



UNITED STATES DEPARTMENT OF EDUCATION  
OFFICE OF INSPECTOR GENERAL

THE INSPECTOR GENERAL

JUL 19 2001

**MEMORANDUM**

TO: Robert D. Muller  
Office of Vocational and Adult Education

FROM: Lorraine Lewis *Lorraine Lewis*

SUBJECT: FINAL REPORT: *Review of the Formula Grant Disbursement Process Within the U.S. Department of Education Office of Vocational and Adult Education*  
(Audit Control Number: ED-OIG/S17-B0015)

Attached is a copy of the final report referenced above. We received your comments concurring with the recommendations in the draft report and have included them as Attachment I of the final report.

You have been designated as the action official responsible for the resolution of the recommendations in this report. Please provide the Post Audit Group Supervisor - Financial Improvement and Post Audit Operations, Office of the Chief Financial Officer within sixty (60) days of issuance of this report with a Corrective Action Plan that builds on the actions you outline in your comments. Then provide the Post Audit Group Supervisor with quarterly status reports on corrective actions until all such actions have been completed or continued follow up is unnecessary.

In accordance with the Freedom of Information Act (Public Law 90-23), reports issued by the Office of Inspector General are available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act. Copies of the report have been provided to the offices shown on the distribution list.

We appreciate the cooperation given to use and Ernst & Young, LLP, during the review. Should you have any questions concerning the draft report, please contact Mr. Todd Givens, Director, Financial Statements Internal Audit, at (202) 205-7945.

Attachment

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**Distribution List:**

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To the Inspector General  
U.S. Department of Education

This report presents the results of our review of the formula grant disbursement process within the U.S. Department of Education's (Department) Office of Vocational and Adult Education (OVAE). This review is part of a larger review of disbursement processes within the Department that was conducted by Ernst & Young, LLP (E&Y) at the request of the Office of Inspector General. The results of work will be provided to the Secretary.

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

The objectives of the review were to determine the processes by which payments can be made by the Department and to assess the controls over the payments in those processes to determine if the controls are operating effectively.

To accomplish the review objectives, we obtained a detailed understanding of the formula grant program, the Grant Administration and Payment System (GAPS), and the control environment surrounding the formula grant disbursement process by attending presentations given by Department officials and conducting interviews with key Department personnel. We also reviewed policy and procedure manuals and Web site information relating to the formula grant program and GAPS. In addition, we reviewed audit reports and other products issued by the Department's Office of Inspector General, the U.S. General Accounting Office (GAO), and independent auditors. Walk-throughs of the formula grant disbursement process were then conducted to validate our understanding of the control environment, control objectives, and control techniques. A limited number of formula grant transactions were selected and tested to validate the disbursement process and to identify areas where internal controls could be potentially improved. Interviews and limited transaction testing were conducted between October 17, 2000, and March 30, 2001.

The work within OVAE was limited to the formula grant disbursement process. An attachment provides a business map detailing the process for formula grant disbursements.

We conducted our work according to the American Institute of Certified Public Accountants Professional Standards for consulting services. These standards require the development of findings, conclusions, and recommendations determined by the objectives of the engagement. In conducting our work, we also compared the control environment to known industry established best practices appropriate to the scope of review described above. On April 5, 2001, the results of this review were discussed with members of the Vocational-Tech Education and Adult Education and Literacy staff.

## INTERNAL CONTROLS

Management is responsible for establishing and maintaining internal controls. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of internal control policies and procedures. The objectives of internal control are to provide management with reasonable, but not absolute, assurance that: assets are safeguarded against loss from unauthorized use or disposition; transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in conformity with accounting principles generally accepted in the United States; and data that support reported performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information. Because of inherent limitations in any internal control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of internal control to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

The Federal Managers' Financial Integrity Act of 1982 requires GAO to issue standards for internal control in the government. Office of Management and Budget (OMB) Circular A-123, Management Accountability and Control, revised June 21, 1995, provides the specific requirements for assessing and reporting on controls.

Recently, other laws have prompted renewed focus on internal control. The Government Performance and Results Act of 1993 requires agencies to clarify their missions, set strategic and annual performance goals, and measure and report performance toward those goals. Internal control plays a significant role in helping managers achieve those goals. Also, the Chief Financial Officers Act of 1990 calls for financial management systems to comply with internal control standards, and the Federal Financial Management Improvement Act of 1996 identifies internal control as an integral part of improving financial management systems.

Rapid advances in information technology have highlighted the need for updated internal control guidance related to modern computer systems. The management of human capital has gained recognition as a significant part of internal control. Furthermore, the private sector has updated its internal control guidance with the issuance of Internal Control - Integrated Framework, published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Consequently, in November 1999 GAO updated the standards for use in the government that provides the overall framework for establishing and maintaining internal control and for identifying and addressing major performance and management challenges and areas at greatest risk of fraud, waste, abuse, and mismanagement.<sup>1</sup> The standards are effective beginning with fiscal year 2000 and the Federal Managers' Financial Integrity Act reports covering that year.

Effective internal control helps in managing change to cope with shifting environments and evolving demands and priorities. As programs change and as agencies strive to improve operational processes and implement new technological developments, management must

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<sup>1</sup>*Standards for Internal Control in the Federal Government*, U.S. General Accounting Office (GAO/AIMD-00-21.3.1, November 1999).

continually assess and evaluate its internal control to assure that the control activities being used are effective and updated when necessary.

## BACKGROUND

OVAE is responsible for the coordination of all literacy related programs and policy initiatives in the Department. OVAE supports a wide range of programs and activities that help young people and certain adults obtain the knowledge and skills they need for successful careers and productive lives. Fiscal year 2000 OVAE appropriations totaled approximately \$1.7 billion.

Funding for the programs are made available through the Carl D. Perkins Vocational and Technical Education Act of 1998 (Perkins III or Perkins Act), Public Law 105-332; and through the Adult Education and Family Literacy Act (AEFLA), Title II of the Workforce Investment Act of 1998.

Under the Perkins Act, administered by the Division of Vocational-Technical Education (DVTE), federal funds are made available to help provide vocational and technical education programs and services to youth. The vast majority of funds appropriated each year are awarded in the form of grants to State Educational Agencies (SEAs). These grants are usually identified as Basic State Grants. Funds for the grants are allotted to States according to a formula based on the SEAs' populations in certain age groups and per capita income.

Under the AEFLA, administered by the Division of Adult Education and Literacy (DAEL), federal funds are made available to SEAs to manage the State-Administered Basic Grant programs. The funds enable out of school adults aged 16 and over to become literate and to complete high school so that they can succeed as workers, parents, and citizens. Funds are allotted to States according to a formula based on the number of adults (aged 16 and over) in each state who do not have a high school diploma or its equivalent, are beyond the age of compulsory school attendance, and are not enrolled in a secondary school.

States that desire to receive a vocational or adult education grant are required, to submit a State Plan (application) to the Department by April 1<sup>st</sup> of each year. The State Plan, valid for a 5-year period, describes and provides assurance on how federal funds will be used. Annual revisions of the State Plan may be submitted as often as an eligible SEA determines it necessary.

Upon receipt of the State Plan in OVAE, it is logged in and a review process takes place. DVTE and DAEL maintain different processes for reviewing the State Plan.

Upon receipt of a State Plan in which vocational funds are being requested, a team composed of individuals from DVTE and a liaison for the State perform an independent review of the State Plan based upon legislative guidelines and programmatic criteria. Results of the independent reviews are documented. The team then convenes to discuss and evaluate the State Plan. A master checklist, along with supporting documentation that summarizes the results of the evaluation, is compiled by the State Liaison. An eligibility funding letter is drafted and electronically logged in for tracking purposes by DVTE. Prior to the funding letter being sent to the eligible SEA, it is reviewed and forwarded to the Assistant Secretary for signature.

The review process of a State Plan employs the services of an Area Coordinator and a review team within DAEL and a State Peer Reviewer employed by the SEA. The Workforce Investment Act of 1998 requires that all State Plans must undergo a "State Peer Review." To ensure this requirement is being fulfilled, the Area Coordinator determines if a State Peer Reviewer has made a request to review a specific State Plan. State Peer Reviewers are allowed to request a State Plan to review other than their State Plan. If the plan requested is available, the State Peer Reviewer will be assigned to it for review. If this plan is unavailable, the State Peer Reviewer will be assigned to review a State Plan at random. The review team within DAEL and the State Peer Reviewer are provided a copy of the State Plan and a review guide for review and approval. Results of the reviews are summarized, recommendations are made for further processing of eligible State Plans, and an eligibility letter is drafted based on allocation tables. Eligibility letters are then forwarded to the Assistant Secretary for signature.

A coordinated effort is undertaken with Budget Services, a component within the Office of the Under Secretary; the National Center for Education Statistics a component within the Office of Educational Research and Improvement; and OVAE to ensure the accuracy of the allocation tables for formula grant funding.

Once the eligibility letter has been signed by the Assistant Secretary for formula grant funding, a comparison is made of the total dollar amount in the eligibility letter to the amount in GAPS, and funds are committed in GAPS. An interface then occurs with the Financial Management Support System (FMSS) so that the dollars are marked and not obligated elsewhere in the Department. Once funds have been committed, a grant award notification letter is sent to the grant recipient. Funds are obligated and available for draw down by the grant recipient once OVAE has completed the reconciliation of funds by comparing the total amount committed and obligated in GAPS to the amount on the grant award notification letter.

## RESULTS

Based on the results of our review, we have identified several areas where enhanced controls and needed operational changes, if properly implemented, will reduce the risk of erroneous payments in the formula grant disbursement process.

Our review of this process disclosed that:

- Policies and procedures are not in place for DAEL approval and monitoring of requests made by State Peer Reviewers. State Peer Reviewers are usually assigned to review State Plans for compliance with policy and grant guidelines. However, State Peer Reviewers are allowed to request to review a specific State Plan other than their own. With an approval and monitoring process, a State Peer Reviewer could be limited to a specific number of consecutive reviews of a specific state's Plan. Management recognized, in our discussions with them, that there is a need to develop policies and procedures that clearly define the process for the approval and monitoring the requests made by the State Peer Reviewers. The approval and monitoring of requests by DAEL would help reduce the potential for complacency and ensure a greater degree of independence by the State Peer Reviewer.

- Reconciliations, comparing total funded amounts and individual award amounts in FMSS to amounts in GAPS, are performed on an informal basis and are not documented. Formal reconciliations would provide a reasonable assurance that the amount of funding that goes to the grant recipient is accurate.

### RECOMMENDATIONS

We recommend that the Assistant Secretary for Vocational and Adult Education:

1. Develop and establish a policy and procedure for approving and monitoring State Peer Reviewer requests.
2. Establish procedures and perform formal reconciliations to ensure the total funded amounts and the individual award amount in FMSS agrees with amounts in GAPS.

### DEPARTMENT'S RESPONSE

The Department agreed with the overall content of the report and concurred with the recommendations. The response describes actions already taken or currently underway, and additional actions that OVAE plans to take by August 2001. These actions are responsive to the concerns expressed in the report, and a full corrective action plan will be developed by OVAE, pursuant to follow up and resolution practices of the Department. The Department's response is included in this report as Attachment I.

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This report is intended solely for the information and use of the management of the Department, OMB, Congress and the Department's OIG, and is not intended to be and should not be used by anyone other than these specified parties.

Attachments

*Ernst & Young LLP*

April 5, 2001  
Washington, D.C.




## UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF VOCATIONAL AND ADULT EDUCATION

JUN 15 2001

## MEMORANDUM

**TO:** Lorraine Lewis  
Office of the Inspector General

**FROM:** Robert D. Muller   
Deputy Assistant Secretary  
Office of Vocational and Adult Education

**SUBJECT:** DRAFT REPORT: Review of the Formula Grant Disbursement Process  
Within the U.S. Department of Education Office of Vocational and Adult  
Education  
(Audit Control Number: ED-OIG/S17-B0015)

This provides our responses to the draft report referenced above, which makes recommendations for improving the formula grants disbursement process within the Office of Vocational and Adult Education. We appreciate the opportunity to comment on this report both now and while it was being developed. We also concur with the specific recommendations made by your office and plan the following actions:

Develop and establish a policy and procedure for approving and monitoring State peer reviewer requests -- By August 1, 2001, the Procedures for Reviewing State Plans for the Division of Adult Education and Literacy will be revised to ensure the independence of State Plan Reviewers. The revised policies and procedures will address the concerns in the draft report. When completed, the procedures will be discussed with staff to ensure compliance with new procedures. In addition, OVAE will provide a copy of the revised procedures to the Office of the Inspector General.

Establish procedures and perform formal reconciliations to ensure the total funded amounts and the individual award amount in FMSS agrees with the amounts in GAPS -- Upon obligation of State formula grants in July of each year, OVAE Executive Office staff will run a report that reconciles the total funded amounts in FMSS with the amounts awarded in GAPS.

Thank you again for the opportunity to review this draft report. If you have any questions concerning this response, please contact Richard Smith of my staff at 205-8974.