MEMORANDUM REPORT ON REVIEW OF CENTER FOR TECHNOLOGY ENTERPRISE, INC. (CITE) BOWLING GREEN, KENTUCKY

APPALACHIAN REGIONAL BROADBAND DEMONSTRATION

ARC Grant Number: KY-14974

Grant Period: October 1, 2004 through July 31, 2006

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Report Number: 08-12

Date: June 23, 2008

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APPALACHIAN REGIONAL BROADBAND DEMONSTRATION

ARC Grant Number: KY-14974

Grant Period: October 1, 2004 through July 31, 2006

Prepared By:

Tichenor & Associates, LLP
Certified Public Accountants
304 Middletown Park Place, Suite C
Louisville, Kentucky 40243

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TICHENOR & ASSOCIATES, LLP

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TO:	Appalachian Regional Commission (ARC) Office of Inspector General (OIG)
FROM:	Tichenor & Associates, LLP Louisville, Kentucky
REPORT FOR:	The Federal Co-Chairman ARC Executive Director OIG Report Number: 08-12
SUBJECT:	Memorandum Review Report on Center for Technology Enterprise, Inc. (CITE), Appalachian Regional Broadband Demonstration, ARC Grant Number: KY-14974.

PURPOSE: The purpose of our review was to determine if (a) the total funds provided to CITE (formerly known as Center for Information Technology Enterprise, Inc.) for its Appalachian Regional Broadband Demonstration grant were expended in accordance with the ARC approved grant budget and did not violate any restrictions imposed by the terms and conditions of the grant; (b) the accounting, reporting, and internal control systems provided for disclosure of pertinent financial and operating information; and (c) that the objectives of the grant are being met.

BACKGROUND: ARC awarded Grant Number KY-14974 to CITE for the period October 1, 2004 through January 31, 2006. The ARC Project Coordinator approved Amendment Number 1 to the Grant Agreement on January 23, 2006 extending the period of performance through July 31, 2006. Total ARC funding for the period was for an amount not to exceed $180,000 or 50.0% of actual, reasonable, and eligible project costs. ARC required that the grant be matched with $180,000 or 50.0% in cash, contributed services, and in-kind contributions, as approved by the ARC.

The purpose of the grant was to provide assistance to undertake an assessment of broadband telecommunications needs and deployment in a six county area of Appalachian Kentucky. Furthermore, the grant would underwrite a GIS mapping assessment project in the six counties to determine what telecommunications services are currently available; the development of leadership teams in communities; locate state

owned towers and other facilities that could be used to deploy technologies on; and assist communities to develop an on-line presence.

SCOPE: We performed a program review of the grant as described in the Purpose above. Our review was based on the terms of the grant agreement and on the application of certain agreed-upon procedures previously discussed with the ARC OIG. Specifically, we determined if the tasks described above were being performed, if the accountability over ARC funds is sufficient as required by applicable Office of Management and Budget (OMB) Circulars, and if CITE was in compliance with the requirements of the grant agreement. In addition, we discussed the program objectives and performance with CITE personnel. Our results and recommendations are based upon those procedures. These review procedures were performed in accordance with applicable Government Auditing Standards.

RESULTS: The following results are based on our review performed at CITE in Bowling Green, Kentucky, on March 5, 2007 through May 9, 2007.

A. Incurred Costs

CITE's financial records report total program costs of $495,990 for the grant period (see **Appendix A**). Of these costs, $180,000 (36.3%) was attributed to ARC expenditures, with the remaining $315,990 (63.7%) attributed to matching and in-kind expenditures.

During the course of the review, we reviewed the direct, indirect, and matching costs claimed and noted instances of noncompliance which are described in the accompanying findings.

1. Improper Allocation of Costs Charged to the ARC Grant

The grant agreement (see **Appendix B**) states that its purpose is to provide assistance to undertake an assessment of broadband telecommunications needs and deployment in a **six county** area of Appalachian Kentucky.

KY-14974 was part of CITE's statewide project *Prescription for Innovation*. CITE also received funding from ARC for grant KY-15056-05 – KY Broadband Prescription for Innovation Initiative – to fund an additional **fifteen county** area of Appalachian Kentcky as part of the project. The period of performance for KY-15056-05, as amended, was January 1, 2005 through March 31, 2007. It was CITE's intention to apply for two additional fifteen-county grants so all of Kentucky's 51 Appalachian counties would be funded by ARC; however, the remaining 30 counties were never funded by ARC.

Because of CITE's original intent to fund all of Kentucky's Appalachian counties with ARC grants, an accounting system was developed to capture all ARC project costs irrespective of county. This accounting system remained in place even after CITE learned that ARC would not be funding the remaining 30 Kentucky Appalachian counties.

Based on prior experience with ARC, where CITE was allowed to allocate 50 percent of statewide costs to ARC grant KY-14118, CITE began allocating the statewide *Prescription for Innovation* costs at a rate of 50 percent to this ARC grant, KY-14974. For the period October through December of 2004, all of the ARC allocation was charged to KY-14974 either for reimbursement from ARC or as matching costs. Beginning in January 2005, when ARC grant KY-15056-05 for an additional fifteen counties began, the ARC allocation (50% of statewide costs) was split between the two ARC grants based on the activity in the 21 counties of the two combined grants. In other words, **all** of the ARC allocation was charged to the two grants, which included six and fifteen counties, respectively, out of 51 Kentucky Appalachian counties. See **Appendix C** for CITE's description of their allocation method.

CITE's total reported program costs for KY-14974 of $495,990 (see **Appendix A**) is 9.7% of the total recorded statewide program costs of $5,112,393 for *Prescription for Innovation* (see **Appendix D** – Total Costs of *Prescription for Innovation*), while representing only 5% (6 of 120) of Kentucky's counties, and is disproportionately large compared to the six counties to be served under this grant. Because of the improper allocation of costs, any reported costs out of proportion to the total reported statewide program costs should be disallowed.

After reducing total reported program costs to 5% of total reported statewide program costs, total program costs are $255,620, of which $127,810 (50%) is attributed to ARC costs and $127,810 (50%) attributed to matching and in-kind costs.

Recommendation:

We recommend that ARC require that CITE revise its final Request for Advance or Reimbursement (Standard Form 270) submitted to ARC to show total grant costs of $255,620, with $127,810 attributed to ARC costs and $127,810 attributed to matching and in-kind costs.

We also recommend that ARC require CITE to return $52,190 of disallowed ARC costs. (See **Appendix E** – Calculation of Disallowed Costs Charged to the ARC Grant.)

ARC's Response:

Concurrent with our review of KY-14974, we also reviewed CITE's ARC grant KY-15056-05 (see OIG Report Number 08-13). ARC's written response addresses both draft reports.

ARC stated that although CITE maintains that all grant expenditures for KY-14974 and KY-15056-05 were incurred in the approved project area, CITE agrees with the accuracy of the audit finding that its record-keeping does not support a county-by-county attribution of costs. ARC further stated that during discussions with CITE to resolve this issue, CITE renewed a previously made request to expand the project service area to include all 51 Kentucky Appalachian counties.

On May 23, 2008, ARC agreed to CITE's request to expand the project service area to include all 51 Kentucky Appalachian counties and to apply the multi-county match rate of 80% ARC funding to CITE's 20% match in cash, contributed services, and in-kind contributions.

CITE recorded total statewide program costs for *Prescription for Innovation* of $5,112,393 (see **Appendix D** – Total Costs of *Prescription for Innovation*). Because the expanded service area represents 42.5% (51 of 120) of Kentucky's counties, CITE's recalculated total program costs for both KY-14974 and KY-15056-05 is $2,172,767 (42.5% of $5,112,393), of which $1,738,214 (80%) is attributed to eligible ARC costs and $434,553 (20%) attributed to matching and in-kind costs. (See **Appendix F** – ARC's Response.)

Auditor's Comment:

ARC agreed to CITE's request to expand the project service area for both KY-14974 and KY-15056-05 to all of Kentucky's 51 Appalachian counties and the recalculated total eligible ARC costs of $1,738,214 is greater than the $1,080,00 of combined funding ($180,000 for KY-14974 and $900,000 for KY-15056-05) provided by ARC. As a result, the recommendation is considered closed.

2. Predetermined budget estimates were used to directly and indirectly charge personnel salary and benefits costs to the ARC grant and were not adjusted to actual costs as required by Federal cost principles

OMB Circular A-122 (Cost Principles for Non-Profit Organizations), Attachment B – Selected Items of Cost, para. 8.m.(2)(a) states that reports of salaries and wages must reflect an after-the-fact determination of the actual activity of each employee. Budget estimates, such as estimates determined before the services are performed, do not qualify as support for charges to awards and are expressly unallowable. OMB Circular A-122 does allow for the interim use of estimated costs provided they are adjusted to actual costs at least annually.

Additionally, OMB Circular A-122, Attachment A – General Principles, para. A.2.(b) states that to be allowable under an award, costs must conform to any limitations or exclusions set forth in the principles or in the award as to types or amount of cost items.

The budget narrative to the grant application states "Employees' time will be charged directly to the project based on actual time records maintained;" however, CITE used predetermined estimates for personnel to direct charge a portion of their salary and benefits to ARC and other programs. Personnel salary and benefit costs charged based on these estimates were not adjusted to actual costs prior to the final request of reimbursement. These estimates were based on employee's anticipated role in the project, rather than actual data. See **Appendix C** for CITE's description of their allocation method.

CITE's President and CEO stated that they did not establish a time reporting system that tracked county specific time because of the administrative burden that placed on their project managers who were often working in numerous counties daily.

For KY-14974, CITE reported personnel salary costs of $203,143, with $88,272 attributed to ARC costs and $114,871 attributed to matching and in-kind costs, and associated fringe benefits of $32,370, with $13,645 attributable to ARC costs and $18,725 attributable to matching and in-kind costs. Because CITE used predetermined estimates, and not actual costs, these amounts should be disallowed.

Recommendation:

Because personnel salary and associated fringe benefits, combined, are $235,513 (47.5%) of the total reported grant costs of $495,990, we recommend that ARC require that CITE further revise its final Request for Advance or Reimbursement (Standard Form 270) submitted to ARC to show total grant costs of $134,200 (a reduction of $121,420 or 47.5% from the revised total grant costs calculated in Finding #1, above), with $67,100 (50%) attributed to ARC costs and $67,100 (50%) attributed to matching and in-kind costs.

We also recommend that ARC require CITE to return an additional $60,710 of disallowed costs. (See **Appendix E** – Calculation of Disallowed Costs Charged to the ARC Grant.)

ARC's Response:

Concurrent with our review of KY-14974, we also reviewed CITE's ARC grant KY-15056-05 (see OIG Report Number 08-13). ARC's written response addresses both draft reports.

ARC stated that CITE agreed with our finding related to the disallowance of personnel salary and fringe benefits costs but asked, in connection with the above mentioned request in Finding #1 to expand the project service area, for the allowance of costs associated with the work of two individuals whose activities were almost exclusively in the Appalachian portion of Kentucky.

On May 23, 2008, ARC agreed to CITE's request and accepted as eligible the personnel salary and fringe benefits costs proposed by CITE prorated at 42.5%, which is the proportion of ARC counties to all Kentucky counties, while disallowing the balance of personnel salary and fringe benefits costs.

Personnel salary and fringe benefits represented approximately 47% of the total reported project costs for KY-14974 and KY-15056-05, combined. Disallowing 47% of the recalculated total program costs attributable to ARC ($1,738,214, see ARC's Response to Finding #1, above) results in a reduction of $816,960 of personnel salary and fringe benefits costs, leaving eligible non-personnel project costs of $921,254.

Prorating by 42.5% the $312,558 of salary and fringe benefits of the two individuals whose activity was almost exclusively in the Appalachian portion of Kentucky results in $132,837 of personnel salary and fringe benefits costs accepted as eligible by ARC.

Combining the ARC's share of eligible non-personnel costs of $921,254 and $132,837 of eligible personnel salary and fringe benefits costs, ARC has accepted final costs for KY-14974 and KY-15056-05, combined, of $1,054,091. Because $1,080,000 was previously disbursed for these two grants, ARC requested that CITE return $25,909 of unsubstantiated personnel salary and fringe benefits costs. CITE returned the funds to ARC on June 2, 2008. (See **Appendix F** – ARC's Response.)

Auditor's Comment:

ARC disallowed $816,960 of personnel salary and fringe benefits costs, less an allowance of $132,837 of salary and fringe benefits for two individuals whose activity was almost exclusively in the Appalachian portion of Kentucky, resulting in final accepted costs of $1,054,091 and CITE returning $25,909 of unsubstantiated personnel salary and fringe benefits costs. As a result, this recommendation is considered closed.

B. Internal Controls

During the course of the audit, we reviewed CITE's system of internal controls. One area of weakness was identified that could have affected the accountability of costs or compliance with the terms of the grant agreement.

1. Completion of Progress Reports

The grant agreement requires that CITE complete an interim progress report for each 120-day period. The grant agreement also requires that a draft final report be submitted for ARC approval within one month of the end of the period of performance.

CITE submitted a draft final report to ARC on September 15, 2006. This was 46 days after the end of the period of performance, which ended July 31, 2006

Recommendation:

We recommend that ARC require CITE to complete final progress reports in a timely manner on any future ARC grants.

ARC's Response:

ARC did not respond to this recommendation.

Auditor's Comment:

ARC has not commented on the recommendation. As a result, we continue to make this recommendation.

C. Program Results

Our review of CITE's Appalachian Regional Broadband Demonstration grant indicated that the specific objectives identified in the grant were achieved.

Tichenor & Associates, LLP
Louisville, Kentucky
November 2, 2007

APPENDIX A

FINAL REQUEST FOR ADVANCE OR REIMBURSEMENT (STANDARD FORM 270) AND WORKSHEET FOR REIMBURSEMENT REQUEST

REQUEST FOR ADVANCE OR REIMBURSEMENT

OMB APPROVAL NO.	PAGE	OF
	1	1

1. TYPE OF PAYMENT REQUESTED	a. "X" one or both boxes		2. BASIS OF REQUEST
	☐ ADVANCE	■ REIMBURSEMENT	☐ CASH
	b. "x" the applicable box		■ ACCRUAL
	■ FINAL	☐ PARTIAL	

3. FEDERAL SPONSORING AGENCY AND ORGANIZATIONAL ELEMENT TO WHICH THIS REPORT IS SUBMITTED	4. FEDERAL GRANT OR OTHER INDENTIFYING NUMBER ASSIGNED BY FEDERAL AGENCY	5. PARTIAL PAYMENT REQUEST NUMBER FOR THIS REQUEST
Appalachian Regional Commission	KY-14974-0-I	

6. EMPLOYER IDENT. NUMBER	7. RECIPIENT ACCOUNT NUMBER OR ID NUMBER	8. PERIOD COVERED BY THIS REQUEST	
		FROM (month, day, year)	TO (month, day, year)
61-1394934		4/1/2006	6/30/2006

9. RECIPIENT ORGANIZATION	10. PAYEE (Where check is to be sent if different than item 9)
Name: Center for Technology Enterprise, Inc.	Name:
Number and Street: P.O. Box 3448	Number and Street:
City, State, and ZIP Code: Bowling Green, KY 42102-3448	City, State, and ZIP Code:

11. COMPUTATION OF AMOUNT OF REIMBURSEMENTS/ADVANCES REQUESTED

PROGRAMS/FUNCTIONS/ACTIVITIES	(a)	(b)	©	TOTAL
a. Total program outlays to date (As of date) 6/30/06	495,990.36			495,990.36
b. Less: Cumulative Program Income				-
.Net Program outlays (Line a minus line b)	495,990.36			495,990.36
d. Estimated net cash outlays for advance period				-
e. Total (Sum of lines c & d)	495,990.36			495,990.36
f. Non-Federal share of amount on line e	315,990.36			315,990.36
g. Federal share of amount on line e	180,000.00			180,000.00
h. Federal payments previously requested	162,000.00			162,000.00
i. Federal share now requested (Line g minus h)	18,000.00			18,000.00
j. Advances required by month, when requested by Federal grantor agency for use in making prescheduled advances — 1st Month				
2nd Month				
3rd Month				

12. ALTERNATE COMPUTATION FOR ADVANCES ONLY

a. Estimated Federal cash outlays that will be made during period covered by the advance	$
b. Less: Estimated balance of Federal cash on hand as of beginning of advance period	
c. Amount requested (Line a minus line b)	$

13. CERTIFICATION

I certify that to the best of my knowledge and belief the data on this form are correct and that all outlays were made in accordance with the grant conditions or other agreements and that payment is due and has not been previously requested.	Signature of Authorized Certifying Official	Date Request Submitted: September 15, 2006
	Typed or Printed Name and Title: Bernie Bogle, Chief Financial Officer	Telephone Number: (270) 781-4320 x 128

This space for agency use

Worksheet for Reimbursement Request

Appalachian Regional Broadband Demonstration
ARC Grant #: KY-14974

Reimbursement Period from 10/1/2004 to 6/30/2006

Approved Budget Category	Approved Budget	Actual Matching (Non-ARC) Cost	Actual ARC Cost	Total Cost	Total Program Outlays to Date	Budget Balance Remaining
Personnel	$ 159,156.00	$ 114,871.00	$ 88,272.25	$ 203,143.25	$ 203,143.25	$ (43,987.25)
Fringe Benefits	31,830.00	18,725.58	13,644.57	32,370.15	32,370.15	(540.15)
Travel	38,800.00	9,194.98	6,087.56	15,282.54	15,282.54	23,517.46
Equipment	-	-	-	-	-	-
Supplies	16,114.00	11,053.81	7,204.64	18,258.45	18,258.45	(2,144.45)
Contractual	42,100.00	112,380.70	28,790.98	141,171.68	141,171.68	(99,071.68)
Construction	-	-	-	-	-	-
Indirect Cost	72,000.00	49,764.29	36,000.00	85,764.29	85,764.29	(13,764.29)
Other Approved Line Items:	-	-	-	-	-	-
Subtotals	360,000.00	315,990.36	180,000.00	495,990.36	495,990.36	(135,990.36)
Lesss Cumulative Program Income	-	-	-	-	-	-
Total	$ 360,000.00	$ 315,990.36	$ 180,000.00	$ 495,990.36	$ 495,990.36	$ (135,990.36)

APPENDIX B

GRANT AGREEMENT

Grant Agreement
Between
Appalachian Regional Commission
and
Center for Information Technology Enterprises, Inc

ARC Contract Number: KY-14974-0-I

Project Title: Appalachian Regional Broadband Demonstration

Grantee: Center for Information Technology Enterprises, Inc
1711 Destiny Place, #108
Bowling Green, KY 42104

Grantee's EIN: 61-1394934
Project Director: Brian Mefford
Telephone Number: 270-781-4320

ARC Project Coordinator:
Harry Roesch
202-884-7774
Fax Number: 202.884.7691

State Administration/Liaison Officer:
Peggy Satterly / 502-573-2382

Part I - Special Provisions

1. Statement of Purpose - Incorporation of Proposal. This agreement implements a grant made under the authorities of Section 302 of the Appalachian Regional Development Act of 1965 (ARDA), as amended, to provide assistance to undertake an assessment of broadband telecommunications needs and deployment in a six county area of Appalachian Kentucky. The ARC grant will underwrite a GIS mapping assessment project in the six counties to determine what telecommunication services are currently available; the development of leaderships teams in communities; locate state owned towers and other facilities that could be used to deploy technologies on; and assist communities to develop an on-line presence.

   This project shall be carried out in general accord with Grantee's proposal, received at ARC on September 27, 2004. Grantee's proposal is incorporated by this reference as Supplement A to Part I. To the extent the Articles of this grant agreement conflict with the incorporated proposal, the Articles shall control.

2. Order of Precedence. This grant agreement is subject to the provisions of the ARDA, the ARC Code and Project Guidelines, the Special Provisions (Part I), the attached Grant Agreement: General Provisions (Part II), and any incorporated Supplements. Any conflict among these provisions shall be resolved giving precedence to these authorities in the order in which they are listed above.

3. Reports. A progress report for each 120-day period and a final report are required under this agreement (see Part II, Article 4).
4. Consideration and Method of Payment.
   - A. Total. For the complete and satisfactory performance of this grant agreement, as determined by ARC, Grantee shall be paid by ARC a total sum not to exceed $180,000 of actual, reasonable and eligible project costs. Grantee shall pay, or cause to be paid, the non-ARC share of $180,000 in cash, contributed services, or in-kind contributions as approved by ARC.
   - B. Method. Progress and advance payments not to exceed 90% of total ARC-approved funds are authorized under this agreement. Upon Grantee's satisfactory completion of the Agreement, Grantee shall receive any balance of funds, which may be due under this agreement (see Part II, Article 11).
5. Budget. Costs will be determined in general accord with the budget (which is attached as Supplement B to Part I and hereby incorporated into this agreement), subject to the terms of this Grant Agreement and to pertinent ARC Code Provisions.
6. Period of Performance. The grant period of performance shall be October 1, 2004 through January 31, 2006.

Period of performance extended to 7/31/06. See Amendment #1

Charles S. Howard
General Counsel

9.29.04
Date

Grantee's Authorized Representative

9/30/04
Date

BUDGET INFORMATION - Non-Construction Programs

OMB Approval No. 0348-0

SECTION A - BUDGET SUMMARY

Grant Program Function or Activity (a)	Catalog of Federal Domestic Assistance Number (b)	Estimated Unobligated Funds		New or Revised Budget		
		Federal (c)	Non-Federal (d)	Federal (e)	Non-Federal (f)	Total (g)
1. ARC	23.011	$	$	$ 180,000.00	$ 180,000.00	$ 360,000.00
2.						0.00
3.						0.00
4.						0.00
5. Totals		$ 0.00	$ 0.00	$ 180,000.00	$ 180,000.00	$ 360,000.00

SECTION B - BUDGET CATEGORIES

6. Object Class Categories	GRANT PROGRAM, FUNCTION OR ACTIVITY				Total
	(1) ARC	(2) Non-Federal	(3)	(4)	(5)
a. Personnel	$ 79,578.00	$ 79,578.00	$	$	$ 159,156.00
b. Fringe Benefits	15,915.00	15,915.00			31,830.00
c. Travel	19,400.00	19,400.00			38,800.00
d. Equipment					0.00
e. Supplies	8,057.00	8,057.00			16,114.00
f. Contractual	21,050.00	21,050.00			42,100.00
g. Construction					0.00
h. Other					0.00
i. Total Direct Charges *(sum of 6a-6h)*	144,000.00	75% 144,000.00	0.00	0.00	288,000.00
j. Indirect Charges	36,000.00	25% 36,000.00			72,000.00
k. TOTALS *(sum of 6i and 6j)*	$ 180,000.00	$ 180,000.00	$ 0.00	$ 0.00	$ 360,000.00
7. Program Income	$	$	$	$	$ 0.00

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Standard Form 424A (Rev. 7-97)
Prescribed by OMB Circular A-102

ARC Contract No. KY-14947

PART II
APPALACHIAN REGIONAL COMMISSION
GRANT AGREEMENT: GENERAL PROVISIONS

Article 1 General Procedures.

All ARC grants shall be administered as follows: grants to state and local government, in accord with OMB Circulars A-102 and A-87; grants to hospitals and other non-profit organizations, in accord with OMB Circulars A-110 and A-122; grants to higher educational institutions, in accord with OMB Circular A-110 and A-21; and other Federal regulations as applicable.

Article 2 Restrictions on Use of ARC Funds.

Grantee warrants that it is cognizant of Section 224(b)(1) of the ARDA, which prohibits the use of ARDA funds to assist businesses to relocate from one area to another; and that, further, in keeping with Commission policy, it will not utilize ARDA funds actively to engage in any activity, the purpose of which is to encourage businesses now operating in one state to relocate into another state. No funds provided under this agreement will be used to publish or distribute material which would solicit such relocation.

Article 3 Work Plan/Detailed Budget.

(1) Grantee shall submit, as required by the ARC Project Coordinator, a work plan and/or budget for any and/or all of the tasks specified in Part I.

(2) Prior to submission of any work plan and/or budget so required by the ARC Project Coordinator, no costs shall be eligible for reimbursement, except those costs directly related to the preparation of such work plan and/or budget. Within one week after receipt, ARC shall complete a preliminary review of the work plan and/or budget and shall immediately advise the Grantee either that it is unacceptable or that it is preliminarily approved. After such preliminary approval by ARC, the Grantee may proceed with work on the project immediately with such modifications in the work plan and/or budget as required by ARC. After approval by ARC all costs incurred for work performed after the effective date which are incurred in accord with the approved work plan and/or budget, and only such costs, shall be eligible for reimbursement.

Article 4 Reports.

(1) Progress Reports. Grantee shall prepare and submit to the ARC Project Coordinator, progress reports indicating the work accomplished under the agreement to date, any problems encountered and ameliorative actions taken, and a forecast of work for the next report period.

(2) Final Report.

(a) Draft; Contents. Within one (1) month after the period of performance (see Part I), Grantee shall prepare and submit to the ARC Project Coordinator for approval, a draft final report of all work accomplished under this Agreement including recommendations and conclusions based on the experience and results obtained.

(b) Review. After ARC review of the draft final report, which will be completed within 15 days after submission by the Grantee, the Commission will either (a) return to the Grantee the approved draft with such comments, including any requirements or suggestions for modifications as deemed necessary, or (b) require resubmission of the draft report if it is deemed necessary, in which case Grantee shall, within 15 days, submit another draft for review and comment.

(c) Final Submission. Within 15 days after receipt of the approved draft final report, the Grantee will prepare and submit to the Commission, through the ARC Project Coordinator, 2 copies of the approved report and a reproducible master.

Article 5 Contracting Procedures.

In contracting for services and/or purchasing equipment under this Agreement, Grantee shall assure that (1) all contracting shall be at prices and on terms most advantageous to the Grantee and to the project; and (2) all interested parties shall have a full and fair chance at doing business with the Grantee. Grantee shall arrange for all contracting through competitive bidding, or, if permitted by state law, other negotiating and contracting procedures that will assure compliance with (1) and (2) above.

Article 6 Subcontracting.

The Grantee shall not enter into subcontracts for any of the work contemplated under this Agreement without obtaining the prior written approval of the Project Coordinator, and subject to conditions and provisions as the Project Coordinator may deem necessary, in his/her discretion, to protect the interests of the Commission: Provided, however, that notwithstanding the foregoing unless otherwise provided herein, such prior written approval shall not be required for the purchase by the Grantee of articles, supplies, equipment and services which are both necessary for and merely incidental to the performance of the work required under this Agreement: Provided, further, however, that no provision of this article and no such approval by the Project Coordinator of any subcontract shall be deemed in any event or in any manner to provide for the incurrence of any obligation by the Commission in addition to the total grant amount and the Commission shall not be responsible for fulfillment of Grantee's obligations to subcontractors: Provided, further, that no subcontracting shall be deemed to relieve the Grantee of any obligations under this Agreement.

Article 7 Coordination and Non-Duplication.

In carrying out the project under this Agreement, Grantee shall assure that the planning, design work and implementation of activities are coordinated with activities conducted by Grantee under other related ARC grants, if any, and shall assure that there shall be no duplication of effort or funding under this

Agreement of any work or payments under those grants.

Article 8 Project Personnel.

ARC reserves the right to approve or disapprove the selection or continued participation of any personnel supported with funds made available under this Agreement.

Article 9 Compliance with Applicable Laws.

Grantee shall assure that all provisions of applicable federal, state, and local laws shall be complied with in the conduct of activities under this grant agreement. The ARC reserves the right to suspend or terminate this agreement in the event that applicable federal, state, and local laws and regulations are not complied with. Such right shall not be exclusive and does not affect rights and remedies provided elsewhere by law, regulation, or agreement.

Article 10 Retention of Rights.

Title to equipment purchased with grant funds resides with the Grantee and assignees and successors approved by ARC, but the equipment must be accounted for during and after the end of the project period. Accountability may be satisfied by continued use during its useful life in the same or other projects related to objectives of the ARC, as approved by ARC. If the equipment is disposed of or transferred during its useful life to a use outside the scope of the ARC objectives, an amount equal to the resale value or the value of the ARC share at the time of disposal must be deposited in the grant account if still open, or the federal share must be refunded to ARC or an ARC-designated successor. ARC reserves the right to transfer such equipment and title thereto or other interest therein, to ARC, or an agency of the federal government or to another Grantee, in the event equipment, leased or purchased with funds under this agreement, is no longer used primarily for the purposes for which it is dedicated under this agreement, or is not used in substantial accord with the applicable provisions of this agreement.

It shall be Grantee's responsibility to monitor all use to ascertain that all such equipment is being used primarily for the purposes outlined herein. Grantee may propose to ARC that the equipment be transferred to another agency or entity which could utilize it for the purposes outlined in this agreement. Such transfers shall be subject to prior approval by the ARC Project Coordinator and to the reservation of rights in this Article.

Article 11 Method of Payment.

(1) Progress Payments. Grantee may receive progress payments (a) on the basis of the work performed; (b) upon ARC concurrence as to reasonableness of costs and submission of Form SF 270 (Request for Advance or Reimbursement); and; (c) upon submission to ARC of, and with the same frequency as, progress reports; and (d) upon determination by the ARC that the requirements of the agreement are being met. The total of such progress payments shall not exceed ninety (90) percent of the total grant amount unless specifically authorized in Part I of this agreement.

(2) Advance Payments. Grantee may receive advances of funds, in amounts sufficient to meet scheduled payroll costs and other related costs, including payments to subcontractors on the following basis: (a) Grantee's certification that a firm commitment has been obtained from each employee appointed under this agreement, or that firm, formal subcontracts have been executed which will require payments for goods and services to be delivered during the period for which advance is sought; (b) upon submission of form SF 270 (Request for Advance or Reimbursement) and on the basis of cost estimates approved by the ARC Project Coordinator; (c) Grantee's certification that any previous advance has been exhausted (if previous advance has not been exhausted, this remainder must be used to meet scheduled expenses payable during the next period); any additional advance subject to ARC concurrence as to need; and (d) satisfactory progress on tasks specified in Part I and the incorporated proposal.

Total Advance Payments shall not exceed 90 percent of the total grant amount unless specifically authorized in Part I of this agreement.

(3) Final Payment. Upon Grantee's satisfactory completion of the Agreement, Grantee shall receive any balance of funds which may be due under this Agreement.

(4) Disbursements. All disbursements shall be for obligations incurred, after the effective date, in the performance of this Agreement, and shall be supported by contracts, invoices, vouchers and other data, as appropriate, evidencing the disbursements.

NOTE: All payment requests must show the 9-digit taxpayer identifying number (TIN) assigned by the Internal Revenue Service. For individuals, the Social Security Number serves as the TIN; for businesses, the Employer Identification Number serves as the TIN.

Article 12 Grant-Related Income.

Grant-related income means gross income earned by Grantee from grant supported activities and shall include, but not be limited to, income from service fees, sale of commodities, or usage or rental fees. All grant-related income shall be reported to ARC in the progress and final reports required by this Agreement.

Article 13 Rebates and Discharges from Liability.

Grantee agrees that any refunds, rebates or credits, or other amounts (including interest earned thereon) received by the Grantee (or any Assignee) shall be paid to the Commission to the extent that they are properly allocable to costs for which the Grantee has been reimbursed under this Article. Grantee will, when requested, assign such amounts to the Commission and execute such releases as may be appropriate to discharge the Commission, its officers and agents from liabilities arising out of this Agreement.

Article 14 Records / Audit.

(1) Grantee shall establish procedures to ensure that all records pertaining to costs, expenses, and funds related to the Agreement shall be kept in a manner which is consistent with generally accepted accounting procedures. The documentation in support of each action in the accounting records shall be filed in such a manner that it can be readily located. Grantee shall maintain custody of time records, payrolls, and other

data, as appropriate, to substantiate all services reported to the Commission as Contributed Services under this Agreement.
(2)All invoices, vouchers, statements of costs, and reports of disbursements of funds are subject to audit.
(3) Any payment may be reduced for overpayment(s) or increased for underpayment(s) on preceding invoices or vouchers. In the event of overpayment(s) ARC reserves the option of requiring the Grantee to reimburse the Commission for the amount of the overpayment(s).
(4) If Grantee has not provided either cash or contributed services of a value determined by the Commission to be sufficient to support the payments made by the Commission, or has failed to obligate or disburse any such sums for the purpose of this Agreement, the final payment shall be reduced, or the Grantee shall make an appropriate refund.
(5) The Grantee agrees that the Federal Co-Chairman of the ARC, the Comptroller General of the United States, the ARC, or the duly authorized representatives of any of them shall, until the expiration of three years after final payment under this Agreement, have access to and the right to examine any books, documents, papers, and records of the Grantee involving transactions related to this Agreement.
(6) The Grantee will, in each subcontract, require the subcontractor to agree to the application of the provisions of this article in a similar manner to the subcontractor's records relating to said subcontract.

Article 15 Indemnification.

Notwithstanding any other provisions of this Agreement, it is expressly agreed that:
(1) Grantee will carry out the program under this Agreement as an independent contractor and not as agent of the Commission;
(2) Grantee assumes sole and complete responsibility for the conduct of the program in such a manner as to assure the safety and welfare of all persons participating in or in any way involved in, or affected by, any activities conducted under this Agreement;
(3) The Commission, by its provision of funds for this project, undertakes no responsibility in this regard;
(4) Grantee shall indemnify and save harmless the Commission, its agents, officers and employees, from and against any and all claims, demands, suits, judgments, settlements, etc., for sums of money for or on account of personal injuries, property damage, or loss of life or property of any persons arising from or in any way connected with the performance of the project covered by this Agreement; and
(5) Further, the Grantee expressly releases the ARC from any liability for any losses or damages suffered by Grantee, directly or indirectly, from or in any way connected with the performance of this Agreement.

Article 16 Grantee's Principal Personnel.

The Project Director shall be responsible for the general guidance and overall supervision of Grantee's efforts. The Project Director shall maintain liaison with the Commission's Project Coordinator. In the event the replacement of the Project Director becomes necessary, the Grantee will advise the Commission, in writing, of the change. The Commission reserves the right to disapprove any proposed substitute or addition.

Article 17 ARC Representative.

The Project Coordinator is responsible for (i) providing liaison between the Commission and the Grantee, and (ii) obtaining approval of work accomplished by Grantee. The Commission may, in its discretion, change the Project Coordinator at any time, in which event it shall notify the Grantee in writing of the change.

Article 18 State Administration and Liaison Officer.

Grantee shall submit copies of all correspondence, reports and requests for payment required to be submitted to ARC simultaneously to the State Administration and Liaison Officer named in this Agreement.

Article 19 Disputes.

(1) Procedure. Except as otherwise provided in this Agreement, in the event of any dispute arising under this Agreement concerning a question of fact which is not disposed of by agreement, a decision regarding the dispute shall be rendered by the Executive Director. The Grantee may, within 20 days from receipt of the Executive Director's written decision, submit to the Commission's Contract Review Committee (ARC-CRC), a written request for a review to which the ARC-CRC shall respond in writing within 60 days. Alternatively, the Grantee and the Executive Director may mutually agree to select any alternative means of dispute resolution to resolve such dispute. The decision of either the ARC-CRC or the arbitrator retained for the purpose of dispute resolution, shall be final and conclusive. Pending final decision under either alternative, the Grantee shall proceed diligently with the performance of the Agreement in accordance with the Executive Director's decision.
(2) Consideration of Questions of Law. This Article does not predude the consideration of questions of law in connection with decisions provided for in the above paragraph; provided that nothing in this grant shall be construed as making final any decision of any administrative official, representative, or the ARC-CRC on a question of law.
(3) ARC Contract Review Committee. The ARC-CRC shall consist of the Federal Co-Chairman and the States' Co-Chairman or their appointed representatives. In a dispute in which one of the parties is either the State of the States' Co-Chairman or a Grantee from said State, the States' Vice Co-Chairman, or his/her representative, shall replace the States' Co-Chairman on the ARC-CRC for that dispute alone. Nothing herein shall operate in any way as a restriction on the powers of the Federal Co-Chairman or any state member of the Commission under the ARDA.

Article 20 Suspension/Termination for Cause.

The ARC shall have the right, upon written notice to the Grantee, to suspend or terminate this Agreement for cause, whenever the Federal Co-Chairman determines there is reasonable basis to believe there has been malfeasance, embezzlement, misappropriation, unauthorized application of federal funds or material false statement in the conduct of this Agreement or any other ARC grant agreement.

:le 21 Termination for Default.

The ARC may, by written notice to Grantee, terminate this Agreement in whole or in part in accordance with Part 52.249 of the Federal Acquisition Regulations' "Default (Fixed-Price Supply and Service)" clause in effect on the date of this Agreement including, but not limited to provisions regarding failure to perform due to causes beyond the control of Grantee, the status of completed and partially completed work after termination for default, excusable default, ARC's right to reprocure, and other remedies. Such regulations are incorporated by reference as part of this Agreement. The rights and remedies of the ARC provided in this Article shall not be exclusive and are in addition to any other rights and remedies provided by law or under this Agreement.

Article 22 Termination for Convenience.

The ARC may, by written notice to the Grantee, terminate this Agreement in whole or in part for the convenience of the Commission, whenever the ARC determines that such action is in its best interest. If this Agreement is so terminated, the rights, duties and obligations of the parties, including compensation of the Grantee, shall be in accordance with Part 49 of the Federal Acquisition Regulation in effect on the date of this Agreement and such regulations are incorporated by reference as part of this Agreement.

Article 23 Official Not to Benefit.

member or delegate to Congress, or resident Commis-ıer, shall be admitted to any share or part of this Agreement, or to any benefit that may arise therefrom; but this provision shall not be construed to extend to this Agreement if made with an incorporated entity for its general benefit.

Article 24 Covenant Against Contingent Fees.

The Grantee warrants that no person or selling agency has been employed or retained to solicit or secure this Agreement upon an agreement or understanding for a commission, percentage, brokerage, or contingent fee, excepting bona fide employees of bona fide established commercial or selling agencies maintained by the Grantee for the purpose of securing business. For breach or violation of this warranty the Commission shall have the right to annul this Agreement without liability or in its discretion to deduct from the grant amount or consideration, or otherwise recover, the full amount of such commission, percentage, brokerage, or contingent fee.

Article 25 Equal Opportunity.

Grantee shall carry out all programs and activities in compliance with Title VI of the Civil Rights Act of 1964, and other federal laws prohibiting discrimination, and in such a manner that no person shall, on the grounds of race, color, national origin, religion, sex, age or disability be excluded from participation in, be denied the benefits of, or be subject to discrimination with respect to any such programs or activities.

Article 26 Patent Rights.

All research and development grants are subject to the government-wide Patent Policies outlined in Department of Commerce regulations (37 CFR Part 401).

Article 27 Statement of Federal Funding.

When issuing statements, press releases, requests for proposals, bid solicitations, and any and all other public documents or announcements describing the project or program funded by this Agreement, Grantee agrees and warrants that it shall clearly state:(1) the percentage of the total cost of the program or project which will be financed with federal money, and (2) the dollar amount of federal funds for the project or program.

Article 28 Lobbying.

No funds made available under this Agreement may be used in any way, directly or indirectly, to influence congressional action on any legislation or appropriation matters pending before Congress; however, this Article does not bar communications with Members of Congress as described in Title 18, section 1913, of the U.S. Code.

Article 29 Copyrights

The Federal Government, through the Appalachian Regional Commission (ARC), reserves a royalty-free, nonexclusive, and irrevocable license to reproduce, publish or otherwise use, and to authorize others to use, for federal government purposes, any work developed under a contract, grant, subgrant, or contract under a grant or subgrant, and to use, and authorize others to use, for federal government purposes, any rights of copyright to which a grantee, a subgrantee or a contractor purchases ownership with grant support or contact funds. Such license to use includes, but is not limited to, the publication of such work on an ARC Web site. Use of such works for purposes related to Appalachia and the development of the Region is generally authorized by ARC to State and local governments in the ARC Region and to other public and private not-for-profit organizations serving the Region, including the Appalachian Local Development Districts.

Appalachian Regional Commission
1666 Connecticut Avenue NW, Suite 700
Washington, DC 20009

AMENDMENT TO CONTRACT: Changes in length, funds, budget, or scope of project.
Amendment No:1
Date: 1/23/2006

ARC Project Number/Title:
KY-14974
Appalachian Regional Broadband Demonstration

Grantee:
Center for Information Technology Enterprises, Inc
1711 Destiny Place, #108
Bowling Green, KY 42104

Contact: Brian Mefford
Phone: 270-781-4320
Email: bmefford@connectky.org

ARC Project Coordinator:
Harry Roesch
Phone: 202-884-7774
Fax: 202-884-7691
Email: hroesch@arc.gov

☒**Change in Performance Period**
The above referenced agreement is amended by extending the period of performance.
The new period of performance is 10/1/2004 to 7/31/2006.

☐**Personnel Change**

☐**Other Amendment. Describe the amendment(s) in the box below.**

The grantee has found that their original 6-8 week planning / aggregation of demand process will actually take as much as 12-20 weeks to accomplish per county. Therefore, they need to extend the contract in order to accomplish the work program.

Additional Amendment Comment

Harry Roesch-Jan 23 2006 12:20PM (Program Manager)

Henry King-Jan 23 2006 2:21PM (Division Director)

APPENDIX C

GRANTEE'S DESCRIPTION OF ALLOCATION METHOD

Governor Fletcher's *Prescription for Innovation*

Grant Number KY-14974
(Demonstration Project – 6 County Grant)
and
Grant Number KY-15056-05
(15 County Grant)

Governor Fletcher's *Prescription for Innovation* was launched on October 1, 2004 as a comprehensive, statewide plan to accelerate technology growth, particularly in the areas of broadband deployment and technology literacy and usage (Attachment A). The initiative maintains four key goals for impacting economic development, which include:

1. Full broadband deployment by the end of 2007;
2. Dramatically improved use of computers and the Internet by all Kentuckians;
3. A meaningful online presence for all Kentucky communities, to improve citizen services and promote economic development through e-government, virtual education, online healthcare; and
4. eCommunity Leadership Teams in every county – local leaders assembled to develop and implement technology growth strategies for local government, business and industry, education, healthcare, agriculture, libraries, tourism and community-based organizations.

Statewide Nature of Governor Fletcher's *Prescription for Innovation*

The Center for Technology Enterprise, Inc. (CiTE) was awarded two grants to implement Governor Fletcher's *Prescription for Innovation* in the ARC region: a demonstration project grant that included 6 counties (KY-14974) and a grant that included 15 counties (KY-15056-05). When the application for grant number KY-15056-05 was filed with the Kentucky ARC office in December, 2004, the request was for a three year grant to implement the initiative in the remaining 45 ARC counties (Attachment B). We were told by the Kentucky ARC office that the ARC would only consider funding one year at a time but they would set the expectation that additional funding requests would be made for years two and three of the project with each request providing for an additional 15 counties. Our intent, based on previous experience with the ARC, was that the *Prescription for Innovation* grant would amend the initial 6 county grant yielding one grant spanning 3¼ years and encompassing the entire Kentucky ARC region.

A portion of the *Prescription for Innovation* was county specific, the eCommunity Leadership Teams and their Strategic Technology Plans in particular, but to a large degree the initiative was statewide in nature because of our broadband availability map (Attachment C). CiTE produced and updated custom GIS based maps that provided accurate intelligence regarding the technology characteristics of Kentucky and its' communities and an assessment of the existing and evolving inventory of broadband. CiTE worked with all broadband providers – independent and competitive telecommunications companies, cable providers, wireless Internet service providers, rural

cooperatives and municipals, and others – to gather, format, and map broadband service within a GIS format. The resulting map was a geographic representation of where broadband service existed, and more importantly, where it did not exist. Pinpointing service gaps allowed for the creation of strategy and policy to fill them.

Once the statewide inventory of broadband service was mapped with accuracy, that data was then leveraged for the sake of broadband buildout by quantifying demand for broadband service; in essence creating telecommunications market analysis. In addition to a demand creation effort at the grassroots level, market intelligence was established through further analysis of the broadband availability map. CiTE constructed market data in underserved areas that were otherwise unavailable to providers. These data included maps illustrating household totals (Attachment D) and density (Attachment E) at the most granular Census block level. These maps were and are critical in building the business case for deployment in rural areas.

Because of the comprehensive statewide nature of the *Prescription for Innovation* and the intent that the grant would eventually be one grant for the entire ARC Kentucky region, an accounting system was developed that would capture all ARC project costs irrespective of county. Seven months into the project in the midst of the grant request and approval process for KY-15056-05 we learned that the ARC would split the initiative into two separate grants: a 6 county demonstration project grant and a *Prescription for Innovation* 45 county grant. The comprehensive nature of the initiative, including the challenges of considering this a county-by- county project, was articulated to the ARC.

On June 3, 2005, ConnectKentucky filed our 2006 pre-application with the Kentucky ARC office (Attachment F) to request funding for 15 additional counties. At this time the 2005 grant (KY-15056-05) had yet to be approved and was later approved on June 23, 2005. In late January or early February, 2006, ConnectKentucky learned that ARC would not fund the additional phases for the remaining 30 ARC counties. As a result, a full 2006 ARC application was never submitted. If subsequent grants for the remaining 30 counties had been awarded as initially projected, the allocation system described below would have functioned efficiently and adequately.

Description of Allocation Method

CiTE has a long-standing relationship with the Appalachian Regional Commission that began at the inception of our organization in 2001. Our first project, ConnectKentucky, was a statewide three year research assessment of how prepared Kentucky was to participate in the networked world. Funding was received from the Commonwealth of Kentucky, from private corporate partners and from the ARC. Since the ARC region comprised 51 of Kentucky's 120 counties and with 32 of those ARC counties being distressed, the ARC agreed to allow CiTE to allocate 50 percent of the statewide costs to their grant. The ConnectKentucky project became so well known throughout the state that our organization began doing business as ConnectKentucky.

Utilizing the precedence of the ConnectKentucky project allocation determined in conjunction with ARC staff, we began allocating the statewide *Prescription for Innovation* cost at a rate of 50 percent to ARC. For the time period of October through December of 2004, all of that cost was charged to the 6 county grant either for reimbursement from the ARC or as match on the grant. Beginning in January 2005 when the 15 county grant began, we began splitting the ARC cost based on the activity in the 21 counties as recorded on our counties engaged spreadsheet (Attachment G). This spreadsheet documented the progress of the eCommunity Leadership Teams in each of Kentucky's 120 counties.

The percent of county meetings held in the 6 counties verses the percent of county meetings held in the 15 counties was used to determine the split between the two grants for that given month. For example, if in June there were 3 meetings in the 6 county area and 7 meetings in the 15 county area (a total of 10 meetings in June) 30 percent of the ARC costs were charged to the 6 county grant and 70 percent of the costs were charged to the 15 county grant.

The counties included in the 6 county grant (#KY-14974) are as follows:

- Bell
- Greenup
- Harlan
- Pike
- Rowan
- Wayne

Greenup, Harlan and Wayne counties were selected for the demonstration grant in October, 2004 and the remaining counties of Bell, Pike and Rowan were identified in January of 2005.

The counties included in the 15 county grant (#KY-15056-05) are as follows:

- Adair
- Bath
- Breathitt
- Clinton
- Floyd
- Johnson
- Knox
- Laurel
- Martin
- Menifee
- Morgan
- Perry
- Pulaski
- Rockcastle
- Wolfe

These counties were selected upon the approval of the *Prescription for Innovation* grant in late June 2005. Beginning in January 2005, ConnectKentucky was already working in many ARC counties and these specific 15 counties were selected based on our estimate, at the time, of the next 15 ARC counties to have the earliest expected date of completion.

Our project managers were assigned to 40 counties each based upon their geographical location. A statewide broadband territory map is attached (Attachment H) that details which project manager was assigned to each specific Kentucky county.

Allocation of Specific Costs

Personnel & Fringe

ConnectKentucky's time and effort from October 1, 2004 through December 31, 2006 was largely devoted to the *Prescription for Innovation*, with the exception of the No Child Left Offline initiative and hosting the RTC conference. Employees reported their hours worked weekly and a percent of their time was charged to the ARC based on their role in the initiative. A listing of the percent of payroll charged directly to ARC per employee is enclosed (Attachment I). We did not establish a time reporting system that tracked county specific time because of the administrative burden that placed on our project managers who were often working in numerous counties daily. Our project managers' primary focus was on executing their portion of the *Prescription for Innovation* in such a way as to facilitate the delivery of 40 county specific strategic technology plans and through the process of developing and delivering those plans, to build awareness and create demand for the use of broadband at a grassroots level throughout the Commonwealth. This approach proved successful in that all 120 county specific technology plans were delivered by December 31, 2006. The Rowan County Strategic Technology Plan is included with this report as an example.

Employee fringe benefits were allocated in the same manner as payroll.

Travel

Travel costs for mileage were based on the current Standard Federal Mileage Rate, actual cost was paid for lodging and per diem was utilized for meals and incidentals (based on the current Federal Rates). Travel costs for Joe Mefford, the Statewide Broadband Director, were charged 50 percent to ARC as his activities were statewide in nature. Travel costs for Ernie Wood, the East Region Project Manger, were charged 100 percent to ARC as he primarily focused on the ARC region. All other travel costs were allocated based on the destination or nature of the travel.

Supplies

Supplies and materials used directly for the county specific technology plans were charged 50 percent to the ARC. Supplies for the specific use of a project manager were charged as follows:

East Region – 100% ARC
Central Region – 50% ARC
West Region – 0% ARC

Beginning in January, 2006, a direct allocation of office supplies was made based on the percent of full-time equivalent staff in the broadband group working in an office compared to all of the full-time staff in that office.

Contractual

Most of our contractual expenses were charged to the ARC based on the location or nature of the work performed. The Kentucky League of Cities, Inc. was a contractor

utilized to provide for the role of the Statewide Broadband Director and was charged 50 percent to the ARC. Another contractor, Eric Mills, LLC, was engaged to provide additional project management services in the eastern region and was charged 100 percent to the ARC.

Indirect Charges

Indirect costs were charged to the ARC based on the percent included on the original applications. For example, on the 6 county grant the ARC direct cost was $144,000 and the ARC indirect cost was $36,000. The percent of indirect cost of direct cost is 25 percent, so for every dollar of direct cost charged to the ARC an additional $0.25 was charged for indirect cost.

APPENDIX D

TOTAL COSTS OF *PRESCRIPTION FOR INNOVATION*

10:35 AM
03/13/07
Accrual Basis

ConnectKentucky - see Note 1
Profit & Loss
October 2004 through December 2006 - see Note 2

All expenses except RTC conference and NCLO.

	Oct '04 - Dec 06
Ordinary Income/Expense	
Expense	
Consultants	668,281.18
Development	31,000.00
Event Expenses	45,250.07
Insurance	35,643.60
Marketing & Promotions	112,735.10
Miscellaneous	40,271.39
Office Expenses	249,888.41
Payroll Expenses	2,716,436.84
Postage and Delivery	28,549.33
Printing and Publications	131,764.53
Professional Development	9,883.61
Professional Fees	31,891.74
Rent	155,486.19
Repairs & Maintenance	49,046.78
Research	169,881.85
Supplies	75,279.58
Telephone	143,372.65
Travel	260,501.63
Utilities	34,115.99
Total Expense	4,989,280.47
Other Income/Expense	
Other Expense	
In-Kind Services	100,400.00
In-Kind Marketing	14,925.73
In-Kind Office Expense	7,787.00
Total Other Expense	123,112.73
Total Expense	5,112,393.20

Note 1: ConnectKentucky is the dba of Center for Technology Enterprise, Inc.

Note 2: Even though the grant period for KY-15056-05 ran through March 31, 2007, Prescription for Innovation was completed December 31, 2006.

APPENDIX E

CALCULATION OF DISALLOWED COSTS CHARGED TO THE ARC GRANT

CENTER FOR TECHNOLOGY ENTERPRISE, INC. (CITE)
ARC GRANT NUMBER: KY-14974

CALCULATION OF DISALLOWED COSTS CHARGED TO THE ARC GRANT

Finding # 1: Improper Allocation of Costs Charged to the ARC Grant

	Total Costs	% of Total	# of Counties	% of Total	Average Cost per County
KY-14974	**$ 495,990**	**9.7%**	**6**	**5.0%**	**$ 82,665**
KY-15056-05	1,158,816	22.7%	15	12.5%	77,254
All other counties	3,457,587	67.6%	99	82.5%	34,925
Totals - *Prescription for Innovation*	$ 5,112,393	100.0%	120	100.0%	42,603

	Total - *Prescription for Innovation*	$ 5,112,393	
	% of counties included in grant	x .05	
(1)	Revised total grant costs	$ 255,620	
	Less matching and in-kind share (50%)	(127,810)	
	Revised ARC share (50%)	$ 127,810	
	Less original ARC share	(180,000)	
	Disallowed costs charged to the ARC grant		$ (52,190)

Finding #2: Predetermined budget estimates used to charge personnel salary and benefits costs to the ARC grant

Costs reported to ARC for KY-14974:		
Personnel salary costs	$203,143	
Fringe benefits costs	32,370	
Total reported personnel salary and fringe benefits costs	$235,513	
% personnel salary and fringe benefits costs ($235,513 / $495,990)	47.5%	

	Revised total grant costs - from (1) above	$ 255,620	
	% personnel salary and fringe benefits costs	x .475	
	Disallowed personnel salary and fringe benefits costs	$ (121,420)	
	Less matching and in-kind share (50%)	60,710	
	Disallowed ARC personnel salary and fringe benefits costs		$ (60,710)

Proposed Final Worksheet for Reimbursement Request after Disallowed Costs Charged to the ARC Grant

Approved Budget Category	Allowable Matching Cost	Allowable ARC Cost	Allowable Total Cost
Personnel	$ -	$ -	$ -
Fringe Benefits	-	-	-
Travel	3,937	3,937	7,874
Equipment	-	-	-
Supplies	4,703	4,703	9,406
Contractual	36,366	36,366	72,732
Construction	-	-	-
Indirect Cost	22,094	22,094	44,188
Totals	$ 67,100	$ 67,100	$ 134,200

APPENDIX F

ARC'S RESPONSE

Date: June 10, 2008

To: Clifford Jennings, ARC Inspector General

From: Thomas Hunter, ARC Executive Director

Subject: Memoranda Reports of Kentucky Broadband Projects (KY-14974 & 15056)

Grantee: Center for Information Technology Enterprises, Inc. (CITI)/ ConnectKentucky

This memorandum contains ARC's agency response to the above-referenced audit reports of the ConnectKentucky projects. I have also attached the following relevant documents:

1. Letter from Brian Mefford, ConnectKentucky, to Harry Roesch, ARC, dated April 10, 2008, containing Grantee's response to the audit reports and its renewed request for a change of project scope;
2. ARC Approval Memorandum, dated April 23, 2008, approving Grantee's request;
3. Letter from Charles Howard, ARC General Counsel, to Brian Mefford, dated May 23, 2008, conveying ARC' s approval and requesting return to ARC of grant payments for unsubstantiated project costs;
4. Letter from Bernie Bogle, ConnectKentucky, to Charles Howard, dated June 2, 2008, returning $25,909 to ARC (copy of check also attached); and
5. Letter from Matt Sawyers, Kentucky Alternate, to Thomas Hunter, dated March 25, 2008, reporting successful implementation of Grantee's program in all Appalachian Kentucky counties.

Both audit reports for these projects found that, while the projects had been successfully carried out and met all grant objectives, Grantee's accounting methodology was insufficient to support full grant expenditures solely in the grant service area. The reports recommended an approach to the allowance of grant costs based on a state-wide county average and the disallowance of all personnel costs to the ARC grants as not supportably incurred solely in the original grant service area.

Although Grantee has maintained that all grant expenditures were incurred in the approved project area, Grantee has conceded the accuracy of the audit finding that its record-keeping does not support a county-by-county attribution of costs. During discussions with ARC staff to resolve the outstanding audit issues, Grantee renewed a request it had previously made to expand the project service area to include all 51 counties in Appalachian Kentucky. Grantee also acceded to the audit findings relating to the disallowance of personnel costs but asked, in connection with its request to expand the project, for the allowance of costs associated with the work of two individuals whose activities were almost exclusively in the Appalachian portion of Kentucky.

Staff considered Grantee's request for an expanded project scope in the light of several factors:

1. Grantee has provided a creditable explanation of why it approached grant accounting as it did: originally expecting to receive ARC assistance for all of Appalachian Kentucky, it constructed its accounting system to assure that all ARC dollars were spent in the ARC Region, but did not break out expenditures by county within the Region. This explanation is borne out by Grantee's original grant application and has no appearance of bad faith.

2. Grantee's original request to expand the project had been made in a timely fashion well within the grant period of performance and was not formally rejected by ARC for program or policy reasons. Soon after ARC approval, Grantee's project attracted additional state grant support and rapidly expanded beyond the original service area. In addition, after the occurrence of start-up costs and with the experience gained from work in the initial counties, the project proceeded more rapidly than anticipated and the costs of the project on a per county basis was greatly reduced. In light of this, Grantee believed it could provide services under the ARC grant to other ARC counties and formally requested action to expand the project scope on August 26, 2006. Grantee's request involved no additional grant funds and appeared to be intended to reduce its matching burden for the grant. Largely because of the difficulty Grantee would experience producing per county budgets to support the expansion and its belief that a formal expansion of the scope was unnecessary, it did not pursue the request and no formal action was taken on it by ARC at that time.

3. The State of Kentucky concurred with Grantee's request, noting the solid benefits accruing from Grantee's program not just in the original service area but throughout Appalachian Kentucky. In addition, Grantee has been cooperative in dealing with staff to resolve the issues raised by the audit reports and provided a substantial amount of additional material relevant to its accounting methodology as requested by ARC.

Accordingly, staff recommended approval of Grantee's request and the Federal Co-Chair agreed on April 23, 2008. The expanded project applied the Kentucky multi-county match rate of 80/20 to both projects and accepted as eligible the personnel costs proposed by Grantee prorated at 42.5%, which is the proportion of ARC counties to all Kentucky counties.

By applying the results of the audit findings, the approval of Grantee's request for an expanded project scope, and the limited allowance of personnel costs, we have accepted final costs for the two Kentucky Broadband projects of $1,054,091. Because $1,080,000 had been disbursed previously for these projects, Grantee was requested to return $25,909 in unsubstantiated personnel costs to ARC. Grantee returned the funds to ARC on June 2, 2008. ARC believes this resolution of the matter to be reasonable in light of both the audit findings and the success of the project in meeting the needs of all Appalachian Kentucky.

TBM

CONNECTKENTUCKY

April 10, 2008

Mr. Harry Roesch
ARC Project Coordinator
Appalachian Regional Commission
1666 Connecticut Avenue, NW
Suite 700
Washington, DC 20009-1068

Dear Mr. Roesch,

Thank you for your consideration of our renewed request to expand the scope of our Appalachian Regional Commission grants KY-14974 and KY-15056-05 from 6 and 15 counties, respectively, to include all 51 ARC counties. All of Appalachian Kentucky has gained and continues to benefit from the ARC's seed investment in our projects. This scope expansion will correct an important administrative oversight that presently hinders our ability to fully and properly report on our grant's successful, sustainable, and long-term impact. We appreciate your consideration of this important request.

In addition, ConnectKentucky sincerely appreciates the time and thoughtful review the Commission has given to the *Prescription for Innovation's* grant audit findings and all of our subsequent informational supplements. From the beginning, we have endeavored to make the most judicious and effective use of the Commission's investment in our projects. Yet, despite our best efforts, our administrative process for cost allocations in the early days of these grants were not perfectly aligned with the ARC's expectations. While this accounting technicality has presented challenges to closing out the grant, please know that we never intended to cause any issues for the ARC and feel confident that we delivered a strong value for the entire Kentucky ARC region by leveraging substantial matching contributions from other non-federal funding sources.

As a means of bringing this matter to a fair, equitable and expeditious resolution, ConnectKentucky agrees with the ARC's suggested method of cost allocation. We have applied the actual grant numbers to ARC's proposed allocation method and have arrived at the calculations outlined below.

The total statewide project costs for the *Prescription for Innovation* was $5,112,393. The total number of Kentucky ARC counties (51) divided by the total number of Kentucky counties (120), equals 42.5% of Kentucky counties being contained within the ARC region. By applying this percentage to the total grant cost, $2,172,767 of the statewide total cost should be attributed to the ARC region. In order to meet the ARC grant requirements, a match of 20% or in this case, $434,553 is needed. This amount should be subtracted from the total ARC region cost leaving $1,738,214 remaining of the total ARC region project costs that were eligible to be funded by the Commission.

However, contained in this total ARC project cost are personnel salary and fringe benefits. Since many of our staff worked in both ARC and non-ARC counties, tracking their time at the individual county level was simply impossible. Yet, this presented a significant issue in the grant audit. As a compromise allocation method, ARC proposed and ConnectKentucky accepts a total disallowance of personnel salary and fringe costs. This line item amount represented approximately 47% of the total project costs reported on these grants for a total of $816,960 ($1,738,214 x 47%) that was included in the total eligible ARC project costs. The non-salary amount of the eligible ARC fundable project costs remaining after subtracting the personnel salary and fringe was $921,254. The ARC approved and funded a total of $1,080,000 which is $158,746 in excess of the $921,254 agreed upon as eligible ARC costs.

ConnectKentucky would propose mitigating this excess by allowing the inclusion of a portion of personnel costs for two staff members as eligible ARC grant costs. These two staff members worked in the field and had virtually all of their time spent in the ARC region: Ernie Woods (90% in ARC region) and Eric Mills (100% in ARC region). We propose including these personnel costs at the statewide county proportion of 42.5%. Ernie was a full-time employee while Eric worked as a consultant. Ernie's total salary and fringe for the grant period was $200,108 while Eric's consultant fees for the period were $112,450. By applying the statewide county percentage of 42.5% to Ernie and Eric's combined personnel cost of $312,558, the total proposed cost to be added back in as an eligible ARC cost for personnel would be $132,837. While 42.5% of their time is far less than the actual percentage of time each of these staff members spent working in the ARC region, ConnectKentucky believes allowing this percentage to be a very cautious and reasonable compromise for our inability to track actual staff time at the county level.

Therefore, by applying this proposed ARC eligible personnel cost of $132,827 back into the total grant cost, the remaining excess previously paid to ConnectKentucky by ARC is $25,909. If the Commission accepts this allocation proposal to fully and finally resolve this matter, ConnectKentucky will promptly refund this amount, $25,909, directly to the Commission. However, ConnectKentucky would respectfully request that all audit findings, related correspondence incident thereto, as well as all of the details of the ultimate resolution of those findings for Appalachian Regional Commission grants KY-14974 and KY-15056-05 be sealed and remain strictly and completely confidential.

Detailed below are the calculations that were presented in a narrative form above. These calculations were undertaken by the ARC to provide an equitable resolution of the audit findings. This exhibit depicts our understanding of the solution based upon our prior conversations.

Total Prescription for Innovation (Rx) Project Costs	$ 5,112,393
51 ARC Counties/120 Total Kentucky Counties	42.5%
Total ARC Prescription for Innovation Project Costs	**$ 2,172,767**

	Total	20% Match	80% ARC
Total ARC Rx Project Costs	$ 2,172,767	$ 434,553	$ 1,738,214
Less Total Salary of 47% per Grant Budgets	(1,021,200)	(204,240)	(816,960)
ARC Rx Project Costs - Non-Salary Items	**$ 1,151,567**	**$ 230,313**	**$ 921,254**

ARC Funding Received	$ 1,080,000
Less 80% ARC Rx Project Costs - Non Salary Items	921,254
	158,746
Less Salary Amount (see below for detail)	132,837
Refund to ARC	**$ 25,909**

Salary Detail

Ernie Woods - Salary (90% ARC region)	$ 200,108
Eric Mills - Consutlant (100% ARC Region)	112,450
	312,558
51 ARC Counties/120 Total Kentucky Counties	42.5%
Allowable Salary Amount	**$ 132,837**

We established our accounting methodologies on assumptions from our organization's prior successful grant history with ARC. Due to these projects tremendous early successes and the Commonwealth's desire to rapidly expand them statewide, our initial assumptions proved incorrect. However, the accounting methodologies used ensured that all of the ARC money was spent in ARC counties of Kentucky. We attempted to address the technical issues of the grant by expanding the scope but it was impractical at the time given the decreasing county project costs as a result of our efficiencies gained through the two grants. Certainly we were acting in good faith to interpret and execute the grant in a responsible fashion and to the benefit of the people of Appalachia; it was never our intent to violate ARC policy in any manner. In fact, because of our goal driven focus, our projects provided a benefit and value far beyond the grant that extended to the entire ARC region.

The results of ConnectKentucky's broadband deployment initiative are astounding and would not have been possible without the funding of received from the Appalachian Regional Commission:

- Broadband availability has grown from approximately 60 percent of households to 95 percent - representing more than 558,000 previously unserved households and more than 1.4 million residents that can now access broadband.

- Home broadband use has grown by 100 percent in the last three years. While home Internet use in Kentucky between 2000 and 2005 slowly ticked up one percentage point per year, the growth over the last two years has nearly quadrupled that rate. Kentucky Internet use now exceeds the national average after years of rankings at the bottom. Meanwhile, computer ownership in Kentucky has risen by over 24 percent in the last three years. The U.S. growth rate in computer use over the same period was approximately 4 percent.

- eCommunity Leadership Teams in each of Kentucky's 120 counties have established a technology growth plan to drive adoption across nine community sectors – government, business and industry, education (K-12 and higher education), healthcare, tourism, libraries, agriculture and community-based organizations.

- 100 percent of Kentucky counties now operate a meaningful web presence for e-government and online citizen services. Two years ago, only one-third of Kentucky counties had a website, and many of these were not functional or had lain dormant for years. ConnectKentucky has established a simple and centralized process for local governments to create a content-rich website at little to no cost for local communities. Through the eCommunity Leadership Teams, ConnectKentucky is working to ensure that every Kentucky county has a meaningful online presence, fully equipped with solutions for more effective and efficient citizen services through e-government, virtual education and online healthcare.

- More than 18,400 technology jobs have been created in Kentucky in the last two years, many in rural areas. In the information technology sector alone, Kentucky's job growth has been 31 times the national growth rate.

- More than $743 million in private capital has been invested in telecommunications infrastructure over the past three years in Kentucky.

The pace of Kentucky's technology expansion is unprecedented. Kentucky is recognized as a national leader in technology acceleration with ConnectKentucky repeatedly acknowledged as the national model for states. We have been recognized as a national leader by:

- Communications Workers of America
- Congressional Research Service
- Federal Communications Commission
- U.S. Government Accountability Office of Congress
- National Governor's Association
- Southern Growth Policies Board
- USDA Rural Utilities Service
- US Economic Development Administration
- White House Office of Technology
- Intel, Apple, Microsoft, Verizon, AT&T (among other private sector companies)
- Numerous states across the nation
- The Information Technology & Innovation Foundation
- The Alliance for Public Technology

As a result of the success of the *Prescription for Innovation*, which would not have been possible without ARC support, ConnectKentucky has become a model for the country, as other states have looked to the Commonwealth for the solutions to their broadband deployment dilemmas. As a response to their inquiries, a parent organization, Connected Nation was formed. Through this entity, other states are replicating ConnectKentucky's model, including the states of Tennessee and Ohio. We expect this list will grow as more and more states realize the importance of having a vast broadband infrastructure to the future of their economies. Moreover, Congress has routinely referenced ConnectKentucky as a model program for creating a national broadband strategy. Various pieces of federal legislation (S. 1190/H.R. 3627, S.1492, H.R.3919) in the current Congress have been modeled on the work of ConnectKentucky and the current version of the farm bill includes the Connect the Nation Act which would effectively extend the ConnectKentucky model to every state in the nation. ARC had the vision four or more years ago to invest in our broadband deployment project and your investment has certainly yielded great dividends.

Not only has ConnectKentucky garnered national attention, we have also received international recognition. In March, as part of the U.S. delegation to APEC, Connected Nation joined with delegates from 21 international economies in Tokyo to provide expert testimony in the seminar "Using ICT for Rural Community Capacity Building," part of the 37th meeting of the APEC Telecommunications and Information Working Group. As a delegate, I was honored to present the experiences of Connected Nation in promoting Information and Communication Technology (ICT) tools and applications to expand broadband adoption and capacity building in rural communities. In addition, we have hosted international delegations from Sweden, Japan, India, New Zealand, China and South Africa regarding ConnectKentucky's initiative to expand broadband.

Through ConnectKentucky's longstanding relationship with the Commission, we have grown a great deal of respect and admiration for the strong sense of purpose, care and efficiency by which grant resources are administered. I certainly appreciate all of the support that the ARC has provided ConnectKentucky as well as the thoughtful review and attentiveness to our responses as we have worked through these audit concerns together. We look forward to hearing back from you as to how we can finally conclude this issue.

Kindest Regards,

Brian R. Mefford
President & CEO

APPALACHIAN REGIONAL COMMISSION
A Proud Past, A New Vision

Office of the Executive Director

To: Anne B. Pope, Federal Co-Chair ABP

Date: April 23, 2008

Subject: Change of Scope for Kentucky Broadband Projects (KY-14974 & 15056)

Grantee: Center for Information Technology Enterprises, Inc. (CITI)/ ConnectKentucky

The purpose of this memorandum is to recommend approval of Grantee's request to expand the scope of the above referenced projects to provide grant supported services beyond the originally approved twenty-one county service area to all fifty-one counties in Appalachian Kentucky. The State of Kentucky concurs with Grantee's request.

In 2004 and 2005, ARC approved two grants to ConnectKentucky to undertake and develop a successful method of assessment of broadband needs and deployment of technology to assist communities to achieve broadband connectivity as soon as possible. Under the projects, Grantee undertook broadband strategic planning and demand aggregation programs and GIS mapping of telecommunications services available in the counties served by the projects. (Ky-14974 was in the amount of $180,000 for 6 counties and KY-15056 was for $900,000 for 15 additional counties.)

The first ARC grant was designed as a demonstration project for what was intended to be a state-wide effort to provide similar services in every Kentucky county. Soon after the ARC project was initiated, Grantee's project attracted additional state grant support and rapidly expanded beyond the original service area. In addition, after the occurrence of start-up costs and with the experience gained from work in the initial counties, the project proceeded more rapidly than anticipated and the costs of the project on a per county basis was greatly reduced.

In light of this, Grantee believed it could provide services under the ARC grant to other ARC counties and formally requested action to expand the project scope by means of a letter dated August 26, 2006, well within the grant period of performance. Grantee's request to expand the project scope involved no additional grant funds and appears to be intended to reduce its matching burden for the grant. Largely because of the difficulty Grantee would experience producing per county budgets to support the expansion and its belief that a formal expansion of the scope was unnecessary, it did not pursue the request and no formal action was taken on it by the Commission at that time. The grants were later closed out with full payment of grant funds on the basis of work performed solely in the twenty-one county service area.

1666 CONNECTICUT AVENUE, NW WASHINGTON, DC 20235 (202) 884-7700 FAX (202) 884-7691

A subsequent audit by ARC's Inspector General's office determined that, while the projects had been successfully carried out and met all grant objectives, Grantee's accounting methodology was insufficient to support full grant expenditures solely in the grant service area. The Inspector General's audit recommended an approach to the allowance of grant costs based on a state-wide county average and the disallowance of all personnel costs to the ARC grants as not supportably incurred solely in the twenty-one county service area.

While Grantee has maintained that all grant expenditures were incurred in the approved project area (largely citing in this connection the additional start-up costs associated with the ARC counties as demonstrations for what became a state-wide effort), it has conceded that its record-keeping does not support a county-by-county attribution of costs. Grantee has provided a creditable explanation of why it approached grant accounting as it did: originally expecting to receive ARC assistance for all of Appalachian Kentucky, it constructed its accounting system to assure that all ARC dollars were spent in the ARC Region, but did not break out expenditures by county within the Region. This explanation is borne out by Grantee's original grant application in the files at ARC and has no appearance of bad faith.

Grantee has been cooperative during the audit process and provided a substantial amount of additional material relevant to its accounting methodology as requested by ARC. In an effort to resolve the outstanding issues, Grantee has now renewed its request to expand the project area to include all of Appalachian Kentucky. Under this approach, Grantee would agree with the Inspector General's recommendations regarding payment of grant costs on a state-wide county average basis, but requests that the average be applied across all Appalachian counties at the 80/20 match rate applicable to a multi-county project in Kentucky. Grantee would also accede to the Inspector General's recommendations regarding personnel costs, asking only for an allowance for a portion of the costs of two staff members whose activities during the grant period were almost exclusively within the ARC Region. Under the proposed resolution, Grantee would return $25,909 in unsubstantiated personnel costs to ARC.

Staff has reviewed Grantee's request and believes it to be reasonable in light of both the audit findings and the success of the project in meeting the needs of not only the original service area but all Appalachian Kentucky. The State of Kentucky has sent a strong letter testifying to the benefits that Grantee's program brought to all its Appalachian counties.

RECOMMENDED:

Thomas M. Hunter

THOMAS M. HUNTER
Executive Director

APPALACHIAN REGIONAL COMMISSION

A Proud Past, A New Vision

May 23, 2008

Brian R. Mefford, President & CEO
ConnectKentucky
P.O. Box 3448
Bowling Green, KY 42102

Change of Scope for Kentucky Broadband Projects
KY-14974 & KY-15056

Dear Mr. Mefford:

I am responding to your letter of April 10, 2008 to Mr. Harry Roesch, ARC Project Coordinator, in which you requested ARC approval to expand the scope of the above referenced projects to provide grant supported services beyond the originally approved twenty-one county service area to all fifty-one counties in Appalachian Kentucky. The State of Kentucky has separately concurred with your request. This letter conveys ARC's approval of your request to expand the project scope and otherwise indicates our agreement to elements of your proposal to resolve isssues raised in audits of these grants by the ARC Inspector General.

In 2004 and 2005, ARC approved two grants to ConnectKentucky to develop and implement a method of assessment of broadband needs and deployment of technology to assist communities to achieve broadband connectivity as soon as possible. Under the projects, ConnectKentucky undertook broadband strategic planning and demand aggregation programs and GIS mapping of telecommunications services available in the counties served by the projects. (Ky-14974 was in the amount of $180,000 for 6 counties and KY-15056 was for $900,000 for 15 additional counties.)

The first ARC grant was designed as a demonstration project for what was intended to be a state-wide effort to provide similar services in every Kentucky county. Soon after the ARC project was initiated, ConnectKentucky's project attracted additional state grant support and rapidly expanded beyond the original service area. In addition, after the occurrence of start-up costs and with the experience gained from work in the initial counties, the project proceeded more rapidly than anticipated and the costs of the project on a per county basis was greatly reduced.

In light of this, ConnectKentucky believed it could provide services under the ARC grant to other ARC counties and formally requested action to expand the project scope by means of a letter dated August 26, 2006, well within the grant period of performance. ConnectKentucky's request

to expand the project scope involved no additional grant funds and appeared to be intended to reduce its matching burden for the grant. Largely because of the difficulty ConnectKentucky would experience producing per county budgets to support the expansion and its belief that a formal expansion of the scope was unnecessary, it did not pursue the request and no formal action was taken on it by the Commission at that time. The grants were later closed out with full payment of grant funds on the basis of work performed solely in the twenty-one county service area.

A subsequent audit by ARC's Inspector General's office determined that, while the projects had been successfully carried out and met all grant objectives, ConnectKentucky's accounting methodology was insufficient to support full grant expenditures solely in the grant service area. The Inspector General's audit recommended an approach to the allowance of grant costs based on a state-wide county average and the disallowance of all personnel and benefits costs to the ARC grants as not supportably incurred solely in the twenty-one county service area.

While ConnectKentucky has maintained that all grant expenditures were incurred in the approved project area (largely citing in this connection the additional start-up costs associated with the ARC counties as demonstrations for what became a state-wide effort), it has conceded that its record-keeping does not support a county-by-county attribution of costs. ConnectKentucky has provided a creditable explanation of why it approached grant accounting as it did: originally expecting to receive ARC assistance for all of Appalachian Kentucky, it constructed its accounting system to assure that all ARC dollars were spent in the ARC Region, but did not break out expenditures by county within the Region. This explanation is borne out by ConnectKentucky's original grant application in the files at ARC and has no appearance of bad faith.

ConnectKentucky has been cooperative during the audit process and provided a substantial amount of additional material relevant to its accounting methodology as requested by ARC. In an effort to resolve the outstanding issues, your recent letter renewed ConnectKentucky's earlier request to expand the project area to include all of Appalachian Kentucky. You have indicated that ConnectKentucky would also agree with the Inspector General's recommendations regarding payment of grant costs on a state-wide county average basis, but have requested that the average be applied across all Appalachian counties at the 80/20 match rate applicable to a multi-county project in Kentucky. You have also indicated that ConnectKentucky would accede to the Inspector General's recommendations regarding personnel and benefits costs, asking only for an allowance for a portion of the costs of two staff members whose activities during the grant period were almost exclusively within the ARC Region. Under the proposed resolution, ConnectKentucky would return $25,909 in unsubstantiated personnel and benefits costs to ARC.

ARC has reviewed your request and determined it to be reasonable in light of both the audit findings and the success of the project in meeting the needs of not only the original service area but all Appalachian Kentucky. The State of Kentucky has sent a strong letter testifying to the benefits that Grantee's program brought to all its Appalachian counties. Accordingly, ARC has approved your request to expand the project service area and agrees to the other elements of your proposal outlined in the preceding paragraph. ConnectKentucky's return of $25,909 to ARC would finally resolve all issues raised in the Inspector General's audits of these grants.

Please let me know if you have any questions regarding this matter. I can be reached at 202-884-7789. Thank you.

Sincerely,

Charles Howard
General Counsel

CONNECTKENTUCKY.

June 2, 2008

Mr. Charles Howard
General Council
Appalachian Regional Commission
1666 Connecticut Avenue, NW
Suite 700
Washington, DC 20009-1068

Dear Mr. Howard:

Pursuant to your correspondence to Mr. Brian Mefford dated May 23, 2008, please find enclosed a check for $25,909 to fully and finally resolve and conclude the audit of ARC grants number KY-14974 and KY-15056.

Thank you for your assistance in this matter.

Sincerely,

Bernie Bogle, CPA
VP, Finance

cc: Mr. Harry Roesch
Mr. Brian R. Mefford

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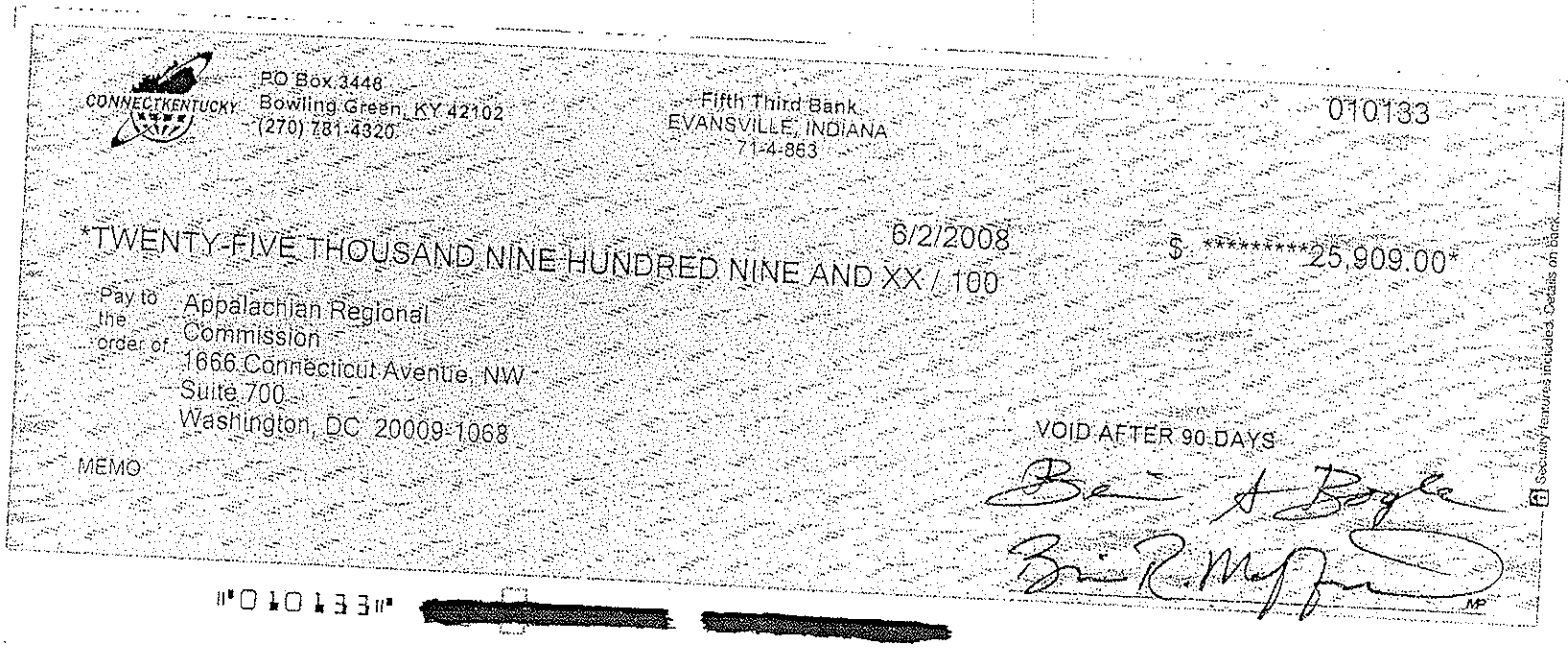
DKJ



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Bowling Green, KY 42102
(270) 781-4320

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Date	Invoice Number	Comment	Amount	Discount Amount	Net Amount
5/23/2008	052308		25,909.00	0.00	25,909.00

Check: 010133	6/2/2008	0010073	Appalachian Regional	Check Total:	25,909.00

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March 25, 2008

Mr. Thomas M. Hunter, Executive Director
Appalachian Regional Commission
1666 Connecticut Avenue, NW
Washington, D. C. 20009-1068

RE: KY- 14974 – Appalachian Regional Broadband Demonstration Project
KY- 15056 – KY Broadband Prescription for Innovation Initiative

Dear Mr. Hunter:

As you know, I was recently appointed as Governor Beshear's Alternate to the Appalachian Regional Commission (ARC) for the Commonwealth of Kentucky. I have been briefed about the audit findings situation relative to the above noted projects that have had grants awarded to the Center for Information Technology Enterprises, Inc. (CITE) or ConnectKentucky. After careful consideration of the documented accomplishments of these projects, I want to offer an assessment of the outcomes that are clearly evident and their impact on Kentucky's Appalachian Region.

The initial project was a demonstration project conducted in six Appalachian counties beginning in September 2004 to undertake and develop a successful method of assessment of broadband needs and deployment of technology to assist communities with the ability to achieve broadband connectivity as soon as possible. The second project launched a plan by CITE in June 2005 to extend this program into fifteen additional counties to undertake broadband strategic planning/demand aggregation program and GIS mapping of all telecommunications services.

Outcomes of these projects include assessment of telecommunications infrastructure that has been GIS mapped, the successful mobilization of local leadership teams in each Appalachian county and provision of community-specific planning programs with implementation phases. In addition, due to the ability of CITE to obtain financial resources from other federal, state and private entities, this program has been successfully extended to all fifty-one of our Appalachian counties to date, as well as to the balance of the state.

The statewide broadband initiative began with the demonstration project conducted in six Appalachian counties and has been recognized as a model program throughout the Commonwealth and has even been referenced in Congressional bills and hearings relative to broadband deployment issues within the past year. I understand that other Appalachian states are working with ConnectKentucky to begin similar programs within their communities.

Positive and productive outcomes documented across our Appalachian Region lead me to conclude that the ARC grants recommended by Kentucky and approved by the Commission have been a solid investment providing our communities with the necessary tools to participate and compete in a global economy and to achieve vital economic progress in the future. I realize that the project audit revealed some accounting procedural irregularities, but review of the extensive project reports filed with both our office and ARC indicate that the ARC grant funds have not only accomplished intended goals but have allowed benefit to extend to all of our Appalachian Kentucky counties.

Let me commend the generous support that you and your staff have offered to us in Kentucky and to ConnectKentucky in the administration of these projects and the ultimate realization of profound benefit to our Appalachian communities.

Sincerely,

Matt Sawyers
Chief of Staff