement and promote economy and efficiency throughout HHS.

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# *Notices*

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**THIS REPORT IS AVAILABLE TO THE PUBLIC**  
at <http://oig.hhs.gov>

Pursuant to the principles of the Freedom of Information Act, 5 U.S.C. § 552, as amended by Public Law 104-231, Office of Inspector General reports generally are made available to the public to the extent the information is not subject to exemptions in the Act (45 CFR part 5).

## **OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS**

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.

## **EXECUTIVE SUMMARY**

### **BACKGROUND**

#### **Child Care and Development Fund**

The Child Care and Development Fund (CCDF) assists certain low-income families in obtaining childcare so that family members can work or attend training or education. The Administration for Children and Families (ACF) administers the CCDF at the Federal level. The Iowa Department of Human Services (the State agency) administers the State's CCDF program.

The CCDF provides targeted discretionary Federal funding for certain activities, such as Infant and Toddler activities and Quality activities, to improve the availability, quality, and affordability of childcare and to support the administration of these activities. States are required to report expenditures of targeted funds on the quarterly Child Care and Development ACF-696 Financial Report, which is a cumulative report for the fiscal year (FY). Federal regulations require that CCDF targeted funds be obligated and liquidated within a specified timeframe. Funds that are neither obligated nor liquidated within this timeframe must revert to the Federal Government.

#### **State Agency's Fiscal Agents**

The State agency contracted with the Iowa Child Care and Early Education Network (the Network), a private entity, to act as its fiscal agent in disbursing Infant and Toddler targeted funds and Quality targeted funds to subgrantees for Federal FYs 1998–2003. The Network's function was to hold the funds pending the State agency's authorization for disbursement. In June 2006, the State agency terminated the Network's contract and directed the Network to transfer the remaining unexpended funds from FYs 1998–2003 to the State Public Policy Group (SPPG), another private entity. The State agency contracted with SPPG to act as its fiscal agent for those funds. As of February 2008, the State agency had not instructed SPPG to disburse the targeted funds to subgrantees; thus, the funds remained unexpended.

The Network had held the funds in an interest-bearing account until it transferred the funds to SPPG. Federal guidance requires that interest earned on Federal funds by a third party (such as the Network) be reported on the quarterly Payment Management System-272 report.

### **OBJECTIVES**

Our objectives were to determine, for FYs 1998–2003, whether the State agency complied with Federal requirements for (1) claiming CCDF targeted funds and (2) remitting interest earned by the Network on those funds.

### **SUMMARY OF FINDINGS**

The State agency did not comply with Federal requirements when claiming \$3,156,226 of CCDF targeted funds for FYs 1998–2003. Specifically, the State agency (1) did not refund to the



Federal Government the targeted funds that remained unliquidated after the timeframe specified in Federal regulations, (2) did not return the funds to the Federal Government when it terminated the Network's contract and transferred funds to a successor contractor after the obligation period for the funds had expired, and (3) did not limit cash advances to the Network to the minimum amounts needed to carry out the purposes of the program. The State agency did not comply with Federal requirements because it relied on a State statute governing the use of State funds and incorrectly applied that statute to Federal funds.

In addition, the State agency did not remit \$155,032 of interest earned by the Network on advanced CCDF targeted funds as required.

## **RECOMMENDATIONS**

We recommend that the State agency:

- refund to the Federal Government \$3,156,226 of unexpended CCDF targeted funds allotted during FYs 1998–2003,
- remit to the Federal Government \$155,032 of interest earned on the CCDF targeted funds held by the Network for FYs 1998–2003,
- ensure that CCDF targeted funds are disbursed in accordance with Federal requirements in the future, and
- review CCDF targeted funds claimed for Federal reimbursement after the audit period and refund any unallowable amounts.

## **STATE AGENCY COMMENTS**

In written comments on our draft report, the State agency did not concur with our first recommendation, concurred with our second and fourth recommendations, and acknowledged but did not concur with our third recommendation.

The State agency's written comments are included in their entirety as the Appendix.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

After reviewing the State agency's comments, we continue to support all of our findings and recommendations.

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## INTRODUCTION

### BACKGROUND

The Administration for Children and Families (ACF), U.S. Department of Health and Human Services, administers the Child Care and Development Fund (CCDF). We undertook this review of Iowa's CCDF program in response to information provided by ACF's regional office. The Iowa Department of Human Services (the State agency) administers the State's CCDF program.

#### **Child Care and Development Fund**

Pursuant to the Child Care and Development Block Grant Act and section 418 of the Social Security Act, the CCDF assists low-income families, families receiving temporary public assistance, and families transitioning from public assistance in obtaining childcare so that family members can work or attend training or education. The CCDF provides targeted discretionary funding<sup>1</sup> for certain activities, such as Infant and Toddler activities and Quality activities, to improve the availability, quality, and affordability of childcare and to support the administration of these activities. These activities are 100 percent federally funded. States are required to report expenditures of targeted funds on the quarterly Child Care and Development ACF-696 Financial Report (ACF-696 report), which is a cumulative report for the fiscal year (FY).

Each State must develop, and submit to ACF for approval, a State plan that identifies the purposes for which CCDF targeted funds will be expended for two grant periods (i.e., 2 Federal FYs). Federal regulations (45 CFR § 98.60) require that CCDF targeted funds be obligated and liquidated within a specified timeframe. Funds that are neither obligated nor liquidated within this timeframe must revert to the Federal Government.

#### **State Agency's Fiscal Agents**

In January 1999, the State agency contracted with the Iowa Child Care and Early Education Network (the Network), a private entity, to act as its fiscal agent in disbursing Infant and Toddler targeted funds and Quality targeted funds to subgrantees for Federal FYs 1998–2003. The Network's function was to hold the funds pending the State agency's authorization for disbursement. The State agency retained control of the decisionmaking process of awarding the targeted funds to subgrantees.

The State agency terminated the Network's contract in June 2006 and directed the Network to transfer the remaining unexpended funds from FYs 1998–2003 to the State Public Policy Group (SPPG), another private entity. The State agency contracted with SPPG to act as its fiscal agent for those funds. As of February 2008, the State agency had not instructed SPPG to disburse the targeted funds to subgrantees; thus, the funds remained unexpended.

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<sup>1</sup>Congress specifically appropriates funding each year for these targeted activities. Targeted funds were referred to in the past as "earmarks." ACF Program Instruction, CCDF-ACF-PI-2007-05 (July 17, 2007).

The Network had held the funds in an interest-bearing account until it transferred the funds to SPPG. Federal guidance requires that interest earned on Federal funds by a third party (such as the Network) be reported on the quarterly Payment Management System (PMS)-272 report.

## **OBJECTIVES, SCOPE, AND METHODOLOGY**

### **Objectives**

Our objectives were to determine, for FYs 1998–2003, whether the State agency complied with Federal requirements for (1) claiming CCDF targeted funds and (2) remitting interest earned by the Network on those funds.

### **Scope**

Our audit covered the period October 1, 1998, through September 30, 2003. We limited our review to the \$3,156,226 of targeted funds that the State agency claimed on its ACF-696 reports during the audit period and that had not been disbursed to subgrantees.<sup>2</sup> We did not review the \$7,423,326 of targeted funds that the Network had disbursed to subgrantees.

We also reviewed the treatment of \$155,032 in interest earned on the FYs 1998–2003 targeted funds that the Network held.

We did not perform a detailed review of the State agency's internal controls because our objectives did not require us to do so. We limited our review to controls over the drawdown of targeted funds, the transfer of targeted funds to the Network, the preparation of ACF-696 reports, and the handling of interest earned on Federal funds.

We conducted fieldwork at the State agency in Des Moines, Iowa.

### **Methodology**

To accomplish our objectives, we:

- reviewed applicable Federal laws, regulations, and program guidance, as well as State laws and the approved Iowa CCDF State plan;
- reviewed the ACF-696 reports for FYs 1998–2003 to determine the amount of targeted funds that the State agency claimed;
- interviewed State agency staff responsible for preparing the ACF-696 reports to obtain an understanding of how the reports were prepared, how the targeted funds were reported, and what documentation was maintained to support expenditures on the reports;

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<sup>2</sup>We were unable to assign these funds to specific FYs.

- reviewed the State agency's supporting documentation used to prepare the ACF-696 reports;
- interviewed State agency officials responsible for drawing down targeted funds from the Federal Government to determine the timing of the drawdown in relation to the transfer of the funds to the Network;
- interviewed Network officials to determine how the Network received and held funds from the State agency;
- reviewed the State agency's and the Network's accounting records to determine the amount of targeted funds transferred to the Network and the amount of the Network's disbursements to subgrantees;
- interviewed SPPG staff to determine the amount of targeted funds transferred from the Network to SPPG and to determine whether SPPG had disbursed any of the funds to subgrantees;
- interviewed State agency officials responsible for handling the interest earned on Federal funds to determine the procedures for reporting interest and the amount of interest returned to the Federal Government;
- reviewed the Network's records, including the audited financial statements, to determine the interest earned on Federal funds and the interest collected by the State agency; and
- reviewed the PMS-272 reports for the first three quarters of calendar year 2007 and the State agency's February 2008 financial status report to determine the amount of interest remitted to the Federal Government.

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, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## **FINDINGS AND RECOMMENDATIONS**

The State agency did not comply with Federal requirements when claiming \$3,156,226 of CCDF targeted funds for FYs 1998–2003. Specifically, the State agency (1) did not refund to the Federal Government the targeted funds that remained unliquidated after the timeframe specified in Federal regulations, (2) did not return the funds to the Federal Government when it terminated the Network's contract and transferred funds to a successor contractor after the obligation period for the funds had expired, and (3) did not limit cash advances to the Network to the minimum amounts needed to carry out the purposes of the program. The State agency did not comply with Federal requirements because it relied on a State statute governing the use of State funds and incorrectly applied that statute to Federal funds.

In addition, the State agency did not remit \$155,032 of interest earned by the Network on advanced CCDF targeted funds as required.

## **UNEXPENDED TARGETED FUNDS**

### **Federal Requirements**

Federal regulations (45 CFR § 98.60(d)(1)) require that CCDF discretionary fund allotments be obligated in the FY in which the funds are awarded or in the succeeding FY. This provision further requires that “[u]nliquidated obligations as of the end of the succeeding fiscal year shall be liquidated within one year.” Any funds that are neither obligated nor liquidated within this timeframe must revert to the Federal Government in accordance with 45 CFR § 98.60(d)(7). Absent applicable State law definitions (45 CFR § 98.60(d)(4)), the terms related to this provision are defined in 45 CFR § 92.3 as follows:

- *Obligations* means the amounts of orders placed, contracts and subgrants awarded, goods and services received, and similar transactions during a given period that will require payment by the grantee during the same or a future period.
- *Outlays* (expenditures) mean charges made to the project or program . . . . For reports prepared on a cash basis, outlays are the sum of actual cash disbursement for direct charges for goods and services, the amount of indirect expense incurred, the value of in-kind contributions applied, and the amount of cash advances and payments made to contractors and subgrantees.
- *Unliquidated obligations* for reports prepared on a cash basis mean the amount of obligations incurred by the grantee that has not been paid. For reports prepared on an accrued expenditure basis, they represent the amount of obligations incurred by the grantee for which an outlay has not been recorded.
- *Unobligated balance* means the portion of the funds authorized by the Federal agency that has not been obligated by the grantee and is determined by deducting the cumulative obligations from the cumulative funds authorized.

Federal regulations (45 CFR § 98.60(g)(2)) state that “[f]unds that are returned (e.g., . . . unused subgrantee funds) as well as program income . . . shall . . . if received after the end of the applicable obligation period . . . be returned to the Federal government.”

Pursuant to 45 CFR § 98.60(f), “[c]ash advances shall be limited to the minimum amounts needed and shall be timed to be in accord with the actual, immediate cash requirements of the State Lead Agency, its subgrantee or contractor in carrying out the purpose of the program in accordance with 31 CFR part 205.”

Federal regulations (45 CFR § 98.11(b)(4)) require that the State agency ensure that the administration of the CCDF program complies with the approved State plan and with all Federal requirements.

## Unallowable Funds Claimed

The \$3,156,226 of targeted funds that the State agency claimed was unallowable because the State agency (1) did not refund to the Federal Government the targeted funds that remained unliquidated after the specified timeframe, (2) did not return the funds to the Federal Government when it terminated the Network's contract after the obligation period for the funds had expired, and (3) did not limit cash advances to the Network to the minimum amounts needed to carry out the purposes of the program.

The State agency claimed the \$3,156,226 for FYs 1998–2003 but had not obligated or liquidated the funds to subgrantees as of the end of our fieldwork (December 2006). Although the State agency did not track these targeted funds by FY, the last FY for which targeted funds were transferred to the Network was FY 2003, and the liquidation period for that FY expired on September 30, 2005. Thus, the State agency did not comply with the requirement of 45 CFR § 98.60(d)(1) that targeted funds be obligated in either the FY in which the funds are awarded or the succeeding FY and be liquidated within 1 year. Simply transferring funds to a third party without receiving any childcare service in return is insufficient to meet Federal requirements applicable to the CCDF.

Upon termination of the Network contract, the State agency directed the Network to transfer the CCDF targeted funds to SPPG to be held until directed by the State agency. The last Federal grant that the Network received was for FY 2003, for which the obligation period ended on September 30, 2004. The termination of the Network contract by the State agency in early 2006 occurred after the end of the obligation period and should, therefore, have resulted in the return of the CCDF targeted funds to the Federal Government pursuant to 45 CFR § 98.60(g). However, as of February 2008, the State agency had not directed SPPG to disburse any of the funds to subgrantees and had not returned the funds to the Federal Government.

In addition, the State agency drew down the entire \$3,156,226 of targeted funds for transfer to the Network but did not direct the Network to disburse the funds for program purposes. Contrary to 45 CFR § 98.60(f), this drawdown did not constitute a use of cash advances that was limited to the minimum amount needed. The State agency's decision to hold those funds for an extended period without disbursing them also did not comply with Federal mandates that cash advances be timed in accordance with actual, immediate cash needs.

The State agency believed, based on a State statute,<sup>3</sup> that the targeted funds were obligated when it executed the contract with the Network and that the obligation was liquidated when it transferred the funds to the Network. However, the State agency's contract with the Network did not constitute an obligation, nor did the transfer of the funds to the Network constitute liquidation absent the receipt of childcare services or other authorized CCDF activities. Even if State or Federal definitions of obligation and liquidation technically were met, the State should

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<sup>3</sup>Iowa Code 8.33 addresses the circumstances under which State funds revert to the State treasury at the end of each FY. The statute states that all unencumbered or unobligated balances of appropriations made for that FY revert to the State treasury. The State agency believed that once a contractual liability was paid, the amount was no longer considered an unobligated balance. However, there is no specific Iowa statutory definition of either "obligation" or "liquidation." Accordingly, the definitions of these terms in 45 CFR § 92.3 apply.

have returned the funds to the Federal Government when it terminated the contract with the Network. Furthermore, the State's drawdown of CCDF funds without an immediate need to provide childcare services was an inappropriate use of a cash advance.

## **INTEREST EARNED ON ADVANCED TARGETED FUNDS**

### **Federal Requirements**

Federal regulations (45 CFR § 92.21(i) and 45 CFR § 74.22(l)) require that recipients that earn interest on advances of Federal funds remit that interest to the Federal Government. Instructions for the PMS-272 report state: "Interest earned on Federal funds received by a recipient from a third party . . . must be accounted for to the Federal Government." These instructions specify that the interest must be reported on line 7 of the PMS-272 report and that States are not exempt from this reporting requirement.

### **Interest Not Remitted**

The State agency incorrectly retained \$155,032 of interest earned by the Network on the FYs 1998–2003 Infant and Toddler and Quality targeted funds. In early calendar year 2007, the Network remitted \$88,487 of this interest to the State agency. At the time of our fieldwork, the State agency was working to collect the remaining \$66,545 from the Network. However, as of February 2008, the State agency had not reported or remitted any of the \$155,032 of interest earned on Federal funds to the Federal Government as required.

## **RECOMMENDATIONS**

We recommend that the State agency:

- refund to the Federal Government \$3,156,226 of unexpended CCDF targeted funds allotted during FYs 1998–2003,
- remit to the Federal Government \$155,032 of interest earned on the CCDF targeted funds held by the Network for FYs 1998–2003,
- ensure that CCDF targeted funds are disbursed in accordance with Federal requirements in the future, and
- review CCDF targeted funds claimed for Federal reimbursement after the audit period and refund any unallowable amounts.

## **STATE AGENCY COMMENTS**

In written comments on our draft report, the State agency did not concur with our first recommendation, concurred with our second and fourth recommendations, and acknowledged but did not concur with our third recommendation.



With respect to our first recommendation, the State agency disagreed that, under both Federal requirements and Iowa law, a liquidation of funds requires receipt of childcare services or other authorized CCDF activities. Specifically:

- The State agency contrasted the language in 42 U.S.C. § 9858h(c), which “uses the permissive ‘may,’ ” with “federal regulations [that] substitute the mandatory ‘shall’ ” in discussing timeframes for obligation of Federal funds and concluded that the “mandatory nature of the federal regulations is at odds with the statutory language and arguably the federal regulations are ultra vires of the authority of ACF.”
- The State agency said that 45 CFR §§ 92.3 and 98.60 provide that an obligation occurs “when there is a contract awarded as well as when goods or services are received.”
- The State agency said that Federal regulations do not define “liquidation” but define only “unliquidated obligation.” The State agency added that “[a]ssuming that the definition of ‘liquidation’ is the opposite of ‘unliquidated obligation’, the Department [the State agency] has met the definition because it has paid the Network the amount specified in the contract.”
- The State agency said that “the words obligation and liquidation are federal terms. In Iowa, that same concept is known as reversion. The federal regulations defer to controlling state law and applicable state law should be applied so long as it controls the availability of funds following the close of a fiscal year.” In this case, according to the State agency, the applicable State law was Iowa Code § 8.33. The State agency further cited a 1979 Iowa attorney general opinion that found that once appropriated funds were given to a local entity, the money was considered already spent or encumbered and was beyond the reach of the reversion statute.

Despite these assertions, the State agency stated that if ACF agreed with “the interpretation of law as set forth by [the Office of Inspector General],” the State agency would accept ACF’s interpretation and refund the \$3,156,226 of CCDF targeted funds to the Federal Government.

With respect to our third recommendation, the State agency referred to its response to our first recommendation. The State agency added that although it believed that the liquidation of the targeted funds during the audit period met Federal requirements, it now obligates and liquidates the funds in accordance with 45 CFR § 98.60(d)(1).

The State agency’s written comments are included in their entirety as the Appendix.

## **OFFICE OF INSPECTOR GENERAL RESPONSE**

After reviewing the State agency’s comments, we continue to support all of our findings and recommendations, including our recommendation that the State agency refund \$3,156,226 of unexpended CCDF targeted funds.

The State agency based its comments on its belief that its contract with the Network (as fiscal agent) and subsequent disbursement of the targeted funds met the definition of liquidation. We continue to disagree on the grounds that the State agency's position is based on an incorrect interpretation of governing Federal requirements. The targeted funds remained unexpended and were never used for the purposes of the grant. Even if the State agency technically met the Federal and State definitions of "obligation" and "liquidation," the State agency should refund the \$3,156,226. The State agency violated 45 CFR § 98.60(g) when it failed to return the funds to the Federal Government upon termination of the Network contract. Furthermore, the State agency violated 45 CFR § 98.60(f) when it drew down CCDF funds without any immediate need, as evidenced by the millions of dollars that it never disbursed during the audit period. The State agency did not comment on these additional regulatory bases that support our recommended refund.

# **APPENDIX**



## STATE OF IOWA

CHESTER J. CULVER, GOVERNOR  
PATTY JUDGE, LT. GOVERNOR

JUN 12 2008

DEPARTMENT OF HUMAN SERVICES  
KEVIN W. CONCANNON, DIRECTOR

Patrick J. Cogley  
Regional Inspector General for Audit Services  
DHHS - Office of Inspector General  
Region VII - Room 284A  
601 East 12<sup>th</sup> Street  
Kansas City, MO 64106

RE: Review of Unexpended Infant and Toddler Targeted Funds and Quality Targeted Funds  
Claimed by the Iowa Dept. of Human Services for FFYs 1998-2003:  
**Report Number: A-07-07-00231**

Dear Mr. Cogley:

Enclosed please find comments from the Iowa Department of Human Services (DHS) to the April 17, 2008 draft report concerning Iowa's targeted Child Care and Development Fund (CCDF) expenditures for Federal Fiscal Years (FFYs) 1998 through 2003.

I appreciate that your office granted DHS a 30-day extension, until June 16, 2008, to respond to the draft OIG report. The attached response addresses each OIG recommendation and provides clarifying comments about the review and draft report.

The Department welcomes the opportunity to work with the OIG to resolve areas of disagreement or other concerns before the final report is issued.

Questions about the attached response can be addressed to:  
Ken Tigges, Div. of Fiscal Management  
Iowa Department of Human Services  
Hoover State Office Building, 1st Floor South  
Des Moines, IA 50319-0114  
Phone: 515-281-6027  
Email: ktigges@dhs.state.ia.us

I understand that this response will be summarized in the body of the final report and included in its entirety as an appendix.

Sincerely,

A handwritten signature in black ink that reads "Kevin W. Concannon".

Kevin W. Concannon  
Director

cc: Jenenne Tambke, Audit Manager

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**IOWA DEPARTMENT OF HUMAN SERVICES (DHS) RESPONSE TO:  
OIG Review of Unexpended Infant and Toddler Targeted Funds and  
Quality Targeted Funds Claimed by the Iowa DHS for FFY 1998-2003:  
Report Number: A-07-07-00231**

**BACKGROUND**

When Iowa first received the targeted quality and infant/toddler funds, we began a comprehensive planning process to determine the most effective use of the funds. In collaboration with the State Child Care Advisory Council and ad hoc workgroups established by the Council, the Department developed a plan that included specific projects to improve both overall quality of child care and infant/toddler care. The Department developed these projects with stakeholders including child care providers, state agencies, Head Start, and Iowa State University. The projects, which continue today, include but are not limited to, the Program for Infant and Toddler Caregiver training and support through regional infant/toddler specialists (which has received national recognition as a model), the T.E.A.C.H Iowa program to support child care provider education, the business practices project, regional child care home consultants to improve the quality of home-based care, and other professional development opportunities for child care providers. This comprehensive plan has served Iowa well in developing quality child care services for children.

For the time period in question, the Department used the CCDF Quality targeted and Infant and Toddler targeted funds to support activities described above to improve access to quality infant and toddler child care services and to improve the overall quality of child care.

The available funds were used only for improvement activities, not for direct child care assistance services. Should any funds ultimately be returned to the federal government, there will be no adverse effect on the access to child care services for children living in families who qualify for the child care assistance program. There would also be no impact on Iowa's quality improvement projects since the Department has held the questioned funds in a separate account pending the final resolution by ACF.

**RESPONSES TO RECOMMENDATIONS**

**OIG Recommendation #1:**

Refund to the Federal Government \$3,156,226 of unexpended CCDF targeted funds allotted during FYs 1998-2003.

**Response:**

The Department does not concur with this recommendation for the following reasons.

OIG finds that federal regulations require State agencies to obligate targeted funds "in either the FY in which the funds are awarded or the succeeding FY and be liquidated within 1 year.

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Simply transferring funds to a third party without receiving any childcare service in return is insufficient to meet Federal requirements applicable to the CCDF.” (Draft Report, p. 5). OIG also interprets relevant Iowa law to find that Iowa law requires a “receipt of childcare services or other authorized CCDF activities” in order to constitute a liquidation of the funds. The Department disagrees with the legal conclusions of OIG both as to federal law and state law.

OIG references the federal regulations regarding obligation and liquidation of federal funds (45 CFR § 98.60 and 45 CFR § 92.3) but conspicuously does not reference the federal statute that controls. The Child Care and Development Block Grant statute states: “Payments to a State from the allotment under section 9858m of this title for any fiscal year may be obligated by the State in the fiscal year or in the succeeding fiscal year.” 42 U.S.C. § 9858h(c). The statute uses the permissive “may”. However, the federal regulations substitute the mandatory “shall”. See, 45 CFR §98.60(d)(1) (“Discretionary Fund allotments shall be obligated in the fiscal year in which funds are awarded or in the succeeding fiscal year. Unliquidated obligations as of the end of the succeeding fiscal year shall be liquidated within one year”). The mandatory nature of the federal regulations is at odds with the statutory language and arguably the federal regulations are ultra vires of the authority of ACF.

The Department also disagrees that the federal regulations provide clear authority on the issue of when federal targeted funds must be returned to the federal government. The federal regulations are murky at best and do not support the conclusion of OIG that “[s]imply transferring funds to a third party without receiving any childcare service in return is insufficient to meet Federal requirements applicable to the CCDF.” OIG cites no authority for the conclusion that there must be a receipt of childcare services. Furthermore, OIG’s conclusion is not supported by the definition of the term “obligation”.

It is provided in 45 CFR § 92.3 that “obligations means the amount of orders placed, contracts and subgrants awarded, goods and services received, and similar transactions during a given period that will require payment by the grantee during the same or a future period.” (emphasis added). See also, 45 CFR § 98.60 (an obligation may include contracts that require the payment of funds to a third party). Thus, an obligation occurs when there is a contract awarded as well as when goods or services are received. The reference to “similar transactions” also indicates that the federal regulation is not intended to be proscriptive in what can be considered an obligation, but rather is meant to provide general examples.

Nowhere in the federal regulations is there a definition of what constitutes a “liquidation” of funds. The term “unliquidated obligation” is defined at 45 CFR § 92.3 as “the amount of obligations incurred by the grantee that has not been paid.” Assuming that the definition of “liquidation” is the opposite of “unliquidated obligation”, the Department has met the definition because it has paid the Network the amount specified in the contract.

OIG dismissed the Department’s argument that state law was controlling because there “is no specific Iowa statutory definition of either “obligation” or “liquidation”. As noted above, there is no federal definition of “liquidation” either, so OIG’s argument should also be applied to federal law. Furthermore, the words obligation and liquidation are federal terms. In Iowa, that same concept is known as reversion. The federal regulations defer to controlling state law and

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applicable state law should be applied so long as it controls the availability of funds following the close of a fiscal year. There is nothing that requires a state law to use the precise terms used by the federal regulations.

In general, there is considerable deference afforded to states with respect to their Child Care and Development Block Grant programs. *See*, 45 CFR § 98.1 (goals of the program include giving each State maximum flexibility in developing child care programs and policies that best suit the needs of children and parents within the State); 45 CFR § 98.11 (lead agency has broad authority to administer program through non-governmental agencies and determine usage and priorities for expenditure of CCDF funds); 45 CFR § 98.54 (funds to be expended in accordance with applicable State law); 45 CFR § 98.67 (agency to expend and account for funds in accordance with applicable State law); 45 CFR § 98.67 (agency shall expend and account for funds in accordance with their own laws and procedures and follow state law and procedure on contracting). This same deference should also be accorded to a State's interpretation of its own laws.

The applicable Iowa law is found at Iowa Code § 8.33. Although Section 8.33 refers only to reversion of state appropriations, the statute serves the same purpose as the federal regulations in that it defines when taxpayer dollars must be returned to the government coffers. The statute states that "On August 31, or as otherwise provided in an appropriate Act, following the close of each fiscal year, all unencumbered or unobligated balances of appropriations made that fiscal term revert to the state treasury....". Iowa Code § 8.33. The term "unencumbered balance" is defined as "the unobligated balance of an appropriation after charging thereto all unpaid liabilities for goods and services and all contracts or agreements payable from an appropriation or a special fund." Iowa Code § 8.2(11). Thus, once a contractual liability is paid, the amount is no longer considered an unobligated balance.

OIG fails to reference an Iowa Attorney General Opinion that is on point. In 1979 Iowa Op. Atty. Gen. 532 (December 27, 1979), the issue was raised as to whether grants made by the Commission on Aging to local area agencies on aging should revert back to the state treasury under §8.33 when those funds had not been fully expended by the local agencies. The opinion holds that when the Commission (a state agency) gave its appropriated funds to the local agencies (non-State entities) the money was considered already spent or encumbered and was beyond the reach of the reversion statute.

The Department had contracts that obligated it to pay the federal targeted funds within a certain period of time to the Iowa Child Care and Early Education Network. Under Iowa law, those monies would be considered an obligated balance and not subject to reversion.

The Department does not dispute that it transferred the funds in question to a successor contractor after the Network's contract was terminated. The Department requests, however, that OIG acknowledge the rationale for the transfer of funds.

At the time the contract with the Network was terminated, the Department was aware that ACF was questioning whether the targeted funds had been properly obligated and liquidated. The Department determined that it would transfer the entire amount of targeted funds to be held by a

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new fiscal agent pending resolution of the matter with ACF. The Department intended to maintain the status quo and thus did not authorize expenditure of any of the transferred funds. The Department requests that OIG acknowledge that the funds were transferred with the intent that the funds be held, in their entirety, until a final determination whether the funds were required to be returned to the Federal Government.

As stated above, the Department disagrees with OIG's legal interpretation of the applicable federal regulations and state law. The Department believes that the federal regulations are inconsistent with federal law and that they do not clearly define the terms obligate and liquidate. In addition, the Department believes that applicable state law authorizes the Department's use of the federal targeted funds.

The Department recognizes, however, that deference will be afforded to ACF in its interpretation of the federal regulations. In the event that ACF agrees with the interpretation of law as set forth by OIG rather than the Department, the Department will accept the interpretation of ACF and refund \$3,156,226 to the Federal Government.

**OIG Recommendation #2:**

Remit to the Federal Government \$155,032 of interest earned on the CCDF targeted funds held by the Network for FYs 1998-2003.

**Response:**

The Department concurs with this recommendation.

The Department acknowledges that the interest earned on the targeted funds should be returned to the Federal Government. The Department's contractor earned interest on the funds it held in violation of its contract with the Department. The Iowa Attorney General's office was engaged to recover this interest. In January of 2007, the Iowa Department of Justice, Special Assistant Attorney General, issued the Network a demand letter for the interest accrued to be returned to DHS. Of the \$155,032 in interest earned over a period of five years, the Department has recovered a total of \$88,487.49. The contracting organization has dissolved and according to a cover letter with payment, the check "...represents all funds remaining in the ICCEEN account." The Department is holding these funds in a separate account.

The Department will refund the full \$155,032 to the Federal Government.

**OIG Recommendation #3:**

Ensure that the CCDF targeted funds are disbursed in accordance with Federal requirements in the future.



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**Response:**

The Department *acknowledges* this recommendation.

The Department does not *concur* with this recommendation, as we believe the obligation and liquidation of targeted funds during the audit review period met the Federal requirements. (See Response to Recommendation #1.)

However, the Department currently obligates and to the extent possible liquidates targeted funds in the Federal fiscal year in which the funds are awarded, in support of Infant and Toddler, Quality and School Age activities. If the Department is not able to fully liquidate the targeted funds in the Federal fiscal year in which the funds are awarded, the Department re-obligates them in the subsequent year and fully liquidates them by the end of the third year, in accordance with 45 CFR § 98.60(d)(1) and as interpreted by OIG in this audit. The Department will continue this approach for the obligation and liquidation of future funds. In addition, monthly expenditure reviews are conducted jointly by child care program and fiscal staff to monitor expenditures for all activities funded with targeted funds and to assure continued compliance with the requirements.

**OIG Recommendation #4:**

Review CCDF targeted funds claims for Federal reimbursement after the audit period and refund any unallowable amounts.

**Response:**

The Department concurs with this recommendation.

DHS has reviewed claims subsequent to the audit period. Targeted funds have been obligated in the Federal fiscal year awarded and have been liquidated in accordance with 45 CFR 98.60(d)(1), as interpreted by OIG in this audit.