

STATE OF MARYLAND
DEPARTMENT OF LABOR, LICENSING AND REGULATION
500 NORTH CALVERT STREET
BALTIMORE, MARYLAND 21202

AUDIT OF INDIRECT COSTS CHARGED TO
EMPLOYMENT AND TRAINING GRANTS
AWARDED BY U.S. DEPARTMENT OF LABOR
FROM JULY 1, 1995, THROUGH JUNE 30, 2000

Report No: 03-01-006-03-315

Date Issued: September 21, 2001

TICHENOR & ASSOCIATES, LLP
CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS

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**This audit report was prepared by Tichenor & Associates,
LLP, under contract to the Office of Inspector General,
and, by acceptance, it becomes a report of the Office of
Inspector General.**

**Assistant Inspector General for Audit
U.S. Department of Labor**

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EXECUTIVE SUMMARY

Tichenor & Associates, LLP, Certified Public Accountants and Management Consultants, under contract to the U.S. Department of Labor (DOL), Office of Inspector General (OIG), audited the indirect costs claimed by the Maryland Department of Labor, Licensing and Regulation (DLLR) as being applicable to grant awards from the DOL Employment and Training Administration (ETA). DLLR records show that it claimed and was reimbursed by DOL for \$50.5 million in indirect costs for the State fiscal years (FYs) ended June 30, 1996, 1997, 1998, 1999, and 2000.

Objectives

The specific objectives of this audit initially were to determine whether direct and indirect costs charged to the Unemployment Insurance (UI) program for the period October 1, 1999, through September 30, 2000 (Federal fiscal year 2000) were reasonable, allocable, and otherwise allowable under the Federal cost principles set forth in U.S. Office of Management and Budget (OMB) Circular A-87 — *Cost Principles for State, Local and Indian Tribal Governments*, and the implementing guidelines set forth in ASMB C-10 — *Cost Principles and Procedures for Developing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*. Further, the audit objectives provided that, depending on the results of our audit of direct and indirect costs charged to the UI program in Federal fiscal year 2000, the scope of the audit could be expanded to include additional years and other Federal grant programs.

Our preliminary audit of direct labor costs (the predominant direct cost) charged to the UI program did not indicate any significant problems with allowability of such costs. At the same time, our preliminary audit efforts did indicate significant problems with the allowability and allocability of claimed indirect costs, dating back to the creation of DLLR on July 1, 1995, and continuing through the completion of our fieldwork. Accordingly, we focused the balance of our audit on determining the allowability and allocability of DLLR claims for (and the recovery of) indirect costs charged to DOL grants administered by DLLR's Division of Employment and Training (DET) for FYs ended June 30, 1996, 1997, 1998, 1999, and 2000. Final cost data for FY 2001 was not available as of the completion of our fieldwork in May 2001.

Scope

Our scope of work included examining the DLLR processes for claiming and recovering indirect costs; determining the nature of the various services provided by DLLR administrative groups and the extent to which they benefitted DOL-funded programs; and evaluating the bases used to allocate costs to the various cost objectives to determine whether the allocations were based on relative benefits received. We were not engaged to, and did not, perform an audit of DLLR's total costs, the objective of which would have been the expression of an opinion on the total costs claimed by DLLR, and, accordingly, we do not express such an opinion.

Audit Results

Although OMB Circular A-87 expressly requires that indirect costs be allocated to cost objectives on the basis of “relative benefits received,” DLLR failed to comply with this requirement. Our audit disclosed that for the 5-year period ended June 30, 2000, DLLR billed and received a total of \$50,523,999 in indirect costs from DOL; however, DLLR’s actual allowable indirect costs properly allocable to DOL grant awards on the basis of “relative benefits received” totaled only \$40,690,940 during this period. In short, DLLR over-charged DOL grant awards a total of \$9,833,059 in indirect costs during this 5-year period. The following schedule summarizes DLLR’s claimed indirect costs, allowable indirect costs, indirect costs recovered from DOL, and any over/under-recovery of indirect costs from DOL for the 5-year period covered by our audit.

(Thousands of dollars)

Description	1996	1997	1998	1999	2000	Total
Claimed Indirect Costs	\$13,669	\$13,490	\$14,475	\$14,999	\$16,463	\$73,096
Questioned Indirect Costs	3,664	3,214	3,698	4,015	4,256	18,847
Allowable DLLR Indirect Costs	10,006	10,276	10,777	10,984	12,207	54,250
Indirect Costs Allocable to DOL/ETA Grants	7,584	7,733	8,144	8,064	9,166	40,691
Indirect Costs Paid by DOL/ETA	10,044	10,316	9,340	10,162	10,662	50,524
Over Recovery from DOL/ETA	\$2,460	\$2,583	\$1,196	\$2,098	\$1,496	\$9,833

Note: A more detailed version is included in the Exhibit at the end of this report. Totals may not foot due to rounding.

Based on our audit, we questioned a total of \$9,833,059 in indirect costs claimed and recovered by DLLR on DOL/ETA grant awards during the 5-year period ended June 30, 2000, primarily because:

- Over \$18.8 million in DLLR support function costs were improperly included in its indirect cost pools, and allocated to DOL grant awards. These costs should have been direct-charged to non-Federal cost objectives. [Note: Some of these questioned costs could have been direct-charged to DOL grant awards (e.g., certain legal services) or included in the indirect cost pool (e.g., certain data processing services) had the employees who performed these services maintained the personnel activity reports required to support these costs, as mandated by OMB Circular A-87. However, because this was not done, these costs are unallowable.]
- The allocation base used by DLLR to distribute its indirect costs to its five operating units was flawed because of inconsistent treatment of similar employees between Federal and State programs. This resulted in DOL/ETA grant awards being allocated more than their fair share of the DLLR indirect cost pool.

- State central services costs included in the State-wide Cost Allocation Plan (SWCAP) included Y2K costs which should have been capitalized. Although DLLR excluded those SWCAP costs clearly identified as Y2K costs from its indirect cost proposals, our review indicated that other Y2K costs (not expressly identified as such) may also have been included in the SWCAP.
- The wage base used by DLLR to compute DET indirect cost rates differed from the wage base used to recover indirect costs on the various DOL grant awards. Assuming all other factors being equal, this would cause DLLR to under-recover its indirect costs.

It is obvious from our audit that DLLR has failed to establish adequate internal control policies and procedures to ensure compliance with the cost principles mandated by OMB Circular A-87. Specifically, we observed that Office of Budget and Fiscal Services personnel did not have an adequate working knowledge of the Federal cost principles mandated by OMB Circular A-87. In addition, since DLLR was created effective July 1, 1995, its Office of Program Analysis and Audit has not conducted any audits of (1) DLLR's indirect costs and/or its indirect cost rate proposals to determine whether they were in compliance with Federal cost principles, and (2) DLLR payroll costs to determine whether they were properly supported by personnel activity reports as required by OMB Circular A-87.

The net effect of the matters summarized above resulted in a substantial shifting of costs from DLLR's State programs (to which such costs were properly allocable) to DOL grant awards in DET which resulted in a significant over-recovery of indirect costs on the DOL/ETA grant awards. Finally, we expect that a similar over-recovery of indirect costs on DOL/ETA grant awards will also occur in FY 2001 because the "conditions" discussed above had not changed as of the completion of our fieldwork in May 2001.

Recommendations

We made several recommendations in the body of the report to DOL/ETA officials. In brief, we are recommending that the cognizant DOL/ETA grant officer(s) direct DLLR to refund the \$9.8 million in indirect costs which it over-recovered for FYs 1996, 1997, 1998, 1999, and 2000, and to adjust its billings to DOL for FY 2001 to preclude further over-recoveries of indirect costs attributable to the findings in this report.

In addition, we are recommending that the DOL Assistant Secretary of Employment and Training direct DLLR to develop and implement internal control policies and procedures to ensure that its indirect cost rate proposals fully comply with the Federal cost principles mandated by OMB Circular A-87, to provide comprehensive training to key personnel within DLLR's Office of Budget and Fiscal Services to ensure that they have an adequate working knowledge of OMB Circular A-87, and to include a provision in its annual audit plans for periodic audit of its indirect cost rate proposals and payroll costs to ensure compliance with the applicable provisions of OMB Circular A-87.

Auditee's Response

We held an exit conference with DLLR officials on May 22, 2001, in which we presented a summary of our findings. They reserved comment on the findings pending receipt of our draft audit report. However, they did request access to certain of our work papers to determine the source of the data we used and to gain an understanding of analytical data we presented. At DLLR's request, we met with several key DLLR officials and provided them with copies of relevant work papers prior to our departure from the audit site.

In their response to our draft report, DLLR officials disagreed with virtually all of our findings and recommendations, and concluded that DLLR had not over recovered its indirect costs and, therefore, did not owe a refund to DOL. Among other things, DLLR stated the methodology used in the audit process was flawed in that: (1) it assumed conditions not required by the Award; (2) the sampling methods employed were insufficient and inapplicable; and (3) the auditors applied "suggested bases" as though their use were mandatory for certain items.

We have incorporated DLLR's detailed comments at the end of each finding, as appropriate. In addition, a copy of DLLR's written response is included, in its entirety, as an appendix to this report.

Auditor's Conclusion

DLLR's written response did not provide any new or compelling evidence which would warrant any change in the findings, conclusions, and recommendations presented in our draft report.

Further, DLLR's response did not address the critical Federal cost principles expressly cited in our report as the basis for our findings, including: (1) the requirement that costs must be allocated to cost objectives in accordance with "relative benefits received;" (2) the requirement that costs must be "accorded consistent treatment" to be allowable; and (3) the requirement that all salaries and wages (and all directly associated costs) of employees who work on multiple direct and/or indirect cost objectives must be supported by personnel activity reports which must meet the criteria mandated in OMB Circular A-87 in order to be allowable. Accordingly, we consider DLLR's response to be generally unresponsive to the findings presented in the draft report.

In summary, all the recommendations are considered unresolved and will be addressed in ETA's formal resolution process.

ACRONYMS AND GLOSSARY

ADP/IT	Automatic data processing/information technology
BLS	U. S. Department of Labor, Bureau of Labor Statistics
CFR	Code of Federal Regulations
CPA	Certified Public Accountant
DBM	Maryland's Department of Budget and Management
DET	Maryland Department of Labor, Licensing and Regulation, Division of Employment and Training
DLLR	Maryland Department of Labor, Licensing and Regulation
DOL	U.S. Department of Labor
ETA	U.S. Department of Labor, Employment and Training Administration
FY	State fiscal year - July 1 to June 30
OAG	Maryland Department of Labor, Licensing and Regulation, Office of the Attorney General
OCD	U.S. Department of Labor, Office of Cost Determination
OIG	U.S. Department of Labor, Office of Inspector General
OIM	Maryland Department of Labor, Licensing and Regulation, Office of Information Management
OIT	Maryland Department of Labor, Licensing and Regulation, Division of Employment and Training, Office of Information Technology
OMB	U.S. Office of Management and Budget
OSHA	Occupational Safety and Health Act
SWCAP	State-wide Cost Allocation Plan
UI	Unemployment Insurance

GLOSSARY

- Direct Cost:** A cost that can be identified specifically with a particular cost objective, e.g., the DOL Unemployment Insurance Program.
- Indirect Cost:** A cost which cannot be identified with a single, final cost objective, but is identified with two or more final cost objectives, one or more of which benefits Federal programs. Such costs are combined into groupings or pools for distribution to benefitting final cost objectives. Indirect cost pools should be distributed to benefitted cost objectives on bases that will produce an equitable result in consideration of relative benefits derived.
- Questioned Cost:** A cost that is questioned because of:
- (a) an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds; or
 - (b) at the time of the audit, such cost is not supported by adequate documentation; or
 - (c) the expenditure of funds for the intended purpose is unnecessary or unreasonable.
- Allowable Cost:** To be allowable under Federal awards, costs must, among other things, meet the following general criteria: (1) be reasonable and necessary for proper and efficient performance and administration of Federal awards; (2) be allocable to Federal awards in accordance with OMB Circular A-87; (3) be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities of the governmental unit; (4) be accorded consistent treatment (e.g., a cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost); (5) except as otherwise provided for in OMB Circular A-87, be determined in accordance with generally accepted accounting principles; (6) be the net of all applicable credits; and finally, (7) be adequately documented.
- Allocable Cost:** A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with “relative benefits received.”

INTRODUCTION

BACKGROUND

The Maryland Department of Labor, Licensing and Regulation (DLLR) was formed on July 1, 1995, by combining the Department of Licensing and Regulation with the Employment component of the Department of Economic and Employment Development.

At the time of our audit, DLLR consisted of five operating units and several supporting groups. For the State fiscal year ended June 30, 2000, DLLR reported expenditures of over \$166.6 million, and employed 2,071 people. The operating unit that administers the U.S. Department of Labor (DOL) grants — the Division of Employment and Training (DET) — was, by far, the largest unit within DLLR with expenditures of \$116.4 million and 1,394 employees. A brief discussion of the various DLLR operating units follows.

Division of Employment and Training

This division develops and maintains Maryland's workforce by training, assisting in job searches, providing unemployment insurance compensation, and reporting on the needs and demands of the labor market. The major DOL programs within this division include Unemployment Insurance (UI), Welfare to Work (WtW), Job Services (JS), Job Training Partnership Act (JTPA), Elderly Disabled Worker Assistance Act (EDWAA), and the Russian Immigrants Program.

The Office of Labor Market Analysis and Information within DET operates several programs designed to collect, assemble, and report data related to various aspects of labor market conditions. The program is carried out in cooperation with the DOL Employment and Training Administration (ETA) and DOL's Bureau of Labor Statistics (BLS).

Division of Financial Regulation

The Division of Financial Regulation regulates the operation of Maryland's state-chartered banks and credit unions, consumer loan companies, sales finance companies, mortgage companies and collection agencies.

Division of Labor and Industry

This division protects and promotes the health, safety, and employment rights of Maryland citizens. Major components of the division's mission include preventing job-related accidents and incidents which result in fatalities and injuries; protecting employee wages and rights; overseeing safety inspection programs for amusement rides, railroads, elevators, boilers, and pressure vessels;

assisting regulated industries and employers in complying with state laws and regulations; and, promoting industry sponsorship of occupational training for the skilled trades and crafts.

Maryland Racing Commission

The Racing Commission, which operates the same as a division, oversees and regulates both the harness and thoroughbred horse racing industry in the state. All participants, from the track itself to the jockeys to the concessionaires who provide food and drink at the racetrack, are licensed by the Racing Commission. The commission ensures proper distribution of wagering dollars, regularly reviews the financial statements of the racing associations, and operates its own lab to test for drugs in horses to maintain the integrity of the sport.

Division of Occupational and Professional Licensing

The Division of Occupational and Professional Licensing protects the public by setting minimum levels of competency for numerous occupations and professions. It accomplishes this through examinations, licensing, and the adjudication of consumer complaints. Professional and consumer members are appointed to the various boards and commissions and serve on a part-time basis. Administrative and clerical support is provided by DLLR. The numerous boards and commissions include, among others, the State Athletic Commission, the State Commission of Real Estate Appraisers, the State Board of Architects, the State Board of Cosmetologists, the State Board of Master Electricians, and the State Board of Public Accountancy.

* * * * *

DLLR annually prepares and submits to DOL's Office of Cost Determination (OCD) an indirect cost rate proposal for the various DOL grant awards administered by DET. In preparing its proposal, DLLR accumulates the total costs of its administrative and support groups (Office of the Secretary, Office of Budget and Fiscal Services, Office of Personnel and Training, Office of the Attorney General, Office of Information Management, and General Services) which provide support services to each of the five operating units described above into a cost pool, and adds the DLLR portion of the Maryland State-wide Cost Allocation Plan (SWCAP). The SWCAP is used to allocate the costs of various State central services to all departments and agencies within the State. These pooled costs are then allocated to the DLLR operating units based on the employee count within each unit in relation to the total employee count for all operating units.

The administrative costs for operating DET (i.e., the Office of Assistant Secretary, Division of Employment and Training) are added to the DLLR pool costs allocated to DET to determine DET's total indirect cost pool. The total DET indirect cost pool is then divided by the total DET direct labor cost base to determine the proposed indirect cost rate submitted to DOL/OCD for review and approval. The proposal is finalized through negotiations with DOL/OCD, and the "fixed" negotiated/approved rate is then supposed to be used to charge and recover indirect costs applicable to DOL grants. However, the negotiated/approved indirect cost rate agreements are based on estimated costs to be incurred, and the agreements are subject to audit.

In response to our inquiries, DOL/OCD officials stated that they had repeatedly expressed concerns about the methodology being used by DLLR in preparing its indirect cost rate proposals since the inception of the agency in 1995.

OBJECTIVES AND SCOPE

Our initial objectives were to conduct an audit of direct and indirect costs charged to the Unemployment Insurance (UI) program for the period October 1, 1999, through September 30, 2000 (Federal fiscal year 2000), to determine whether such costs were reasonable, allocable, and otherwise allowable under the Federal cost principles set forth in OMB Circular A-87 — *Cost Principles for State, Local and Indian Tribal Governments*, and the implementing guidelines set forth in ASMB C-10 — *Cost Principles and Procedures for Establishing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*. Further, the audit objectives provided that, depending on the results of our audit of direct and indirect costs charged to the UI program in Federal fiscal year 2000, the scope of the audit could be expanded to include additional years and other Federal grant programs.

Our preliminary audit of direct labor costs (the predominant direct cost) charged to the UI grant program did not indicate any significant problems with the allowability of such costs. At the same time, our preliminary results indicated potential significant problems with the allowability of indirect costs beginning with the reorganization of DLLR on July 1, 1995, and continuing to the present time. Accordingly, the primary focus of our audit was on the DLLR claims for and recovery of indirect costs applicable to DOL grants administered by DET for the State fiscal year ended June 30, 1996, 1997, 1998, 1999, and 2000.

The primary objectives of our audit were to examine the DLLR processes for claiming and recovering indirect costs to determine the allowability and allocability of (1) the services provided by the DLLR administrative groups for the benefit of federally-funded programs, (2) the expenses included in each center, and (3) the methods used to allocate these indirect costs to operating units. The objectives of this review pertained solely to the indirect costs applicable to and recovered under DOL/ETA grant awards. We were not engaged to, and did not, perform an audit of DLLR's total costs, the objective of which would have been the expression of an opinion on the total costs claimed by DLLR, and, accordingly, we do not express such an opinion.

Under Federal cost reimbursement principles, only actual incurred costs are allowable — budget estimates are not allowable. However, when actual costs are not readily available, the Federal cost principles permit the use of budget estimates for billing purposes on the condition that the claimed costs are adjusted to actual allowable costs at least annually. For example, the indirect cost rate proposals submitted by DLLR to DOL's OCD were based on budget estimates which provide a basis for negotiating "fixed" indirect cost rates for billing purposes and, theoretically, are adjusted to actual costs through the use of "carry-overs" of its over/under-recovery of indirect costs from the preceding year. As previously stated, the negotiated indirect cost rate agreements provide that DLLR's recovery of indirect costs using these "fixed" indirect costs are subject to audit.

We used actual costs in calculating DLLR's allowable indirect costs for FYs 1996, 1997, 1998, 1999, and 2000. In addition, we used the same, simplified, "one-step" allocation methodology used by DLLR in allocating its indirect cost principles to its various cost objectives.

This engagement was performed in accordance with auditing standards established by the American Institute of Certified Public Accountants, and with the *Government Auditing Standards* (1994 Revision) issued by the Comptroller General of the United States, except that the scope of our engagement did not include expressing a formal written opinion on the reasonableness and allowability of the total claimed costs by DLLR, its system of internal controls, or its compliance with laws and regulations applicable to all Federal grants/contracts.

Our audit fieldwork was performed at DLLR offices in Baltimore, Maryland, primarily during the period January 8, 2001, through May 24, 2001. An entrance conference was held on October 31, 2000, with the Deputy Secretary of DLLR and various other DLLR officials. However, the actual start of our detailed audit of indirect costs was delayed until January 8, 2001. An exit conference was held on May 22, 2001, with the Secretary of DLLR and various other DLLR officials.

FEDERAL COST REIMBURSEMENT PRINCIPLES

The DOL grants awarded to DLLR provide for payment of allowable, reasonable, and allocable incurred costs as determined by OMB Circular A-87. In addition to Circular A-87, the grant award and the "Common Rule" (as implemented by DOL at 29 CFR § 95) governing grants to State and local governments, contain a number of compliance requirements which must be met in order for costs to be allowable. Among other things, the costs must be in accordance with generally accepted accounting principles, and the grant accounting records must be supported by adequate source documentation such as canceled checks, paid bills, payroll records, time and attendance records, contract and subcontract award documents, etc.

General Principles for Determining Allowable Costs

Attachment A to OMB Circular A-87 establishes general principles for determining allowable costs, both direct and indirect, incurred by state, local, and Indian tribal governments under grants, cost-reimbursement contracts, and other agreements with Federal agencies. The principles are established for the purpose of determining the reasonableness, allowability, and allocability of costs claimed, and are not intended to dictate the extent of Federal or contractor/grantee participation in the financing of a particular program or project. Accordingly, they describe what may be reimbursed or recovered under a Federal award. The principles are designed to ensure that the Federal Government bears its fair share of costs incurred, except where specifically restricted or prohibited by law.

Under OMB Circular A-87, costs charged to Federal programs must meet the tests of allowability, reasonableness, and allocability. To be **allowable**, costs must meet the following general criteria:

- Be necessary and reasonable for proper and efficient performance and administration of Federal awards.
- Be allocable to Federal awards under the Circular (e.g., on the basis of relative benefits received).
- Be authorized (or not prohibited) under state or local laws and regulations.
- Conform to any limitations or exclusions set forth in these principles, Federal laws, the terms and conditions of the Federal award, or any other governing regulations as to types and/or amounts of cost items.
- Be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities/programs of the governmental unit.
- Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost. Similarly, a cost may not be allocated to a Federal award as an indirect cost if any other cost incurred for the same purpose in like circumstances has been charged to the award as a direct cost.
- Except as otherwise provided for in the Circular, costs must be determined in accordance with generally accepted accounting principles.
- Not be included as a cost used to meet cost sharing or matching requirements of any other Federal award in either the current or a prior period, except as specifically provided by Federal law or regulation.
- Be the net of all applicable credits.
- Be adequately documented.

A cost may be considered reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the costs. The question of reasonableness is particularly important when governmental units or components are predominantly federally funded. In determining **reasonableness** of a given cost, consideration will be given to:

- Whether the cost is of a type generally recognized as ordinary and necessary for the operations of the governmental unit or the performance of the Federal award.
- The restraints or requirements imposed by such factors as sound business practices; arms-length bargaining; Federal, state, and other laws and regulations; and, terms and conditions of the Federal award.
- Market prices for comparable goods or services.
- Whether the individuals concerned acted with prudence in the circumstances considering their responsibilities to the governmental unit, its employees, the public at large, and the Federal Government.
- Significant deviations from the established practices of the governmental unit which may unjustifiably increase the Federal award's cost.

The basic guidelines for costs to be **allocable** are briefly summarized, as follows:

- A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with the “relative benefits received.”
- All activities which benefit from the governmental unit’s indirect costs, including unallowable activities and services donated to the governmental unit by third parties, will receive an appropriate allocation of the indirect costs.
- Any cost allocable to a particular Federal award or cost objective under the principles provided for in this Circular may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by law or terms of the Federal awards, or for other reasons. However, this prohibition would not preclude governmental units from shifting costs that are allowable under two or more awards in accordance with existing program agreements.
- Where an accumulation of indirect costs will ultimately result in charges to a Federal award, an approved cost allocation plan and/or an approved indirect cost rate agreement will be required as described in Attachments C, D, and E of A-87.

OMB Circular A-87 mandates that the U.S. Department of Health and Human Services (HHS) issue implementing guidelines for A-87 on behalf of the entire Federal Government. HHS has developed and issued these guidelines in ASMB C10 — *Cost Principles and Procedures for Establishing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*. These additional guidelines include discussions of the requirements for preparing and submitting cost allocation plans, public assistance cost allocation plans, and state and local indirect cost rate proposals. In addition, these guidelines address types of indirect cost rates, acceptable methodologies for indirect cost rate determinations, allocation bases, special rates, the submission and documentation of indirect cost rate proposals, the review/negotiation/approval of indirect cost rates, etc.

Specific Principles for Determining Allowability of Selected Items of Cost

Attachment B to OMB Circular A-87 provides specific principles to be applied in determining the allowability or unallowability of selected items of costs. These principles apply whether a cost is treated as direct or indirect. For the purposes of this audit, the single most important principle in this section of A-87 is Attachment B, paragraph 11.h. — *Support for salaries and wages* — which states, among other things:

(3) Where employees are expected to work solely on a single Federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications will be prepared at least semi-annually and will be signed by the employee or supervisory official having first hand knowledge of the work performed by the employee.

(4) Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation Such documentary support will be required where employees work on:

- (a) More than one Federal award,*
- (b) A Federal award and a non-Federal award,*
- (c) An indirect cost activity and a direct cost activity,*
- (d) Two or more indirect activities which are allocated using different allocation bases,
or*
- (e) An unallowable activity and a direct or indirect cost activity.*

(5) Personnel activity reports or equivalent documentation must meet the following standards:

- (a) They must reflect an after-the-fact distribution of the actual activity of each employee,*
- (b) They must account for the total activity for which each employee is compensated,*
- (c) They must be prepared at least monthly and must coincide with one or more pay periods, and*
- (d) They must be signed by the employee.*
- (e) Budget estimates or other distribution percentages determined before the services are performed do not qualify as support for charges to Federal awards*

Internal Control Standards

Internal control standards issued by the U.S. General Accounting Office establish minimum acceptable levels of quality control systems for Federal programs and activities. Some of the specific standards include:

- **Documentation.** All transactions and other significant events are to be clearly documented, and the documentation are to be readily available for examination. Such documentation should be complete and accurate and should facilitate tracing the transaction or event and related information from before it occurs, while it is in process, until after it is completed.

- **Recording of Transactions and Events.** Transactions and other significant events are to be promptly recorded and properly classified. This standard applies to (1) the entire process or life cycle of a transaction or significant event and includes the initiation and authorization, (2) all aspects of the transaction or event while in process, and (3) its final classification in summary records.
- **Execution of Transactions and Events.** Transactions and other significant events are to be authorized and executed only by persons acting within the scope of their authority.

FINDINGS

Although OMB Circular A-87 expressly requires that indirect costs be allocated out to cost objectives on the basis of “relative benefits received,” DLLR failed to comply with this requirement. Our audit disclosed that for the 5-year period ended June 30, 2000, DLLR billed and received a total of \$50,523,999 in indirect costs from DOL; however, DLLR’s actual allowable indirect costs properly allocable to DOL grant awards on the basis of “relative benefits received” totaled only \$40,690,940 during this period. In short, DLLR over-charged DOL grant awards a total of \$9,833,059 in indirect costs during this 5-year period. The following schedule summarizes DLLR’s claimed indirect costs, allowable indirect costs, indirect costs recovered from DOL, and any over/under-recovery of indirect costs from DOL for the 5-year period covered by our audit.

(Thousands of dollars)

Description	1996	1997	1998	1999	2000	Total
Claimed Indirect Costs	\$13,669	\$13,490	\$14,475	\$14,999	\$16,463	\$73,096
Questioned Indirect Costs	3,664	3,214	3,698	4,015	4,256	18,847
Allowable DLLR Indirect Costs	10,006	10,276	10,777	10,984	12,207	54,250
Indirect Costs Allocable to DOL/ETA Grants	7,584	7,733	8,144	8,064	9,166	40,691
Indirect Costs Paid by DOL/ETA	10,044	10,316	9,340	10,162	10,662	50,524
Over-Recovery from DOL/ETA	\$2,460	\$2,583	\$1,196	\$2,098	\$1,496	\$9,833

Note: A more detailed version is included in the Exhibit at the end of this report. Totals may not foot due to rounding.

Based on our audit, we questioned a total of \$9,833,059 in indirect costs claimed and recovered by DLLR on DOL/ETA grant awards during the 5-year period ended June 30, 2000, primarily because:

1. Over \$18.8 million in DLLR support function costs were improperly included in its indirect cost pools, and allocated to DOL grant awards. These costs should have been direct-charged to non-Federal cost objectives. [Note: Some of these questioned costs could have been direct-charged to DOL grant awards (e.g., certain legal services) or included in the indirect cost pool (e.g., certain data processing services) had the employees who performed these services maintained the personnel activity reports required to support these costs, as mandated by OMB Circular A-87. However, because this was not done, these costs are unallowable.]

2. The allocation base used by DLLR to distribute its indirect costs to its five operating units was flawed because of inconsistent treatment of similar employees between Federal and State programs. This resulted in DOL/ETA grant awards being allocated more than their fair share of the DLLR indirect cost pool.
3. State central services costs included in the SWCAP included Y2K costs which should have been capitalized. Although DLLR excluded those SWCAP costs clearly identified as Y2K costs from its indirect cost proposals, our review indicated that other Y2K costs (not expressly identified as such) may also have been included in the SWCAP.
4. The wage base used by DLLR to compute DET indirect cost rates differed from the wage base used to recover indirect costs on the various DOL grant awards. Assuming all other factors being equal, this would cause DLLR to under-recover its indirect costs.

The net effect of the matters summarized above was a substantial shifting of costs from DLLR's State programs (to which such costs were properly allocable) to DOL grant awards in DET with the result of a significant over-recovery of indirect costs on the DOL/ETA grant awards.

Further, we expect that a similar over-recovery of indirect costs on DOL/ETA grant awards will also occur in FY 2001 because the conditions discussed above had not changed as of the completion of our fieldwork in May 2001.

In their response to our draft report, DLLR officials disagreed with most of our findings. We have incorporated DLLR's comments at the end of each finding, along with our conclusion. In addition, a copy of DLLR's written response is included, in its entirety, as an appendix to this report.

The detailed results of our review are presented in the individual findings on the following pages of this report.

FINDING 1. Certain DLLR Support Function Costs were Improperly Included in Indirect Cost Pool and Allocated to DOL Grant Awards on Basis Other Than “Relative Benefits Received”

Our audit disclosed, and a recent internal DLLR study confirmed, that a substantial portion of the costs/effort expended by certain DLLR support groups under the Office of the Secretary — e.g., the Office of the Attorney General (OAG), the Office of Information Management (OIM), and Executive Direction — primarily benefitted non-DET programs (mostly State programs), and should have been excluded from the DLLR indirect cost pools during the 5 years covered by our audit. However, these costs were included in their entirety in DLLR’s indirect cost pool of which about 75 percent was allocated to DET on a basis other than “relative benefits received,” and eventually recovered under DOL grants.

The following table summarizes by year (1) DLLR’s actual incurred costs for each support unit which it normally included in its indirect cost pool; (2) the amounts we questioned based on our audit findings; and (3) DLLR’s actual allowable indirect cost pool amounts.

DLLR INDIRECT COST POOL BY GROUP

DLLR Group	1996	1997	1998	1999	2000	Total
Exec. Direction	\$1,396,037	\$2,084,914	\$2,019,690	\$2,289,656	\$2,745,975	\$10,536,272
Budget and Fiscal	\$2,111,613	\$1,785,168	\$1,902,522	\$2,004,590	\$2,040,525	\$9,844,418
General Services	\$4,650,250	\$4,751,889	\$4,599,596	\$4,296,189	\$5,064,170	\$23,362,094
Attorney General	\$1,904,988	\$1,825,213	\$1,820,689	\$1,937,779	\$1,995,925	\$9,484,594
Information Mgmt	\$1,409,557	\$867,905	\$1,372,656	\$1,504,819	\$1,572,939	\$6,727,876
Personnel and Training	\$906,878	\$1,069,343	\$1,488,626	\$1,626,964	\$1,624,976	\$6,716,787
Total Pool Allocated	\$12,379,323	\$12,384,432	\$13,203,779	\$13,659,997	\$15,044,510	\$66,672,041
Costs Questioned:						
Exec. Direction	\$349,009	\$521,229	\$504,923	\$572,414	\$686,494	\$2,634,069
Attorney General	\$1,904,988	\$1,825,213	\$1,820,689	\$1,937,779	\$1,995,925	\$9,484,594
Information Mgmt	\$1,409,557	\$867,905	\$1,372,656	\$1,504,819	\$1,572,939	\$6,727,876
Total Costs Questioned	\$3,663,554	\$3,214,347	\$3,698,268	\$4,015,012	\$4,255,358	\$18,846,539
Allowable Costs*	\$8,715,769	\$9,170,085	\$9,505,511	\$9,644,985	\$10,789,152	\$47,825,502

*Total Pool Allocated minus Total Costs Questioned = Allowable Costs

As previously discussed in this report, OMB Circular A-87 requires that indirect costs be allocated to cost objectives on the basis of “relative benefits received.” In addition, the implementation guide for OMB Circular A-87 recommends that legal services (such as those provided by OAG) be charged/allocated based on “direct hours,” i.e., treated as direct rather than indirect costs. These same guidelines also recommend that data processing services (such as those provided by OIM) be direct-charged based on “system usage” rather than being treated as an indirect cost. However, our audit disclosed that DLLR failed to comply with these Federal cost principles. The net effect of DLLR’s non-compliance with these Federal cost principles is that substantial costs were improperly shifted to DOL grant awards. These costs were properly chargeable/allocable to DLLR’s State programs, as discussed below.

**A. OAG Costs Were Not Allocated to Users
on the Basis of Relative Benefits Received**

Our review of the indirect cost proposals submitted by DLLR for the 5 fiscal years ended June 30, 1996, through 2000 concluded that the DLLR indirect cost pools contained about \$9.5 million in OAG costs. The DLLR indirect costs pools were subsequently allocated to DLLR’s operating units, including DET which is primarily responsible for administering DOL/ETA grants. The allocations were based on annual employee counts for each operating unit. Since DET employed about 75 percent of all employees within the operating units, DET was allocated about 75 percent of the OAG costs in the pool. However, as discussed below, only about 22 percent of the OAG effort directly benefitted DOL/ETA grant awards administered by DET.

During discussions with various DLLR employees, we learned that a significant portion of OAG’s legal workload involved the handling/processing of appeals for DLLR’s Division of Professional and Occupational Licensing, while very little legal work was performed for DET. In following up on this information, we obtained supporting documentation for a DLLR internal study performed during the latter part of calendar year 2000. The internal study contained an analysis of each employee’s workload for all persons working in the DLLR Office of the Secretary, including OAG employees.

According to the DLLR study, only about 22 percent of OAG’s effort directly benefitted DOL/ETA grant awards administered by DET, while the remaining 78 percent of OAG’s effort directly benefitted DLLR’s non-DET programs (mostly State programs). In response to our questions, DLLR’s principal counsel stated that she and her assistant met with each OAG attorney to talk about how his or her time was divided between Federal and non-Federal projects, and the percentage of time spent on each. Based on these discussions, OAG notified DLLR about the allocation of each of its staff member’s time between DET, Occupational Safety and Health Act (OSHA) programs (not addressed in this report), and non-Federal (State) programs. She informed us that the 2000 data was fairly representative of the efforts of OAG for the past 5 years. In response to our questions, she stated that no time cards or other payroll distribution records were prepared by or required of OAG employees.

OAG performs a variety of legal services for the various units within DLLR. These services include, among other things, interpreting regulations, preparing and reviewing contracts, handling appeals against DLLR, and representing DLLR in all cases before the circuit court. It is our understanding that OAG has only limited involvement in UI appeals until the appeals reach the circuit court because DET has its own appeals board. The other DLLR units, such as Financial Regulation and Occupational and Professional Licensing, rely heavily upon OAG for handling their appeals.

Our analysis of supporting documentation for the DLLR's internal study of OAG determined that about 22 percent of OAG's time was spent on behalf of DET (primarily in support of DOL/ETA grant awards). Another 11 percent of OAG's time was spent on behalf of Maryland's Occupational Safety and Health programs (a combination of both State and Federal OSHA programs) which were not addressed in our audit.

While the OAG data may not be precise and completely accurate, we believe it clearly demonstrates that DLLR's annual employee counts are not an acceptable base for allocating OAG costs to operating units on the basis of "relative benefits received," as required by OMB Circular A-87. To the contrary, DLLR's use of employee counts as an allocation base for OAG costs has resulted in shifting a significant amount of DLLR's support function costs from its various State programs (to which the costs were properly allocable) to DOL/ETA grant awards in violation of the Federal cost principles set forth in A-87.

Further, DLLR's legal costs should have been charged as direct costs to the benefitting cost objectives rather than being included in DLLR's indirect cost pool. More specifically, the implementation guide for OMB Circular A-87 recommends that legal services be charged/allocated based on "direct hours" (i.e., treated as a direct cost rather than an indirect cost). Accordingly, we have excluded all OAG costs — totaling about \$9.5 million — from the DLLR indirect cost pools for FYs 1996, 1997, 1998, 1999, and 2000.

Finally, assuming that the recent DLLR internal study were valid, about 22 percent of OAG's costs could have been charged to DOL/ETA grant awards as direct costs had the OAG employees maintained personnel activity reports or equivalent documentation which met the detailed documentation standards set forth in OMB Circular A-87, Attachment B, paragraph 11.h., subsection (5), which must be met in order to support claimed salaries and wages (and all directly associated non-personnel costs). However, as previously discussed, DLLR's principal counsel acknowledged that no personnel activity reports or other equivalent documents were prepared by or otherwise required of OAG employees.

Accordingly, the costs of any OAG legal services which may have been rendered to DET are unallowable as direct costs because they do not meet the minimum "documentation" standards mandated by Federal cost principles and the internal control standards issued by the U.S. General Accounting Office.

Auditee's Response

In their response to our draft report, DLLR officials in part stated:

According to the audit, all Office of the Attorney General (OAG) costs were included in the indirect cost pool and then allocated to the operating units based on the annual employee counts for each operating unit. This meant that DET, with 75 percent of the employee count, was allocated 75 percent of the OAG costs. The Auditors believe that this percentage should have been 22 percent. After acknowledging that some level of legal services were provided, the Auditors disallowed all OAG costs based on the recommendation in A-87 that legal costs be direct billed.

DLLR notes that when DET was merged into the Department of Licensing and Regulation (DLR) to create DLLR, six OAG positions were added to the existing staff as a result of the work which was transferred. This included four attorneys, one serving as counsel to DET, and three handling Unemployment Insurance (UI) appeals. The other positions were a secretary working for the four attorneys, and a paralegal who prepared the extensive documents which need to be filed with the court in each appeal.

One of the attorney positions was contractual, and was not filled after 1998. The other five positions are still principally devoted to the work of the Division of Employment and Training, which is reflected in the State job description forms, MS 22's, for each employee. In order to have more flexibility in assigning work to attorneys in the office, and as a way of attracting qualified applicants to a more diverse mix of job responsibilities, OAG has in the past several years divided up some of the appeals work so that there are now five attorneys handling appeals to Circuit Court in UI cases in addition to other cases from the Maryland Occupational Safety and Health (MOSH) program and the Division of Occupational and Professional Licensing. The sum of the time dedicated to the UI work is at least equal to, and probably slightly greater than, the work of two attorneys dedicated solely to UI appeals. The spreading of UI work to a wider pool of attorneys has also led to an increased number of support staff handling UI work for these attorneys. Instead of one secretary doing all of the UI support work, there are three secretaries doing part of this job.

In addition to the line attorneys, Principle Counsel and Deputy Counsel spend a significant portion of their time on DET matters, both as supervisors, and in direct legal service. Personnel matters, procurement issues, and significant UI questions such as the increasing characterization of employees as independent contractors are examples of the kind of legal work that has demanded the close attention of Principal Counsel and Deputy Counsel.

The characterization of this level of involvement by a staff of approximately 30 individuals as "very little legal work" being performed for DET is wrong, unfair, and misleading. The lack of understanding of the nature of the work done by the OAG is shown in the comparison set forth of the OAG's involvement in UI appeals as opposed to that in other DLLR units. The draft report states that OAG has limited involvement in UI appeals because DET has its own appeals board

while other units rely heavily on OAG for handling their appeals. In fact, the role of the board of appeals is very similar to that of the OAH [Office of Administrative Hearings] and the boards and commissions in the other parts of the Department. All render final decisions which may be appealed to the Circuit Court, and all of those appeals are handled by the OAG.

The bottom line of the audit with regard to OAG is that all costs for this office have been excluded and disallowed, without regard to the fact that the services were rendered to DET. This decision is based on a recommendation in A-87 that legal services be charged/allocated based on direct charges.

This is a misguided and erroneous result for several reasons. First, OAG costs have been part of the indirect cost pool since the merger of the departments, and no questions have been raised by DOL about this method of accounting during that time period. In fact, that is probably the most appropriate way of handling the costs given the diverse case assignments of many of the attorneys in the office, including both the Principle [sic] Counsel and Deputy Counsel. Second, the language of A-87 is only a recommendation, not a requirement. If, after these costs have been incurred, DOL wants to recommend that the method of accounting be changed, the change should be prospective, not retroactive. It is wrong to punish the Department by disallowing legitimate costs based on a recommendation. Third, the audit does not question that OAG performed legal work for DET during the time of the audit. Disallowance of all of the costs for this work would be in total disregard of this reality.

Auditor's Conclusion

DLLR's written response did not provide any new or compelling evidence which would warrant any change in this finding, nor the related conclusions and recommendations.

First, the number of positions added to OAG when DET was merged into DLR (DLLR's predecessor agency), and the State job description forms for these positions, are completely irrelevant to this finding and do not meet the mandatory requirements set forth in OMB Circular A-87, Attachment B, paragraph 11.h. for supporting salaries and wages (and all directly associated non-personnel costs) charged to Federal awards (directly or indirectly), as discussed in the Federal Cost Reimbursement Principles section of this report — namely, personnel activity reports which, in turn, must also meet very specific criteria. In addition, use of predetermined numbers of authorized positions and/or job descriptions, as cited by DLLR, would fall under the same general category as “budget estimates or other distribution percentages determined before the services are performed” which do not qualify as support for charges to Federal awards.

Second, DLLR acknowledged in its response that the Principal Counsel and Deputy Counsel (like their staff) provide both direct and indirect legal services. Accordingly, they too must maintain detailed personnel activity reports which comply with the requirements of OMB Circular A-87, Attachment B, paragraph 11.h. in order for their time to be charged, directly or indirectly, to Federal awards. However, as stated in our finding, OAG personnel failed to maintain personnel activity reports which are expressly required by A-87 for employees who work on multiple direct

and/or indirect cost objectives. We do not dispute that OAG provides legal support services to both direct and indirect functions within DLLR — the problem is that there is no acceptable record as to how much time was spent by OAG on each of these various direct and indirect functions. One of the general principles for determining the allowability of costs, whether direct or indirect, is that they must be adequately documented. In the case of salaries and wages, A-87 mandates very strict criteria which this documentation “must” meet.

Third, the characterization that OAG performed “very little legal work” for DET actually came from several DLLR officials — not the auditors. However, we believe that their characterization is consistent with the facts in this case. Based on raw data provided to the audit team by OAG’s Principal Counsel, only about 22 percent of OAG’s efforts during the period covered by our audit directly benefit the Federal grant awards administered by DET. We consider this to be “very little” compared to the 75 percent of OAG costs allocated to the Federal awards as indirect costs.

Fourth, DLLR’s statement that we excluded and disallowed all OAG costs, without regard to the fact that legal services were rendered to DET, based on a “*recommendation in A-87 that legal services be charged/allocated based on direct charges*” is incorrect. The primary criteria were (1) a cost (whether direct or indirect) is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with the “*relative benefits received;*” and (2) where employees work on multiple activities or cost objectives (direct or indirect), “*a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation. . .*” and the “*Personnel activity reports or equivalent documentation must meet. . .*” a number of mandatory criteria which we cited in our report. [Emphasis added.] However, DLLR’s response ignores the primary criteria cited in our report and focuses, instead, on a secondary criteria contained in the implementation guide to OMB Circular A-87 (not A-87 itself) which does recommend that legal services be charged/allocated based on “direct hours.” The underlying purpose of this “recommendation” is to ensure that legal services are, in fact, charged/allocated on the basis of “*relative benefits received.*”

Fifth, the fact that OAG costs have been included in DLLR’s indirect cost pool since the merger of the departments, and has not been questioned by OCD during that time period, does not make unallowable and/or unsupported costs allowable and/or adequately supported. OCD does not have the resources to conduct detailed audits of every indirect cost proposal it receives from the various state and local governmental entities for which it has cognizance and, accordingly, OCD includes a statement in every negotiated indirect cost rate agreement that the rates are “subject to audit.” In addition, OMB Circular A-87, Attachment E, paragraph E.3. expressly states, regarding the negotiation and approval of indirect cost rates, that:

The results of each negotiation shall be formalized in a written agreement between the cognizant agency and the governmental unit. This agreement will be subject to re-opening if the agreement is subsequently found to violate a statute, or the information upon which the plan was negotiated is later found to be materially incomplete or inaccurate.

Finally, our report does not wrongly “punish” DLLR as alleged in its written response. The Federal cost principles on which this report is based were “*designed to provide that Federal awards bear their fair share of cost recognized under these principles. . . .*” In this regard, OMB Circular A-87, Attachment E, paragraph E.4. clearly states that:

Refunds shall be made if proposals are later found to have included costs that (a) are unallowable (i) as specified by law or regulation, (ii) as identified in Attachment B of this Circular, or (iii) by the terms and conditions of Federal awards, or (b) are unallowable because they are clearly not allocable to Federal awards. These adjustments or refunds will be made regardless of the type of rate negotiated (predetermined, final, fixed, or provisional).

In summary, we believe that DLLR’s written response was: (1) non-responsive to the basic issues raised in this finding; and (2) did not provide any new or compelling evidence which would warrant any change in this finding or its related conclusions and recommendations.

B. OIM Costs Also Were Not Allocated to Users on the Basis of Relative Benefits Received

Our review of the indirect cost proposals submitted by DLLR for the 5 fiscal years ended June 30, 1996, through 2000 showed that the entire cost of about \$6.7 million for OIM, like OAG, was included in the DLLR indirect cost pools. The DLLR indirect cost pools were subsequently allocated to DLLR’s operating units, including DET which is primarily responsible for administering DOL/ETA grants. Again, the allocations were based on annual employee counts for each operating unit. Since DET employed about 75 percent of all employees within the operating units, DET was allocated about 75 percent of the OIM costs in the pool.

During a prior audit, we learned that between 85-90 percent of the central services automatic data processing and information technology (ADP/IT) costs billed to DLLR by the Annapolis Data Center were being direct-charged to DOL/ETA grant awards administered by DET, while the remaining 10-15 percent of the central services ADP/IT costs were charged to DLLR’s Office of Budget and Fiscal Services. None of the central services ADP/IT costs billed to DLLR was direct-charged to any of DLLR’s other four operating units (primarily State programs).

In response to our query, the Director of OIM stated the other four DLLR operating units obtained all of their ADP/IT services “in-house” from OIM rather than utilizing the Annapolis Data Center. He said OIM provides various computer type services to the non-DET programs and to DLLR’s support groups such as the Office of Budget and Fiscal Services and the Office of Personnel and Training. The services provided to the non-DET operating units included printing all occupational and professional licenses for all persons licensed by the State, and for tracking the number on each license issued. In addition, it operates and maintains the DLLR internet service for all units — both support and operating units. He further stated that OIM generally does not provide any computer services to DET because that unit utilizes the Annapolis Data Center and has its own computer staff.

Based on that information, it is obvious that at least some of the OIM costs should have been direct-charged to DLLR's non-DET operating units (primarily State programs) rather than 100 percent of its costs being included in the DLLR indirect cost pool.

Our analysis of the raw data supporting the recent DLLR internal study, and discussions with the OIM Director, indicated that about 45 percent of OIM salaries should have been direct-charged to non-Federal programs, and the remaining 55 percent direct-charged to DLLR support units such as the Office of Budget and Fiscal Services and the Office of Personnel and Training, the costs of which are properly included in the DLLR indirect cost pools for allocation to all operating units.

However, the above percentages represent estimates by the OIM Director — he said he did not ask staff members what they spent their time doing. Instead, based on his personal knowledge, he classified the OIM staff members as either working 100 percent on non-Federal programs, or divided 50-50 between Federal and non-Federal programs. Our further discussions with the Director disclosed that the 50-50 divided employees were actually spending their time on delivering services for valid indirect support units such as the Office of Budget and Fiscal Services and the Office of Personnel and Training. In response to our query, he stated that OIM staff members did not prepare time cards or other payroll distribution records, nor were they required to do so by DLLR. Finally, the OIM Director informed us that he believed the 2000 data was fairly representative of the efforts of OIM over the past several years.

While the OIM data based on the Director's estimates may not be precise and completely accurate, we believe it clearly demonstrates that DLLR's annual employee counts are not an acceptable base for allocating OIM cost to operating units on the basis of "relative benefits received" as required by OMB Circular A-87. To the contrary, DLLR's use of employee counts as an allocation base has resulted in shifting a significant amount of DLLR's support units' costs from the various State programs (to which the costs were properly allocable) to DOL/ETA grant awards in violation of the Federal cost principles set forth in A-87.

Further, DLLR's data processing costs should have been charged as direct costs to the benefitting cost objectives (including the Office of Budget and Fiscal Services, and the Office of Personnel and Training), rather than being included in DLLR's indirect cost pool. More specifically, the implementation guide for OMB Circular A-87 recommends that data processing services be charged/allocated to the benefitting cost objectives based on "system usage" (i.e., treated as a direct cost rather than an indirect cost). Accordingly, we have excluded all OIM costs — totaling about \$6.7 million — from the DLLR indirect cost pools for FYs 1996, 1997, 1998, 1999, and 2000.

Finally, assuming that the recent DLLR internal study results for OIM were valid, about 55 percent of OIM's costs could have been charged as direct costs to the benefitting cost objectives, including DLLR's Office of Budget and Fiscal Services and Office of Personnel and Training had the OIM employees maintained personnel activity reports or equivalent documentation which met the detailed documentation standards set forth in OMB Circular A-87, Attachment B, paragraph 11.h., subsection (5), which must be met in order to support claimed salaries and wages (and all

directly associated non-personnel costs). However, as previously discussed, the OIM Director has acknowledged that no personnel activity reports or other equivalent documents was prepared by, or otherwise required of, OIM employees.

Accordingly, the costs of any OIM ADP/IT services which may have been performed for DLLR's support units are also unallowable because they do not meet the minimum "documentation" standards mandated by Federal cost principles and the internal control standards issued by the U.S. General Accounting Office.

Auditee's Response

In their response to our draft report, DLLR officials in part stated:

It has been the Department's belief that the services provided by OIM were properly included in the Indirect Cost Pool because they are generally incurred for a common or joint purpose benefiting [sic] more than one cost objective and are not readily assignable to the cost objectives specifically benefited [sic].

The OIM provides the entire Department with Internet and Intranet development and e-mail administration. OIM also provides Data Processing services to the Office of the Secretary (Executive Direction, Attorney General, Budget & Fiscal Services and Personnel Services). All of these services have an impact on the day-to-day operations of the federal DET programs.

OIM is comprised of five units:

- 1) The **Software Development Support Unit** provides computer programming and PC and mainframe computer programming for State (FMIS) and federal (FARS) reports for Budget & Fiscal Services. Within this Unit, the AS/400 Programming Group provides programming support to the general funded units and the Annapolis Data Center (ADC). Mainframe Programming Group provides programming support to DET, Labor Market Analysis and Information and Budget & Fiscal Services.*
- 2) The **AS/400 Computer Operations Unit** oversees the daily computer operation of OIM's two AS/400 computers. This Unit also manages the ADC mainframe printing of reports for FMIS and FARS reports for Budget & Fiscal Services.*
- 3) The **PC Support Unit** provides PC and printer setup, configuration and repair services to over 275 PC users including the aforementioned units that provide services to the federal DET programs.*
- 4) The **Internet/Intranet Services Unit** provides web site development, support and administration services for DLLR's web site, CareerNet web site, and DLLR's employee-focused Intranet web site. This Unit supports and services DLLR's e-business and*

e-commerce software systems that include Electronic Licensing and develops interactive World Wide Web computer software programs for use by DLLR's customers and partners.

- 5) *The LAN Administrator administers the Local Area Network (LAN) and Email for the 500 North Calvert Street location.*

Because of OIM's umbrella services, this office is rightfully a support function under the direction of DLLR's Office of the Secretary, thus making it eligible for inclusion in the Indirect Cost Pool and in compliance with the Department's DOL-approved Cost Allocation Plan. The Audit Report should not have excluded OIM from the Pool. DLLR asks for a credit in the findings for that portion of the OIM charges that are appropriately charged to the grant.

Auditor's Conclusion

DLLR's response ignores the information contained in our finding about (1) DLLR's large purchases of ADP/IT central services each month (averaging between \$125,000 and \$150,000 per month) from the Annapolis Data Center of which between 85-90 percent was being direct charged to DOL grant awards administered by DET, while the remaining 10-15 percent was being direct charged to the Office of Budget and Fiscal Services; and (2) the OIM Director's statement, in response to our query, that the other four operating units obtain all of their ADP/IT services "in-house" from OIM rather than using the Annapolis Data Center.

This situation alone clearly demonstrates an inconsistent treatment of costs in like circumstances (ADP/IT services costs) which resulted in these costs being allocated to Federal awards on a basis other than "relative benefits received" in violation of the Federal cost principles set forth in OMB Circular A-87. As cited in our report, A-87 states that a cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect costs. Similarly, a cost may not be allocated to a Federal award as an indirect cost if any other cost incurred for the same purpose in like circumstances has been charged to the award as a direct costs. The reason for these particular requirements is to prohibit "double counting" of costs which occurred at DLLR when the DOL grant awards administered by DET paid for their ADP/IT services purchased from the Annapolis Data Center as direct costs, and were then allocated a share of the "in-house" OIM ADP/IT costs (improperly included in the indirect cost pool) which should have been direct charged to the other four DLLR operating units.

We do not question the fact that some of the ADP/IT services performed by OIM were in direct support of some of DLLR's valid indirect cost functions (e.g., Budget and Fiscal Services, Personnel and Training Services, the agency's internet/intranet systems, etc.), and OIM may have even provided some programming support to DET. In addition, we agree that the ADP/IT services provided by OIM are a "support function." However, this does not justify including OIM's total operating costs in DLLR's indirect cost pool (of which about 75 percent was allocated to DET) rather than direct charging all OIM ADP/IT costs to the various DLLR user

groups (both support and operating units) as “recommended” by the implementation guide to OMB Circular A-87.

Again, as was discussed in the preceding finding on the OAG costs, the purpose of the “recommendation” in the A-87 implementation guide to charge ADP/IT costs on the basis of “system usage” was to ensure that the costs were charged to cost objectives on the basis of “relative benefits received.” DLLR’s practice of including OIM costs in its indirect cost pool is a violation of this Federal cost principle.

Further, although OIM apparently did provide ADP/IT support to valid indirect cost functions and may have provided some ADP/IT services to DET, it failed to maintain the required personnel activity reports mandated by OMB Circular A-87 when employees work on more than one direct and/or indirect cost activity and, accordingly, has no acceptable basis for charging costs to the various direct and indirect activities on the basis of “relative benefits received.” Costs which are not properly supported by required documentation are expressly unallowable under Federal cost principles.

In summary, we believe that DLLR’s written response was: (1) non-responsive to the basic issues raised in this finding; and (2) did not provide any new or compelling evidence which would warrant any change in this finding or its related conclusions and recommendations.

C. Certain Executive Direction Costs Were Not Allocated on the Basis of Relative Benefits Received

The indirect cost proposals submitted by DLLR for the 5 fiscal years ended June 30, 1996, through 2000 revealed that the entire cost of about \$10.5 million for Executive Direction, was included in the DLLR indirect cost pool, and subsequently allocated to DLLR’s five operating units including DET. However, our audit disclosed, and the internal DLLR study confirmed, that 10 of the 31 employees engaged in Executive Direction functions and activities at the time of the study performed tasks that benefitted only non-Federal programs — they did not benefit Federal programs. The salaries of these 10 employees accounted for about 25 percent of the total salaries in the Office of the Secretary - Executive Direction for FY 2000.

DLLR did not have comparable data readily available for our review for the other years covered by our audit; however, it is reasonable to assume that the non-Federal functions performed by the 10 employees identified in the DLLR study were also being performed in prior years, whether by the same employees or by others. Accordingly, because OMB Circular A-87 requires that indirect costs include only those costs that jointly benefit Federal and non-Federal programs, we have excluded about \$2.6 million (25 percent of the salary, fringe benefits, and directly-related non-personnel costs associated with these non-Federal functions) from the DLLR indirect cost pools for FYs 1996, 1997, 1998, 1999, and 2000.

The DLLR Office of the Secretary - Executive Direction engages in executive oversight, general administration, public information, and comprehensive planning for the commissions, boards,

divisions, and agencies of the department. The internal DLLR study on each employee's workload within the Office of the Secretary contained a schedule listing the extent to which each of the 31 employee's efforts benefitted Federal and non-Federal programs. While most employees' efforts proved to benefit both Federal and non-Federal programs (and were properly included in the DLLR indirect cost pool), there were 10 employees whose efforts benefitted only non-Federal programs. In response to our query, the person who assembled the study data stated that one of the executives within the Office of the Secretary had prepared the Executive Direction portion based on that person's knowledge of each employee's duties and responsibilities.

We also reviewed the records maintained by the Office of Personnel and Training to obtain job descriptions for the 10 employees identified in the internal DLLR study, and several other employees. Our review of the job descriptions for these individuals supported the validity of DLLR's data that there were 10 persons whose efforts benefitted only non-Federal programs and activities. For example, one of the 10 persons was a program manager working in the Maryland Secretary of State's Office in the Inter/Intra Governmental Relations Unit which handles issues that arise between Maryland and other states. Another was an office assistant serving as the receptionist for the Division of Occupational and Professional Licensing (a State program), and providing various clerical support services for the Office of the Commissioner. The list also included an administrator whose main job was to manage, direct, and organize a multi-functional public information and government relations office handling media and press relations, publication production, and legislative issues management. The job descriptions for remaining employees likewise identified their duties and functions as benefitting only non-Federal programs and activities.

We compiled the FY 2000 salaries for the 10 people who performed only non-Federal functions and related them to the total salaries for the Executive Direction function. The salary data for the 10 people amounted to over \$376,000 of the unit's \$1,502,000 total (or about 25 percent). Since all costs follow salaries (benefits and non-personnel costs), we excluded 25 percent, or \$2.6 million, from the DLLR indirect cost pools for FYs 1996, 1997, 1998, 1999, and 2000 because they did not benefit, either directly or indirectly, Federal programs.

Auditee's Response

In their response to our draft report, DLLR officials in part stated:

The decision to exclude 25 percent of Executive Direction was made based on information gathered in FY 2001 which was not consistent with the status of information in the years covered by the audit. For example, if one were to look at a position control log for the period ending 6/30/99, there were only 4 positions out of 37 which should not be considered as part of the indirect cost pool. The salary of one of these individuals is the subject of another audit and has been resolved in that audit, so in reality there were 3 positions out of 36, which did not belong in the cost pool. The salaries for these three individuals totaled approximately 9.5 percent of the total salaries reported for that period in the report. It is inappropriate to use a 25 percent exclusion, on the basis of data that is beyond the audit period. The Department asks that for

FY 98 the 9.5 percent exclusion rate be used and for FY 99 and 2000 the 3.4 percent exclusion rate be used. We further request that no exclusions be imposed for FY 96 and 97, since the Department does not have, and was not required to keep, the back-up records.

Table C	<i>FY 1998</i>	<i>FY 1999</i>	<i>FY 2000</i>	
<i># of positions</i>	<i>1 of 29</i>	<i>3 of 36</i>	<i>3 of 36</i>	
<i>% of salaries</i>	<i>3.4 %</i>	<i>3.4%</i>	<i>9.5%</i>	
<i>Total \$</i>	<i>\$2,019,690</i>	<i>\$2,289,656</i>	<i>\$2,745,975</i>	
<i>Exclusion \$</i>	<i>\$68,669</i>	<i>\$77,848</i>	<i>\$260,868</i>	<i>\$407,385</i>

This would allow DLLR to recover \$2,226,694 that is currently being disallowed.

In support of this position, DLLR notes that the Code of Federal Regulations 29 CFR 97.42, Section (c)(4) Indirect cost rate proposals, cost allocation plans, etc. states:

“(i) If submitted for negotiation. If the proposal, plan or other computation is required to be submitted to the Federal Government (or to the grantee) to form the basis for negotiation of the rate, then the three year retention period for its supporting records starts from the date of such submission.”

Documentation on file indicates that the cost allocation plan for Fiscal Years 1996 and 1997 was submitted to the Department of Labor on February 26, 1996 and was accepted by them on November 20, 1996. Therefore, the period to question the cost allocation plan for Fiscal Years 1996 and 1997 expired on February 26, 1999, before the entry date for this audit.

Auditor’s Conclusion

DLLR did not dispute our finding that 10 of 31 employees engaged in Executive Direction functions and activities at the time of the internal study performed tasks that benefitted only non-Federal programs (e.g., they did not benefit Federal programs). Instead, DLLR argued that the percentage of personnel engaged in these functions were significantly lower in the earlier years than the 25 percent we calculated.

DLLR is correct in its observation that this finding is based on information gathered by DLLR in the first few months of FY 2001. We attempted, however, to obtain the same internal study data for the other years covered by our audit, but were told that such data were not available. Accordingly, we applied the 25 percent factor to the Executive Direction costs for the earlier years based on the assumption that the basic functions being performed by the 10 individuals were also being performed during the prior years — whether by the same employees, or by other employees.

DLLR's response did not provide any evidence showing that the functions in question were new to FY 2001 and did not exist in the prior years. To the contrary, DLLR's response clearly indicated that at least some of the functions did exist in the prior years. However, the position control logs cited by DLLR as support for its calculations do not constitute adequate documentation as to what tasks/functions were actually being performed by specific employees under Federal cost principles, nor do they clearly show that the functions in question did not exist in the earlier years.

The Code of Federal Regulations provision (29 CFR § 95.47(c)(4)) cited by DLLR as a basis for limiting our finding deals with the retention of records which support its indirect cost rate proposals — it does not create a statute of limitations on the period we may use in questioning costs found to violate Federal cost principles or found to be materially incomplete or inaccurate. OMB Circular A-87, Attachment E, paragraph E.3. states that the negotiated indirect cost rate agreements “...will be subject to re-opening if the agreement is subsequently found to violate a statute, or the information upon which the plan was negotiated is later found to be materially incomplete or inaccurate.” [Emphasis added.] For the record, DLLR did provide to us its supporting records for its FY 1996 and 1997 indirect cost rate proposals; however, these records were not the basis of this finding.

In summary, DLLR did not provide any new or compelling evidence which would warrant any change in this finding, nor the related conclusions and recommendation.

FINDING 2. Allocation Base Used by DLLR to Distribute its Indirect Costs was Flawed Because of Inconsistent Treatment of Similar Employees Between Federal and State Programs

Our review of DLLR’s indirect cost rate proposals disclosed that the allocation base (annual employee counts) used to distribute indirect costs out to its five operating units was flawed because of inconsistent treatment of two categories of employees. More specifically, we found that DET legal personnel assigned to its Unemployment Insurance (UI) program Appeals Board, and computer personnel assigned to its Office of Information Technology (OIT), were routinely included in the annual “employee counts” used to allocate DLLR indirect costs because they were charged as direct costs to DOL grant awards. However, their counterparts in DLLR/OAG and DLLR/OIM who provided similar legal and ADP/IT support services to the non-DET operating units (primarily State programs) were not included in the annual employee counts. Instead, the DLLR/OAG and DLLR/OIM employees and all associated costs were included in the DLLR indirect cost pool, as discussed in Finding 1. DLLR’s failure to ensure consistent treatment for similar categories of employees in calculating its allocation base resulted in the DOL grant awards administered by DET being allocated more than their fair share of the DLLR indirect cost pool.

OMB Circular A-87 states that indirect cost pools should be distributed to benefitted cost objectives on bases that will produce an equitable result in consideration of “relative benefits derived.” In addition, as discussed earlier in this report, the Federal cost principles state that costs must be “accorded consistent treatment” to be allowable. For example, OMB Circular A-87, Attachment A, paragraph C.1.e. states, among other things, that *“A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.”* Conversely, OMB Circular A-87, Attachment E, paragraph A.1. states that *“A cost may not be allocated to a Federal award as an indirect cost if any other cost incurred for the same purpose, in like circumstances, has been charged to the award as a direct cost.”*

Our audit disclosed that DLLR failed to comply with each of these interrelated Federal cost principles. For example, our review of the DLLR indirect cost rate proposals for FYs 1996 through 2000 found that the DLLR indirect cost pool was allocated to operating units such as DET and the Division of Occupational and Professional Licensing on the basis of annual employee counts. The total allocation base was the total number of employees within the five operating units — i.e., Division of Employment and Training (DOL grants), Division of Financial Regulation, Division of Labor and Industry, Maryland Racing Commission, and Division of Occupational and Professional Licensing — minus those employees assigned to the upper management group within each unit. The employee count of each operating unit was then compared to the total allocation base to determine the percentage of DLLR indirect cost to be allocated to each unit. In FY 1999, for example, the total allocation base for the five operating units was 1,642 employees of which DET employees totaled 1,270, or 77.3 percent.

Our review of the DLLR organization structure, the indirect cost rate proposals, and the duties and responsibilities of employees within the operating and support units disclosed that both the DLLR Office of the Secretary and DET each had two groups of employees that appeared to be performing similar duties and responsibilities. More specifically, DLLR/OIM and DLLR/OAG had counterparts in DET who performed similar support functions for the various DOL grant awards.

For example, DLLR/OIM and DET/OIT are both computer groups with data processing program analysts, computer information specialists and data processing operating technicians. Our discussions with the two groups revealed that they both provided the same general ADP/IT support services; however, they served different constituents. Both entities prepare and operate computer programs based on special requirements as well as everyday requirements of their constituents. DLLR/OIM primarily served the four operating units with non-Federal programs, and DLLR's support units — mainly DLLR's Office of Budget and Fiscal Services, and the Office of Personnel. DET/OIT, on the other hand, generally served only DET programs.

In addition, despite the similarity in what they do, DLLR/OIM has been treated as an indirect cost and allocated to all operating units, whereas DET/OIT has been treated as a direct cost to DOL grant awards. Such inconsistent treatment is contrary to A-87 requirements. Because DET/OIT is treated as a direct cost, DLLR/OIM must also be treated as a direct cost. Moreover, this would be consistent with the implementation guide for OMB Circular A-87 which recommends that ADP/IT costs be charged as direct costs based on "system usage." When the treatment of cost is inconsistent, such as in this instance where DET/OIT is a direct cost and DLLR/OIM is an indirect cost, DET bears all the OIT costs, plus most of DLLR/OIM costs through the DLLR indirect cost pool.

The other two groups of employees that appeared to be performing similar duties and responsibilities are the DLLR/OAG and the DET UI Appeals Board. For example, DLLR/OAG spends about 78 percent of its efforts assisting the four DLLR operating units which primarily conduct non-Federal programs because these units — unlike DET — do not have their own legal staff. Much of DLLR/OAG's efforts involves the processing/handling of appeals filed by persons or entities seeking to obtain or maintain occupational or professional licenses which are controlled by DLLR. However, as mentioned in Finding 1, DLLR/OAG is included as an indirect cost in the DLLR indirect cost pool, and, therefore, is not included in the allocation base for allocating DLLR indirect cost to the five operating units.

The DET UI Appeals Board, on the other hand, was established to hear and decide appeals on UI claims matters which arise from the tax provisions of UI law and other appealable matters related to these laws. During FY 2000, the Appeals Board employed 50 persons including, among others, members of the Board, hearing examiners, a legal assistant, and administrative persons such as clerks and typists. Accordingly, the cost of the Appeals Board is a direct cost to the applicable DOL grant(s). However, DLLR has improperly included the Appeals Board employees in the annual employee count allocation base used to determine the amount of DLLR indirect costs to be allocated to DET.

As previously discussed, this constitutes a violation of various cost principles mandated by OMB Circular A-87, including inconsistent treatment of like costs incurred for the same purpose which, in turn, has resulted in an allocation base which does not allocate indirect costs to DET's DOL grant awards on the basis of "relative benefits received." When there is inconsistent treatment of costs, such as in this instance where the UI Appeals Board is treated as a direct cost while DLLR/OAG is treated as an indirect cost, DET bears all the cost of the Appeals Board and much of OAG through the DLLR indirect cost pool.

To assure that this inconsistent treatment of costs does not result in DOL absorbing an unfair share of DLLR indirect costs, we have excluded the DET/OIT and UI Appeals Board staff from the annual employee counts which DLLR used to allocate its indirect cost pool to DET and the other four operating units, and recalculated the percentage of such costs applicable to the DOL grant awards administered by DET. For example, with the exclusion of the DET/OIT and UI Appeals Board employees from the allocation base in FY 1999, DET's share of DLLR indirect costs was reduced from 77.3 percent down to 74.9 percent. Similar calculations in the other 4 years determined that DET's share of DLLR indirect costs would be lower in all 5 years covered by our audit.

Auditee's Response

In their response to our draft report, DLLR officials in part stated:

In reviewing the draft report, DLLR believes Finding 2 to be flawed because of a basic misunderstanding of certain departmental functions. The Department therefore ask that this finding be removed from the report.

In this section, an assumption is made that OIM and OIT, because they both provide computer services are functioning for the same purpose, in like circumstances. This is simply not true. OIT functions directly for the DET program. In addition to providing the day-to-day support that is so critical in ensuring that DET services are timely provided, OIT also does the comprehensive developmental work which allows the Maryland DET Programs to remain at the leading edge of technology. OIT has successfully tackled projects such as the creation of call centers and Internet claims processing. On a day-to-day basis OIT services the system that issues the unemployment checks. In contrast to that, OIM provides centralized services that benefit the Department as a whole and DET on a proportionate basis, specifically the support of web pages, budget, payroll and personnel systems, which are critical to the Department as a whole. We believe these distinctions argue for the separate treatment these two units received.

Further, there is an assumption that "the other two groups that appeared to be performing similar duties and responsibilities are the DLLR/OAG and the DET UI Appeals Board." This assumption is inaccurate. The centralized, Statewide office, Office of Administrative Hearings (OAH), and the boards and commissions, provide services similar to those provided by the DET UI Lower Appeals and Appeals Board, respectively, to the State programs. The OAH, a direct charge unit, conducts hearings and issues decisions regarding the actions of the DLLR units.

The boards and commissions serve as the final decision makers. The Office of the Attorney General, among other responsibilities, assists the programs to prepare their cases and tries cases before the OAH and before the DET UI Appeals Board. The OAG also takes cases to court on behalf of DET and of other Departmental programs.

By law, the Attorney General is the lawyer for the State. DET uses the services of the OAG for its legal services. The argument in this section is inaccurate and in fact supports the practice of the Department of charging its legal staff as an indirect cost to the programs. Further, the employees in the Appeals Office are an integral part of the DET/UI Program and its employees are properly included in the annual employee allocation base for DET.

In light of these misunderstandings, DLLR requests that this finding be removed.

Auditor's Conclusion

We disagree with DLLR's position that the computer services being provided by DLLR/OIM and DET/OIT do not constitute services for the same purpose in like circumstances. We also disagree with DLLR's position that the legal services being provided by DLLR/OAG and the DET appeals boards do not constitute services for the same purpose in like circumstances. We do agree that there may be some differences in the specific nature of the computer services and legal services being provided by each of these units.

However, there can be no dispute about the fact that the ADP/IT and legal personnel who support DET programs (the OIT and the appeals board staff, respectively) are included in DET's allocation base (annual body counts), where as the ADP/IT and legal personnel who provide similar services in support of the other four DLLR operating units (the DLLR/OIM and DLLR/OAG staff) are not included in their respective allocation bases. This is clearly a violation of various Federal cost principles mandated by OMB Circular A-87, particularly the requirement for consistent treatment, and the allocation of costs on the basis of "relative benefits received," and has resulted in the DOL grant awards being allocated more than their fair share of DLLR's indirect costs.

Further, the fact that DLLR/OIM and DLLR/OAG may also provide ADP/IT and legal services to valid indirect support functions (e.g., budget, accounting, personnel, etc.) in no way alters the fact that DLLR is in violation of Federal cost principles.

In summary, we believe that DLLR's written response was non-responsive to the basic issues raised in this finding, and did not provide any new or compelling evidence which would warrant any change in the finding or its related conclusions and recommendations.

FINDING 3. SWCAP Costs Allocated to DLLR Included Y2K Costs Which Should Have Been Capitalized

Allowable and allocable State central services costs included in an approved SWCAP may be included in DLLR's indirect cost pool to be distributed to all benefitting cost objectives. Although the scope of our audit did not include a detailed audit of Maryland's actual central services costs allocated to DLLR in FYs 1996 through 2000, our limited analysis of certain SWCAP costs raised a number of serious questions about the allowability and allocability of such costs to DLLR. For example, the amount of actual FY 1997 SWCAP costs incurred and allocated to DLLR totaled only \$798,138 whereas the actual FY 1998 SWCAP costs allocated to DLLR totaled \$9,428,275 — an increase of over \$8.6 million. We determined that at least \$8.4 million of this increase represented costs incurred by the State of Maryland to correct Y2K computer problems.

Because of its concerns about this significant increase in the amount of SWCAP costs allocated to it in FY 1998 due to the Y2K problem, DLLR consulted with DOL's Office of Cost Determination (OCD) on how such costs should be handled in its indirect cost rate proposals. DLLR officials said they were advised by OCD that the Y2K costs did not constitute "recurring operating expenses," and, therefore, should not be included in its indirect cost rate proposals. Accordingly, DLLR excluded the \$8,436,047 in "specifically identified" DLLR Y2K costs from its indirect cost rate proposal for FY 1998, and claimed only the remaining difference of \$992,228 (\$9,428,275 - \$8,436,047). (DLLR also included the same \$992,228 amount as estimated SWCAP costs in its indirect cost rate proposals for FYs 1999 and 2000 because it had not yet received approved SWCAPs for these years.)

We concur with the position taken by OCD. We believe the Y2K costs represent material "capital improvements" which increased the useful life of the State's computer systems and, accordingly, should be capitalized and amortized to benefitting cost objectives over the useful life of the improvements in accordance with generally accepted accounting principles.

However, although DLLR excluded the "specifically identified" Y2K costs from the SWCAP costs claimed in its FY 1998 indirect cost proposal, our limited review of costs included in the Maryland SWCAPs raised a number of questions about (1) the methodology used to prepare the annual SWCAPs, and (2) the validity of the cost data.

For example, DLLR is a relatively small agency which generally only accounts for about 1 to 2 percent of the entire State budget, and the total number of State employees, yet, about 25 percent of the total actual Y2K costs of about \$32 million incurred in FY 1998 for the entire State was allocated to DLLR. In addition, we have information showing that DOL granted over \$4 million in Federal funds to DLLR in FYs 1998 and 1999 to fix Y2K problems in the UI program administered by DET.

Taken together, these two issues raise a question about whether the \$8.4 million in Y2K costs allocated to DLLR in FY 1998 may have included Y2K projects funded with Federal monies. Accordingly, we requested that Maryland's Department of Budget and Management (DBM) officials provide us with a detail list describing each Y2K project included in the \$8.4 million allocated to DLLR in FY 1998. We also asked that the list contain a detailed description of each project; show how, and to what extent, each project benefitted the various DOL grant awards administered by DET; and show how each project was funded — whether with State funds, Federal funds, or a combination. DBM initially agreed to compile and deliver the requested data in about a week. However, after repeated follow-up calls over a period of several weeks regarding the status of our request, DBM officials acknowledged that they had “serious concerns” about the information they had compiled, and needed to do further research.

Approximately a month after our initial request, a DBM staff member called to say that her superiors wanted to know why we wanted this data since DLLR had excluded the \$8.4 million in Y2K costs for the SWCAP costs included in its indirect cost rate proposal. In addition, she also said no one seemed to know to what extent the projects benefitted the Federal programs. Further, she stated that the Y2K costs were applicable to FMIS — Maryland's State-wide accounting system and personnel benefits system. However, if this were true, a valid question exists as to why the \$8.4 million in Y2K costs were direct-charged to a small agency like DLLR, rather than being allocated out on the basis of employee count the way DBM costs are normally allocated out to all benefitting State agencies.

Further, an informal listing of Y2K project costs totaling \$32 million for FY 1998 (which we obtained from another source) did include over \$6 million in Y2K projects which we were told were directly applicable to DOL programs administered by DET and were federally funded. Accordingly, we are inclined to believe that the reason for DBM's reluctance to provide us with the requested information was that at least some of the projects included in the \$8.4 million in Y2K costs charged to DLLR were, in fact, funded with Federal dollars.

Finally, in addition to the above questions regarding “specifically identified” Y2K costs allocated to DLLR in the SWCAP, our comparative analysis of other SWCAP costs (not specifically identified as Y2K costs) also raised a number of questions regarding the validity of the SWCAP cost data allocated to DLLR. For example, our comparative analysis of various central services SWCAP costs allocated to DLLR disclosed:

- (1) the costs for the Legislative Auditor went from \$6,602 in FY 1998 to \$391,353 in FY 1999;
- (2) DBM costs went from \$265,394 in FY 1997 to \$543,975 in FY 2000;
- (3) Personnel Services and Benefits increased from \$273,291 in FY 1997 to \$521,621 in FY 2000; and
- (4) total SWCAP costs allocated to DLLR more than doubled from \$798,138 in FY 1997 to \$1,757,540 in FY 2000.

Our cursory review of the SWCAPs revealed few details which might explain these large increases.

Another comparative analysis of actual SWCAP costs for DBM disclosed very large increases in contractual services within the Office of Chief of Office of Information Technology totaling over \$100 million between FY 1997 and FY 2000. We also noted one instance involving the function of Personnel Services and Benefits in which the salary and fringe benefit costs for 11 employees increased from \$758,271 in FY 1998 to \$4,947,377 in FY 2000. We believe these unexplained increases could possibly indicate that additional Y2K costs (not expressly identified as such) may also have been included in SWCAP central services functions rather than being treated as capital expenditures.

While our comparative analyses and cursory review of the actual SWCAP costs did not clearly identify the underlying reasons for the significant increases discussed above for FYs 1998 through 2000 compared to FY 1997, we did note that no other central services function which increased in total costs approximated the magnitude of the increases in the DBM costs. DBM was primarily responsible for administering all Y2K contracts for the entire State. In addition, there is no doubt that this responsibility was a major undertaking for the agency.

The Y2K problem, in our opinion, contaminated the SWCAP costs to the point that they do not reflect the routine recurring central services costs for the State. Nevertheless, DLLR is entitled to recover a reasonable amount of SWCAP costs. Accordingly, we accepted the SWCAP costs allocated to DLLR for FYs 1996 and 1997 (which did not appear to include any Y2K costs), and added an annual 10 percent cumulative increase to the FY 1997 costs which we believe will permit DLLR a reasonable recovery of its applicable SWCAP costs.

The following table lists the amount of SWCAP costs included in each of DLLR's indirect cost rate proposals, and the amounts we believe represent a reasonable recovery (excluding Y2K costs). We believe the difference of \$124,509 is relatively minor considering the problems we noted in the SWCAPs.

Fiscal Year	Proposed Amount	Amount Allowed	Difference
1996	\$851,984	\$851,984	- 0 -
1997	\$851,984	\$798,138	\$53,846
1998	\$992,228	\$877,952	\$114,276
1999	\$992,228	\$965,747	\$35,481
2000	\$992,228	\$1,062,322	(\$70,094)
TOTALS	\$4,680,652	\$4,556,143	\$124,509

Auditee's Response

In their response to our draft report, DLLR officials in part stated:

The agency proactively excluded certain charges from the indirect cost pool. DLLR acted in good faith, and in consultation with the Office of Cost Determinations, to limit the amount charged under the Statewide Cost Allocation Plan (SWCAP). The \$8.4 million that were simply excluded could likely have been capitalized and included in the proposal. The capitalized costs would more than offset the \$124,509 disallowed costs contained in the draft report. DLLR's good faith efforts and negotiations should be respected and this finding, and associated dollar findings, should be removed from the audit.

Auditor's Conclusion

We disagree that the finding should be removed from the audit. As stated in the finding above, we have reason to believe that a substantial portion of the \$8.4 million in Y2K costs allocated to DLLR in the SWCAP was funded by DOL grants and, at least that portion of the \$8.4 million should not be capitalized and included in DLLR's indirect cost proposals. Also, as discussed above, Maryland DBM officials declined to provide the detailed cost data we requested on the \$8.4 million showing (1) how, and to what extent each Y2K project benefitted the various DOL grant awards administered by DET; and (2) how each project was funded — whether with State funds, Federal funds, or a combination thereof. Based on an informal listing we obtained from another source, we have strong indications that over \$6 million of the \$8.4 million in Y2K costs were, in fact, funded with Federal dollars.

DLLR did not provide any new or compelling evidence which would warrant any change in this finding, nor the related conclusions and recommendations.

FINDING 4. Wage Base Used by DLLR to Compute DET Indirect Cost Rates Differed from Wage Base Used to Recover Indirect Costs

Our audit disclosed that the direct wage base used by DLLR to calculate its proposed DET indirect cost rates for fiscal years ended June 30, 1996, 1997, 1998, 1999, and 2000, differed somewhat from the direct wage base used to recover its indirect costs on the various DOL grant awards administered by DET. This inconsistency in the base used for establishing versus applying indirect cost rates is contrary to OMB Circular A-87. All other factors remaining equal, this would cause DLLR to under-recover its indirect costs. However, because DLLR used the same indirect cost rate negotiated for FY 1996 to recover its indirect costs in all subsequent fiscal years, we were unable to readily determine the dollar impact of this finding.

The following terms, as defined in OMB Circular A-87, clearly establish that the direct cost base used to calculate the indirect cost rate should also be used to allocate the indirect costs to individual programs.

“Indirect cost rate” is a device for determining in a reasonable manner the proportion of indirect costs each program should bear. It is the ratio (expressed as a percentage) of the indirect costs to a direct cost base.

“Base” means the accumulated direct costs (normally either total direct salaries and wages or total direct costs exclusive of any extraordinary or distorting expenditures) used to distribute indirect costs to individual Federal awards. The direct cost base selected should result in each award bearing a fair share of the indirect costs in reasonable relation to the benefits received from the costs.

Both of these statements address a direct cost base and this base is used to both (1) develop the indirect cost rate (costs in the indirect cost pool divided by the direct cost base); and (2) distribute or allocate indirect costs to programs (indirect cost rate times the direct cost base).

Our audit found that the wage base used to calculate the indirect cost rate for DET was comprised of the budgeted salaries and wages of all DET employees (including all DET/OIT personnel), minus the budgeted salaries and wages of the DET administrative staff. However, our review of the monthly project cost reports (GA-17 reports) for each of the DOL grant awards disclosed that not all DET employees were included as direct labor cost on which DLLR calculated the indirect costs to be recovered from the DOL grants. Some of the labor costs of DET/OIT personnel were charged to the DOL grants as “other direct costs” rather than as direct labor costs. In response to our queries, DLLR’s chief accountant agreed with our finding, but was unable to explain how this situation had occurred.

Although we are reporting this matter as a finding to further illustrate DLLR’s failure to comply with the Federal cost principles, we have not made any additional recommendations to correct

this situation because the problem will be corrected by other recommendations resulting from Finding 2.

Auditee’s Response

In their response to our draft report, DLLR officials in part stated:

The Auditor’s fourth finding was that “not all DET employees were included as direct labor costs on which DLLR calculated the indirect costs to be recovered from DOL grants.” The problem was with DET/OIT, where personnel were charged to DOL grants as “other direct costs” rather than as direct labor costs. The Department concurs with this finding. The effect of this oversight, by which OIT direct personnel costs were not included as direct labor costs, was that the size of the DET direct labor pool was diminished in the Department’s drawdown calculations. As noted by the Auditor, this caused “DLLR to under-recover its indirect costs.” In Table A [sic], we have calculated the net effect of this under-recovery by applying the approved indirect cost rate, per the cost allocation plans for the respective years, to the direct labor costs for DET/OIT. The result is that the Department under-recovered approximately \$3.2 million. The Department requests that this amount be remitted to the Department or used to offset any of the alleged over-recovery reported by the Auditors which may be determined to be valid.

<i>Table D</i>	<i>FY 1996</i>	<i>FY 1997</i>	<i>FY 1998</i>	<i>FY 1999</i>	<i>FY 2000</i>	<i>Allowable Cost</i>
<i>Additional OIT Costs not Included in Wage Base for Draws</i>	1,860,799	2,021,810	1,753,729	2,523,762	2,750,866	10,910,966
<i>Applicable Rate</i>	26.90%	26.90%	33.55%	28.72%	32.10%	
<i>Additional Indirect Cost Allowable</i>	500,555	543,867	588,376	724,824	883,028	3,240,650

Auditor’s Conclusion

We reported this finding simply to point out that DLLR was inconsistent in the bases it used to compute versus recover its indirect costs, and that DLLR would have under-recovered its indirect costs had all other factors remained equal. However, all other factors did not remain equal, as discussed in the other findings in this report, and DLLR significantly over-recovered its indirect costs.

Moreover, DLLR is not entitled to off-set its alleged \$3.2 million in under-recovered indirect costs because we have already factored this into our calculation of the net amount of DLLR’s total over-recovery of indirect costs as shown in the exhibit at the end of this report.

Finally, as discussed in Finding 2, our review disclosed that the inclusion of OIT personnel in the allocation base (annual employee counts) used to distribute DLLR indirect costs to its various operating units constituted an inconsistent treatment of cost in like circumstances which resulted in those costs being allocated to DET awards on a basis greater than “relative benefits received,” in violation of OMB Circular A-87.

In summary, DLLR’s written response did not disclose any new or compelling evidence which would warrant any change in this finding, or its related conclusions and recommendations.

CONCLUSIONS AND RECOMMENDATIONS

CONCLUSIONS

Based on the results of our audit, we have concluded that DLLR has over-charged DOL grant awards a total of \$9,833,059 in indirect costs over the 5-year period ended June 30, 2000. This occurred because DLLR has failed to implement adequate internal control policies and procedures to ensure compliance with Federal cost principles mandated by OMB Circular A-87, the “Common Rule” (as implemented by DOL at 29 CFR § 95), and the terms and conditions of the various DOL grant awards.

As discussed in the body of this report, our audit disclosed that:

- (1) the costs of certain support units and personnel under the Office of the Secretary, which should have been direct-charged to the benefitting cost objectives, were improperly included in its indirect cost pool;
- (2) two categories of DET support personnel — legal and ADP/IT staff — were improperly included in the employee count allocation base for DET, while “like” support personnel were not included in the employee count allocation base for DLLR’s non-Federal (State) programs;
- (3) certain SWCAP costs included in DLLR’s indirect cost pool were highly questionable; and
- (4) the wage base used by DLLR to compute DET indirect cost rates differed from the wage base used to recover its indirect costs.

The first three findings caused DLLR to over-recover its indirect costs while the fourth finding, all other factors remaining equal, would cause DLLR to under-recover its indirect costs.

We believe that these findings occurred because DLLR failed to establish adequate internal control policies and procedures to ensure compliance with the cost principles mandated by OMB Circular A-87. During our fieldwork, for example, we observed that most of the personnel in DLLR’s Office of Budget and Fiscal Services generally did not seem to be familiar with the Federal cost principles set forth in OMB Circular A-87 — several actually borrowed our file copy to make copies for themselves. Further, since DLLR was created effective July 1, 1995, its Office of Program Analysis and Audit has not conducted any audits of (1) DLLR’s indirect costs and/or its indirect cost rate proposals to determine whether they were in compliance with Federal cost principles, and (2) DLLR payroll costs to determine whether they were properly supported by personnel activity reports as required by OMB Circular A-87.

Nevertheless, a DLLR official has certified that he had reviewed the indirect cost rate proposals and that, to the best of his knowledge and belief, all costs in the proposal were (1) allowable in accordance with the requirements of the Federal award(s) to which they apply, and OMB Circular A-87; and (2) allocable to Federal awards on the basis of a beneficial or causal relationship between the expenses incurred and the agreements to which they are allocated in accordance with applicable requirements.

In response to our queries, the DLLR personnel responsible for preparing its annual indirect cost rate proposals stated that the proposals were prepared by closely following the same procedures used by their predecessor organization before the July 1, 1995, merger. The current Director of the DLLR Office of Budget and Fiscal Services stated they were planning to make some changes in the methodology used to prepare the proposal, but were awaiting completion of our audit.

RECOMMENDATIONS

We recommend that:

1. the cognizant DOL Grant Officer(s) direct DLLR to refund the \$9,833,059 in unallowable costs questioned in this report, pursuant to OMB Circular A-87, Attachment E, paragraph E.4. (Findings 1, 2, 3, and 4.)
2. the cognizant DOL Grant Officer(s) direct DLLR to adjust its billings to DOL for FY 2001 indirect costs to preclude further over-recoveries of indirect costs attributable to the findings in this report. (Findings 1, 2, 3, and 4.)
3. the Assistant Secretary for Employment and Training direct DLLR to develop and implement internal control policies and procedures, required by 29 CFR § 95.21(b)(6), to ensure that its indirect cost rate proposals fully comply with the reasonableness, allocability, and allowability criteria mandated by OMB Circular A-87. (Findings 1, 2, 3, and 4.) These internal control policies and procedures should ensure, among other things, that:
 - a. DLLR Office of Attorney General and Office of Information Management costs are direct-charged to the benefitting cost objectives, rather than being included in the indirect cost pool and allocated out to DOL grant awards on a basis other than “relative benefits received.” (Finding 1.)
 - b. All personnel and non-personnel costs associated with staff in the Office of the Secretary who perform no tasks which directly or indirectly benefit Federal grant awards are excluded from the DLLR indirect cost pool, and direct-charged to the benefitting cost objectives. (Finding 1.)
 - c. All DET legal (UI Appeals Board) and computer (Office of Information Technology) personnel are excluded from the employee count allocation base used to distribute the DLLR indirect cost pool out to the five operating units. (Finding 2.)

- d. Only valid allowable SWCAP costs, properly allocable to DLLR, are included in the DLLR indirect cost pool. Capital expenditures (such as the Y2K costs incurred by the State of Maryland) are unallowable. (Finding 3.)
 - e. DLLR uses the same wage base to recover indirect costs on its DOL grant awards that it uses to compute the indirect cost rates. (Finding 4.)
4. the Assistant Secretary for Employment and Training direct DLLR to provide comprehensive training to key personnel within the Office of Budget and Fiscal Services to ensure that they have an adequate working knowledge of the Federal cost principles mandated by OMB Circular A-87. (Findings 1, 2, 3, and 4.)
5. the Assistant Secretary for Employment and Training direct DLLR to include a provision in its annual audit plans for periodic audit of
- a. DLLR's indirect cost rate proposals and supporting documentation to ensure compliance with Federal cost principles; and
 - b. DLLR's payroll costs to ensure that they are properly supported by personnel activity reports (or semi-annual certifications, where appropriate) as required by OMB Circular A-87.

Auditee's Response

In their response to our draft report, DLLR officials disagreed with virtually all of our findings and recommendations, and concluded that it had not over-recovered its indirect costs and, therefore, did not owe a refund to DOL. Among other things, DLLR stated the methodology used in the audit process was flawed in that (1) it assumed conditions not required by the Award; (2) the sampling methods employed were insufficient and inapplicable; and (3) the auditors applied "suggested bases" as though their use were mandatory for certain items.

We have incorporated DLLR's detailed comments at the end of each finding, as appropriate. In addition, a copy of DLLR's written response is included, in its entirety, as an appendix to this report.

Auditor's Conclusion

DLLR's response did not provide any new or compelling evidence which would warrant any change in the findings, conclusions and recommendations presented in our draft report.

Further, DLLR's written response did not address the critical Federal cost principles expressly cited in our report as the basis for our findings, including: (1) the requirement that costs must be allocated to cost objectives in accordance with "relative benefits received;" (2) the requirement

that costs must be “accorded consistent treatment” to be allowable; and (3) the requirement that all salaries and wages (and all directly associated costs) of employees who work on multiple direct and/or indirect cost objectives must be supported by personnel activity reports which meet the criteria mandated in OMB Circular A-87 in order to be allowable. Accordingly, we consider DLLR’s written response to be generally unresponsive to the findings presented in the draft report.

In summary, all the recommendations are considered unresolved.

TICHENOR & ASSOCIATES, LLP
CERTIFIED PUBLIC ACCOUNTANTS and MANAGEMENT CONSULTANTS

WASHINGTON OFFICE

12531 CLIPPER DRIVE SUITE 202
WOODBIDGE VA 22192

PARTNERS

WILLIAM R. TICHENOR
DEIRDRE REED

BUSINESS: (703) 490-1004
METRO: (703) 352-1417
FAX: (703) 491-9426
E-MAIL: TICHASSOC@AOL.COM

Mr. John J. Getek
Assistant Inspector General for Audit
Office of Inspector General
U.S. Department of Labor
200 Constitution Ave., NW
Washington, DC 20210

INDEPENDENT ACCOUNTANT'S REPORT ON AUDIT

Tichenor & Associates, LLP, was engaged by the Office of Inspector General (OIG), U.S. Department of Labor (DOL), to conduct an audit of direct and indirect costs charged to the Unemployment Insurance (UI) program administered by the State of Maryland's Department of Labor, Licensing and Regulation (DLLR) for Federal fiscal year 2000, to determine whether such costs were reasonable, allowable, and allocable under the Federal cost principles set forth in OMB Circular A-87. The audit objectives provided that, depending on the results of our audit, the scope of the audit could be expanded to include additional years and other Federal grant programs.

The preliminary results of our audit of direct labor costs (the predominant direct cost) charged to the UI grant program generally failed to indicate any significant problems with the allowability of such costs. At the same time, our preliminary results indicated potential significant problems with the allowability of indirect costs beginning with the reorganization of DLLR on July 1, 1995, and continuing on to the present time. Accordingly, we focused the balance of our audit on the DLLR claims for and recovery of indirect costs applicable to DOL grants administered by DET for the State of Maryland fiscal years ended June 30, 1996, 1997, 1998, 1999, and 2000.

We were not engaged to, and did not perform, an audit of DLLR's total costs charged to DOL grant awards, the objective of which would have been the expression of an opinion on the total costs claimed by DLLR, and, accordingly, we do not express such an opinion.

Based on the results of our audit, we questioned a total of \$9,833,059 in indirect costs charged to DOL grant awards to DLLR during FYs ended June 30, 1996, 1997, 1998, 1999, and 2000 which were not in compliance with the Federal costs principles mandated by OMB Circular A-87. Specifically, we found that:

- (1) the costs of certain support units and personnel under the Office of the Secretary, which should have been direct-charged to the benefitting cost objectives, were improperly included in its indirect cost pool;
- (2) two categories of DET support personnel — legal and ADP/IT staff — were improperly included in the “employee count” allocation base for DET, while “like” support personnel were not included in the “employee count” allocation base for DLLR’s non-Federal (State) programs;
- (3) certain SWCAP costs included in DLLR’s indirect cost pool were highly questionable; and
- (4) the wage base used by DLLR to compute DET indirect cost rates differed from the wage base used to recover its indirect costs.

The first three findings caused DLLR to over-recover its indirect costs while the fourth finding, all other factors remaining equal, would cause DLLR to under-recover its indirect costs.

This limited-scope audit was performed in accordance with applicable standards established by the American Institute of Certified Public Accountants, and the *Government Auditing Standards* issued by the Comptroller General of the United States. Our engagement did not include expressing a written opinion on the reasonableness and allowability of DLLR’s total claimed costs, the adequacy of its overall system of internal controls, or its compliance with laws and regulations applicable to Federal grant awards. Our detailed findings, conclusions, and recommendations are contained in the accompanying report.

This report is intended solely for the use of the U.S. Department of Labor; however, the final report is a matter of public record and its distribution is not limited.

TICHENOR & ASSOCIATES, LLP
Woodbridge, Virginia
May 24, 2001

EXHIBIT

Maryland Department of Labor, Licensing and Regulation
Schedule of DLLR/DET Claimed Indirect Costs, Auditor Adjustments
and DET Indirect Costs Recovered on DOL Grants

DESCRIPTION	Fiscal Year	Fiscal Year	Fiscal Year	Fiscal Year	Fiscal Year	
	1996	1997	1998	1999	2000	TOTALS
Actual Costs in Unaudited Indirect Cost Pool Office of the Secretary						
Executive Direction	\$1,396,037	\$2,084,914	\$2,019,690	\$2,289,656	\$2,745,975	\$10,536,272
Budget and Fiscal Services	2,111,613	1,785,168	1,902,522	2,004,590	2,040,525	\$9,844,418
General Services	4,650,250	4,751,889	4,599,596	4,296,189	5,064,170	\$23,362,094
Office of the Attorney General	1,904,988	1,825,213	1,820,689	1,937,779	1,995,925	\$9,484,594
Office of Information Management	1,409,557	867,905	1,372,656	1,504,819	1,572,939	\$6,727,876
Personnel Services and Training	906,878	1,069,343	1,488,626	1,626,964	1,624,976	\$6,716,787
Subtotals - Office of the Secretary	\$12,379,323	\$12,384,432	\$13,203,779	\$13,659,997	\$15,044,510	\$66,672,041
Plus: Allowable SWCAP	\$851,984	\$798,138	\$877,952	\$965,747	\$1,062,322	\$4,556,143
DET Administrative Costs	\$438,129	\$307,629	\$393,621	\$373,613	\$355,772	\$1,868,764
Total Claimed Indirect Costs by DLLR	\$13,669,436	\$13,490,199	\$14,475,352	\$14,999,357	\$16,462,604	\$73,096,948
Questioned Costs						
Less: Total Exec. Direction Costs for 10 of 31 positions	(349,009)	(521,229)	(504,923)	(572,414)	(686,494)	\$(2,634,069)
100% Office of Attorney General (OAG)	(1,904,988)	(1,825,213)	(1,820,689)	(1,937,779)	(1,995,925)	\$(9,484,594)
100% of Office of Information Management (OIM)	(1,409,557)	(867,905)	(1,372,656)	(1,504,819)	(1,572,939)	\$(6,727,876)
Total Questioned Indirect Costs	(\$3,663,554)	(\$3,214,347)	(\$3,698,268)	(\$4,015,012)	(\$4,255,358)	(\$18,846,539)
TOTAL ALLOWABLE DLLR INDIRECT COSTS	\$10,005,882	\$10,275,852	\$10,777,084	\$10,984,345	\$12,207,246	\$54,250,409
Indirect Costs Allocable to DET	\$7,714,409	\$7,831,644	\$8,351,507	\$8,321,051	\$9,471,926	\$41,690,537
Less: Indirect Costs Recoverable from non-DOL Sources	\$130,230	\$99,074	\$207,429	\$257,220	\$305,644	\$999,597
INDIRECT COSTS ALLOCABLE TO DOL GRANTS	\$7,584,179	\$7,732,570	\$8,144,078	\$8,063,831	\$9,166,282	\$40,690,940
Less: Actual DOL Indirect Costs Recovered	\$10,044,437	\$10,315,875	\$9,339,642	\$10,161,998	\$10,662,047	\$50,523,999
OVER-RECOVERY FROM DOL	\$2,460,258	\$2,583,305	\$1,195,564	\$2,098,167	\$1,495,765	\$9,833,059

AUDITEE'S RESPONSE