
Controls Over Excessive Cash Drawdowns By Grantees

FINAL AUDIT REPORT



ED-OIG/A19F0025
December 2006

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U.S Department of Education
Office of Inspector General
Washington, DC

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UNITED STATES DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL

OPERATIONS INTERNAL AUDIT TEAM

December 18, 2006

Memorandum

TO: Lawrence Warder
Chief Financial Officer
Office of the Chief Financial Officer

FROM: Helen Lew /s/
Assistant Inspector General for Audit
Office of Inspector General

SUBJECT: Final Audit Report
Controls Over Excessive Cash Drawdowns by Grantees
Control Number ED-OIG/A19F0025

Attached is the subject final audit report that covers the results of our review of excessive cash drawdowns by grantees during Fiscal Year (FY) 2005. An electronic copy has been provided to your Audit Liaison Officer. We received your comments concurring with three of the four findings and associated recommendations in our draft report.

Corrective actions proposed (resolution phase) and implemented (closure phase) by your office(s) will be monitored and tracked through the Department's Audit Accountability and Resolution Tracking System (AARTS). ED policy requires that you develop a final corrective action plan (CAP) for our review in the automated system within 30 days of the issuance of this report. The CAP should set forth the specific action items, and targeted completion dates, necessary to implement final corrective actions on the findings and recommendations contained in this final audit report.

In accordance with the Inspector General Act of 1978, as amended, the Office of Inspector General is required to report to Congress twice a year on the audits that remain unresolved after six months from the date of issuance.

In accordance with the Freedom of Information Act (5 U.S.C. §552), reports issued by the Office of Inspector General are available to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act.

We appreciate the cooperation given us during this review. If you have any questions, please call Michele Weaver-Dugan at (202) 245-6941.

Enclosure

cc: Blanca Rodriguez, Director, Grants Policy Oversight Staff (GPOS), Office of the Chief
Financial Officer (OCFO)
Constance Davis, Director, Financial Systems Operations (FSO), OCFO
Charlesetta Griffin, Audit Liaison, GPOS
Greg Robison, Audit Liaison, FSO

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EXECUTIVE SUMMARY

The objective of our audit was to determine whether the Department's controls identify and prevent excessive cash drawdowns by grantees. As a corrective action to a prior Office of Inspector General (OIG) audit,¹ the Department developed a report to monitor potentially excessive drawdowns by discretionary grantees. The Excessive Drawdown Report identifies those discretionary grantees that may have exceeded drawdown thresholds by drawing funds in excess of a grant's immediate cash needs. It represents the Department's primary internal control in this area. The Grants Policy and Oversight Staff (GPOS) is responsible for generating the report on a monthly basis from the Grants Administrative Payment System (GAPS) and distributing the information to applicable Principal Offices (POs). PO staff are responsible for researching each grant on the report and providing a response to GPOS on the results.

Overall, we found the Department's controls did not effectively identify or prevent excessive cash drawdowns. Our audit revealed that the Excessive Drawdown Reports did not identify 1,379 unique grants that met the excessive drawdown threshold criteria during FY 2005. The net² drawdown activity for these grants totaled \$212 million. We also found that the reports included some grants that did not meet the criteria. In addition, we found GPOS did not always fulfill its responsibility to ensure program offices monitored excessive drawdowns. As a result, the Department is not monitoring all grants for excessive drawdowns, and cannot ensure its grantees are compliant with fiscal requirements.

We also found improvements were needed in the use of payment flags to prevent inappropriate drawdowns. Finally, we found that tools such as the Excessive Drawdown Reports had not been developed and implemented for formula grants.

To correct these weaknesses, we recommend that the Department:

- Correct the deficiencies noted in the query used to generate the Excessive Drawdown Report, automate the process for generating the report, and provide additional fields to allow GPOS staff to enter resolution status provided by the POs.
- Ensure GPOS staff follow up with PO staff on grants to which they do not respond and periodically report to senior management on PO responses.
- Develop and implement a method to communicate payment flag information to all program offices responsible for monitoring additional grants awarded to the same recipient and require PO staff to evaluate information received on payment flags for other awards to grantees to which they have also made or are making awards.
- Resolve issues noted in the payment flag reporting functionality with GAPS.
- Ensure appropriate GAPS reports are developed and implemented to permit effective monitoring of formula grant programs and processes.

¹ ED-OIG/A03-80010, *Audit of Drawdown Controls in Grant Administration and Payment System*, issued September 13, 2000.

² Drawdowns less any returns of funds.

The Department concurred with three of the four findings and associated recommendations. The Department did not agree with Finding 4, stating that the Chief Financial Officer does not have the authority to oversee formula grants, including developing policy for their administration. However, OIG believes the development and implementation of the Excessive Drawdown Report, or similar reports, for formula grants would serve as a tool to assist the PO staff in monitoring grantees' fiscal activities to ensure they comply with statutory and regulatory requirements. A task of the Deputy Secretary's Grants Improvement Project, headed by OCFO, is to develop a Handbook for Formula Grants, which would include policies and procedures related to the fiscal management of formula grants. As such, we added to the recommendation that the Chief Financial Officer work in conjunction with the Deputy Secretary's Grants Improvement Project. The full text of the Department's response is provided as an enclosure to this report.

BACKGROUND

Office of Management and Budget (OMB) Circular A-123, dated June 21, 1995,³ entitled *Management Accountability and Control*, provides guidance on improving the accountability and effectiveness of Federal programs and operations by establishing, assessing, correcting, and reporting on management controls. The Circular states, “Management controls must provide reasonable assurance that assets are safeguarded against waste, loss, unauthorized use, and misappropriation.” These controls are defined as “. . . the organization, policies, and procedures used by agencies to reasonably ensure that (i) programs achieve their intended results . . . (iii) programs and resources are protected from waste, fraud, and mismanagement . . .”

The Department of Education’s (Department) *Handbook for the Discretionary Grant Process* (Handbook) states, “Monitoring is an integral part of grant administration and oversight after a grant has been awarded.” The Handbook further states,

Well-designed monitoring must also address [Department of Education’s] ED’s fiduciary responsibility to ensure grantees’ compliance with legal and fiscal requirements and to protect against fraud, waste and abuse.

The Department’s Grants Policy and Oversight Staff (GPOS), within the Office of the Chief Financial Officer (OCFO), is responsible for policy development, oversight, research and analysis, and improvement of the Department’s discretionary grants process. According to the Handbook, GPOS works collaboratively with other Department offices to achieve effective monitoring of grant programs and to ensure that monitoring activities and processes are conducted with consistency and are compliant with Department regulations and policies. GPOS supports the Department’s Principal Offices (POs) that administer the discretionary grant programs.

The Handbook directs the Department’s program staff to pay particular attention to grantees’ fiscal activities as part of the monitoring process by using the Grants Administration and Payment System (GAPS) as the primary tool. GAPS provides payment and expenditure reporting to users. One of the available reports is the Excessive Drawdown Report, which assists program offices in identifying those discretionary grantees that may have violated cash management policies and regulations by drawing funds in excess of a grant’s immediate cash needs. GPOS generates Excessive Drawdown Reports on a monthly basis and distributes the information to various POs. PO staff are responsible for researching each grant on the report to determine whether excessive drawdowns have been made, to assist the grantee in resolving any problems with excess cash balances, and to report back to GPOS on the results.

³ OMB Circular A-123 was revised December 21, 2004, effective for Fiscal Year (FY) 2006 and beyond. The circular quoted above was in effect during our audit period, FY 2005. Similar language also appears in the revised circular.

AUDIT RESULTS

We found the Department's controls did not identify and prevent excessive cash drawdowns by grantees during FY 2005. Our audit disclosed that (1) Excessive Drawdown Reports did not effectively identify all potentially excessive drawdowns, (2) GPOS did not ensure program offices monitored excessive drawdowns, (3) improvements were needed in use of payment flags to prevent inappropriate drawdowns, and (4) formula grants were not monitored through the Excessive Drawdown Reports. As a result, grantees may be drawing down funds in excess of their immediate cash needs for each grant and using the funds for inappropriate purposes.

In its comments to the draft report, OCFO concurred with three of the four findings and associated recommendations. OCFO did not concur with Finding 4 and its recommendation. The comments are summarized at the end of each finding. The full text of OCFO's comments on the draft report is included as an attachment to the report.

FINDING NO. 1 – Excessive Drawdown Reports Did Not Effectively Identify All Potentially Excessive Cash Drawdowns

The Excessive Drawdown Report was developed to monitor drawdowns by discretionary grantees and identify potential excessive drawdown conditions. This report identifies grantees that have drawn funds in excess of three specific thresholds during the budget period in place when the report is generated. The report represents the Department's primary internal control in this area. We found, however, that the Excessive Drawdown Report did not identify all grants with potential excessive drawdown conditions and included grants that were no longer active. Evaluation of GAPS transactional data identified 1,379 unique grants that met the excessive drawdown threshold criteria, but the grants did not appear on one or more Excessive Drawdown Reports during FY 2005. These grants represented net drawdown activity totaling \$212 million during the year, as follows:

- 867 grants with FY 2005 funding or an active budget period during FY 2005 that met excess drawdown thresholds were not included in any of the Excessive Drawdown Reports generated by GPOS. These grants included an estimated \$154.4 million in net drawdowns during FY 2005.
- 512 grants with potential excessive drawdowns were not included in one or more monthly GPOS reports, but were included in later months during FY 2005. These grants represented an estimated \$57.6 million in net drawdowns during FY 2005.

We also determined that 166 grants listed on the Excessive Drawdown Reports generated during FY 2005 had budget periods that ended prior to FY 2005, did not have any fiscal activity during FY 2005, and did not represent potentially excessive drawdowns.

Grant Policy Bulletin #27: Monitoring Discretionary Grants for Excessive Drawdowns (Bulletin), dated May 24, 2001,⁴ states,

The GAPS [Excessive] Drawdown Report (report) has been developed to assist program offices in identifying those grantees that might have violated cash management policies and regulations by drawing down funds in excess of a grant's immediate cash needs.

The report indicates those grants that have drawn an unusually large proportion of grant funds in any of the first three quarters of the grant's current budget period. A grant will appear on the report if the following drawdown thresholds are exceeded:

- As of the end of the first quarter of the grant's current budget period, **more than 50%** of the funds obligated for that budget period have been drawn.
- As of the end of the second quarter of the grant's current budget period, **more than 80%** of the funds obligated for that budget period have been drawn.
- As of the end of the third quarter of the grant's current budget period, **100%** of the funds obligated for that budget period have been drawn.

The existing process for generating the Excessive Drawdown Reports is cumbersome and time consuming. There is also a great deal of manual manipulation involved in formatting the reports to be sent to the POs and in reviewing PO responses. In order to run the reports, GAPS only allows users to input one PO and one FY at a time, resulting in GPOS staff having to run the reports multiple times, and combine multiple grant year reports to provide a complete report to each PO. Since the report includes all previously identified grants, and POs may have responded to these potential excessive drawdowns, GPOS manually compares prior reports and responses from the POs each month and manually deletes previously reported drawdowns that had been resolved. GAPS does not include a feature to allow GPOS staff to run the report for all POs and all active grants, or to indicate whether a potentially excessive drawdown has been resolved so that the grant does not appear again on the report until the next threshold is reached.

We attempted to evaluate the programming source code used to generate the Excessive Drawdown Report. However, OCFO staff could not locate a copy of the source code for the program currently in use. OCFO did provide a copy of a program it stated was similar to that currently in use on the system and likely to be the starting point for enhancements and corrective measures to the existing program. Our evaluation of this program, detail transactional data extracted from GAPS, and Excessive Drawdown Reports that were generated by GPOS during the audit period noted the following deficiencies in the processing methodology used for selection of the grants:

⁴ The Bulletin was in effect during the scope of our review, but was rescinded with the update of the Handbook in February 2006. These requirements are also included in the updated Handbook, Section 5.3.8, subparagraph 6.

- Grants with potential excessive drawdowns were not included in the report until after the end of the quarter in which the condition occurred. In some cases, this resulted in a significant time lag from when the condition occurred to when it first appeared on an Excessive Drawdown Report. For example, if an excessive drawdown condition occurred during the first week of the quarter for a grant with a 12-month budget period, the grant would not be included on the report until after the end of the first quarter – three months later.
- Only the first grant budget period was used to calculate potentially excessive drawdowns. Active grants in later budget periods were not included on the reports, regardless of the drawdown status.
- Grants were included in the reports regardless of whether the grant period was active or whether funding activity occurred during the budget period. In many cases, these were older grants for which the budget period had ended prior to FY 2005, and there was no FY 2005 funding for the grant.
- At the start of a new year, grant records are “rolled over” in the GAPS software to facilitate continuation awards. Early “roll-over” of grants for continuation award purposes prevented grants from being properly evaluated for excess drawdown conditions. The roll-over process resulted in the status for a future budget period being reflected as the current budget period for the grant. In one example evaluated, this action occurred approximately six months before the actual start date of the new budget period. Once this action occurred, the actual “current” budget period would no longer be evaluated, and if an excess drawdown condition occurs, it would not be properly identified and included on the report.
- Similarly, early posting of future year authorizations were improperly included in the total obligations used to calculate the percentage of funds drawn down for the current period. As a result, the percentage of funds drawn down was understated and grants with drawdowns meeting the thresholds were not included on the report.
- We also noted minor differences of one day in the calculations for the current quarter and for the number of days in the current budget period. These calculations were used in determining the percentages of funds drawn. Deficiencies noted resulted in inaccurate calculation of the quarter end dates and in some cases may have impacted the grants included or excluded from the reports.

In addition, GPOS stated that it did not distribute the Excessive Drawdown Reports for the months of October and November 2004 and January 2005 because it was testing a new query for the report with the GAPS Report Team. GPOS stated a report was generated in January 2005, but it found that the January 2005 activity was the same as that in the December 2004 report that had previously been compiled. Therefore, GPOS distributed the December 2004 activity to POs in early February 2005. GPOS did not distribute reports in April 2005 due to workload issues in GPOS. GPOS also stated that in FY 2005, it only generated the reports for grants with award years from FY 2003 through FY 2005 since most grants were of three years’ or less duration. In

addition, grants awarded in FY 2005 were not usually included in the report requests until six months after the start of the FY.

To evaluate GPOS' statement that most grants were of three years' duration or less, we analyzed FY 2005 funding and found that of the 11,483 new and continuation awards, 2,668 unique grants (23 percent) were originally awarded prior to FY 2003, and therefore were not monitored for excessive drawdowns. These grants represented approximately \$969 million in FY 2005 funding.

As a result of the deficiencies noted in the Excessive Drawdown Report programming, and GPOS' process for generating the reports, the Department did not identify and monitor all grants with potentially excessive drawdown activity during FY 2005. Grantees may be making cash drawdowns in excess of immediate needs. The funds drawn down are at risk for inappropriate use without detection by the Department. Without identifying possible excessive drawdowns soon after they occur, the Department cannot ensure that grantees are financially compliant and that drawdowns are not made in excess of each grant's immediate cash needs. In addition, the inclusion of grants that did not have fiscal activity resulted in PO staff researching grants that did not represent potentially excessive drawdowns.

Recommendations

We recommend the Chief Financial Officer:

- 1.1 Take immediate action to correct the deficiencies noted in the query used to generate the Excessive Drawdown Report to ensure all potentially excessive drawdowns are identified for all active grants, and to ensure that grants that are no longer active are not included in the report.
- 1.2 Redesign the query used to generate the Excessive Drawdown Report in GAPS to allow GPOS staff to query for all active grants, regardless of award year, for all POs. Design this query to run automatically each month and be placed in a location for GPOS staff to access.
- 1.3 Design additional fields in GAPS to allow GPOS staff to enter resolution information for potentially excessive drawdowns so that, if resolved, the grants do not appear on future reports until the next threshold is reached.

OCFO Comments:

OCFO concurred with the finding and recommendations. OCFO stated it has corrected the six query deficiencies noted in the first recommendation to ensure the Excessive Drawdown Report identifies all potentially excessive drawdowns for all active grants, and that grants that are no longer active are not included. In addition, OCFO stated the remaining two recommendations require data base enhancements, which are included in the G5 Phase I implementation. In the interim, OCFO stated a temporary work process has been developed to provide the necessary information to the POs.

FINDING NO. 2 – GPOS Did Not Ensure Program Offices Monitored Excessive Drawdowns

GPOS did not always fulfill its responsibility to ensure program offices monitored excessive drawdowns. We found that GPOS did not always follow up with POs that did not respond to the reports referred for their research and resolution. We reviewed in detail the Excessive Drawdown Reports generated by GPOS during FY 2005 for two POs – the Office of Innovation and Improvement (OII) and the Office of Postsecondary Education (OPE). These two offices represented 425 of the total 495 potentially excessive drawdowns for the year (86 percent). These drawdowns were made by 263 unique grantees. We found the POs did not provide responses for 159 of the 425 excessive drawdowns (37 percent) they were responsible for researching and resolving. These drawdowns were made by 121 unique grantees. We sampled the responses these POs did provide for 69 potentially excessive drawdowns, and found that the POs did not have documentation to support 8 of the responses provided (12 percent). In two cases, the PO stated the grantee would return funds, but this did not occur.

The Bulletin states GPOS is “. . . responsible for providing overall department-wide oversight to ensure that program offices are monitoring for excessive drawdowns.” The Bulletin further states,

GPOS will run the report on a monthly basis and will contact the Points of Contact and program managers to ensure that problems with excess cash balances have been resolved and the proper documentation is maintained regarding the status of each grant on the report.

In its referral of potentially excessive drawdowns, GPOS establishes a two to three week deadline for the PO to respond, and requests the response include the following information:

1. Indicate how the drawdown is consistent with approved project activities and approved budget.
2. If Program Staff determine that an excessive drawdown has occurred, indicate the date the grantee was contacted and notified of Department policy.
3. Indicate the date the grantee resolved the cash management problem.
4. Indicate if funds were (1) returned to ED or (2) the grantee made an on-line adjustment.

When a PO does not respond to drawdowns listed on the monthly Excessive Drawdown Report, GPOS highlights these unresolved drawdowns in red text on subsequent exception reports until they are resolved. However, GPOS staff stated that, due to time constraints, they do not always follow up with the POs that do not respond.

By not ensuring that the POs review the information and provide timely responses, the Department is not monitoring all grants for excessive drawdowns, and cannot ensure its grantees are compliant with fiscal requirements and are not making drawdowns in excess of their immediate cash needs. PO staff may not take seriously their responsibilities to research and respond to grants listed on the Excessive Drawdown Report if the requirement to respond is not enforced. By not resolving possible excessive drawdowns soon after they occur, the Department cannot ensure that grantees are financially compliant and that drawdowns are not made in excess

of each grant's immediate cash needs.

Recommendations

We recommend that the Chief Financial Officer:

- 2.1 Ensure GPOS staff follow up with PO staff on grants to which they do not respond.
- 2.2 Develop and implement a process to periodically report to senior management on the responsiveness of POs to the monthly Excessive Drawdown Reports.

OCFO Comments:

OCFO concurred with the finding and recommendations. OCFO stated that it would develop internal procedures to ensure followup with PO staff on grants where they did not initially respond to reports referred for research and resolution. OCFO also said an excessive drawdown summary report would be developed and provided to senior management on a periodic basis to alert them about the responsiveness of PO staff to the monthly excessive drawdown reports.

FINDING NO. 3 – Improvements Are Needed in Use of Payment Flags to Prevent Inappropriate Drawdowns

The Department uses payments flags in GAPS to route or stop payments to grantees. These payment flags prevent inappropriate drawdowns by requiring review and approval by Department staff for the release of funds. We found, however, that improvements were needed in the use of payment flags to ensure that a payment flag applied to one grant is communicated to all program staff managing other grants by the same grantee, and to ensure payment flag reports in GAPS present complete and consistent information.

The revised Handbook, dated February 24, 2006, Section 5.3.8, "Fiscal Monitoring," Subparagraph 7, "Resolving Excess Cash Balances," states,⁵

- c. If the grantee does not resolve excess cash balances within two weeks after being contacted, the program official must consult with the program attorney and take one of the following actions:
 - 1) Activate the Route Payment Flag in GAPS and notify the grantee that all future payment requests will be routed to the program office for approval. Activating this flag ensures that payments will not be made without program staff approval.
 - 2) Require the program staff to transfer the grant from the advance payment method to the reimbursement payment method in GAPS, which requires

⁵ Prior to the recent update of the Handbook, the three payment flags and their uses were defined in Grants Policy Bulletin #27, *Monitoring Discretionary Grants for Excessive Drawdowns*, dated May 24, 2001. The revised Handbook was in effect for the scope of this review – payment flags as of May 2006.

that the grantee be reimbursed for expenses incurred. The license holder must activate the Reimbursement Flag in GAPS to take this action. Under the reimbursement method, the grantee must submit vouchers as proof of expenditures and explain why these expenditures are allowable. The program staff member may approve drawdowns only after the grantee has substantiated expenditures greater than the amount of the excess balances. If a new drawdown is appropriate, the program staff member brings supporting documentation to the license holder, who then can authorize payment.

- d. If the excess cash balances remain unresolved after taking the actions under paragraph c. above, the program official must consult with the program attorney and decide whether to designate the grantee as high-risk. If the grantee is designated high-risk, the program official must notify the grantee, and activate the stop payment flag in GAPS. Activating the stop payment flag will prevent the grantee from drawing down funds on an individual award or, if necessary, any award made to the entity until the excess cash issue has been resolved.

Specifically, we reviewed 163 awards made to 106 unique grantees during FY 2001 through FY 2005 to which payment flags had been assigned in GAPS. We found that 64 of the unique grantees (60 percent) had other active awards to which no payment flags had been applied. These 64 grantees had a total of 894 non-flagged awards with \$6.6 billion available to draw down as of May 22, 2006.

In GAPS, PO staff can generate reports to show payment flags by recipient, including the *Risk Management Report* and the *Payment Flag History – By Grantee*. However, we found payment flag information was not completely or consistently presented within the system. For example, a printed version of the *Risk Management Report* for all POs and all awards from FY 2003 returned 12,143 records with obligations totaling \$38.3 billion. The data from the same report exported to an electronic file only included 2,492 records with obligations totaling \$13.1 billion.

We also found that the most recent action in the *Payment Flag History – By Grantee* report did not correspond to the payment flag status in the *Risk Management Report* for 107 of the 163 awards reviewed (66 percent). Of these 107 awards:

- 59 awards reported a reimbursement flag in the *Risk Management Report*, however the *Payment Flag History – By Grantee* report indicated that route and/or stop payment flags were in effect,
- 46 awards with the route payment or stop payment flags listed as on the *Risk Management Report* did not match the most recent action on the *Payment Flag History – By Grantee* report, and
- 2 awards had multiple flags on the *Risk Management Report* that did not match the status on the *Payment Flag History – By Grantee* report.

Finally, we found that when the *Payment Flag History – By Grantee* listed a flag for an individual award, the flag did not always appear on the *Risk Management Report*. We reviewed all flag actions presented in the *Payment Flag History – By Grantee* reports for the 106 unique

recipients with the payment flags on the *Risk Management Report*. We identified a total of 212 awards with route payment and/or stop payment flags as the most recent action in the *Payment Flag History – By Grantee* report for which no flag was listed on the *Risk Management Report*.

GPOS confirmed that there is currently no mechanism in place to communicate payment flag information to all program offices that are responsible for monitoring additional grants awarded to the same grantee. While PO staff can generate GAPS reports to check if payment flags have been assigned to specific grantees, there is no requirement to do so. Nor is there any function within GPOS or in GAPS to communicate information regarding payment flags to all offices with grants to the same grantee.

With respect to the incomplete data in the *Risk Management Report*, the GAPS Report Team determined an error in the application caused the export to “crash” before it was completed. The GAPS Report Team stated they would work to identify the source of the problem and correct the issue. In addition, GPOS and GAPS Report Team staff were unsure why the reimbursement flag was not displayed on the *Payment Flag History – By Grantee* report, and stated this flag could be added to the report.

Due to the lack of communication regarding payment flags, and inconsistencies relating to payment flag reporting, the use of awarded funds may not be monitored at a level commensurate with the actual risk. Payment flags that have been placed on one award for financial responsibility and compliance issues, may be applicable to all awards for that grantee. In addition, program officials may not have complete and accurate data relating to payment flags to consider in making management decisions. This places these additional awards at risk of mismanagement or the same circumstances that resulted in application of the payment flag on one award.

Recommendations

We recommend that the Chief Financial Officer:

- 3.1 Develop and implement a method to communicate payment flag information, including the reasons the flag was imposed or cleared, to all program offices responsible for monitoring additional grants awarded to the same recipient.
- 3.2 Establish and implement policies and procedures to require PO staff to evaluate information received on payment flags for other awards to grantees to which they have also made or are making awards.
- 3.3 Review the payment flag reporting functionality within GAPS and correct issues noted with respect to exporting reports and inconsistencies between reports.

OCFO Comments:

OCFO concurred with the finding and recommendations. OCFO stated it would develop and implement necessary policies and procedures to address the first two recommendations. With

respect to the third recommendation, OCFO said it modified the Payment Flag History Report to include reimbursement flags and corrected the inconsistencies.

FINDING NO. 4 – The Department Did Not Monitor Formula Grants Through the Excessive Drawdown Reports

The Department developed the Excessive Drawdown Report in GAPS to identify grantees that may have violated cash management policies and regulations by drawing down funds in excess of a grant's immediate cash needs. However, this report was applied only to discretionary grants and did not include formula grants. The Department does not have a report to facilitate monitoring of excessive drawdowns for formula grants.

Standards for Internal Control in the Federal Government, issued by the Government Accountability Office, dated November 1999, provides the minimum level of quality acceptable for internal control in government and the basis against which internal control is to be evaluated. The Standards state,

These standards apply to all aspects of an agencies operations: programmatic, financial, and compliance . . . In implementing these standards, management is responsible for developing detailed policies, procedures, and practices to fit their agency's operations and to ensure they are built into and an integral part of operations.

The third standard for internal control, "control activities," is defined as follows:

Internal control activities help ensure that management's directives are carried out. The control activities should be effective and efficient in accomplishing the agency's control objectives . . . Control activities are an integral part of an entity's planning, implementing, reviewing, and accountability for stewardship of government resources and achieving effective results.

Education Department General Administrative Regulations, Part 80, "Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments," dated November 26, 2003, establishes uniform administrative rules, including financial management, for Federal grants and subawards to State, local and Indian tribal governments. Section 80.20(b)(7), entitled "Cash management," states,

Procedures for minimizing the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by grantees and subgrantees must be followed whenever advance payment procedures are used.

GPOS staff stated that some PO staff use portions of the *Discretionary Grant Handbook* to monitor formula grants, but there is no centralized policy for monitoring formula grants, and there is an overall lack of direction for formula grants. GPOS agreed that the Excessive Drawdown Report and other GAPS reports would be useful monitoring tools for formula, as well as discretionary grants. GPOS staff stated that different thresholds may need to be established for the formula grant programs, but they would work with the POs to create these thresholds.

Because the Excessive Drawdown Report or a similar report has not been developed for formula grants, the Department lacks assurance that program staff are adequately monitoring these grants to ensure that Department funds are being expended appropriately. In FY 2005, the Department awarded approximately \$38.7 billion in formula grants. By not identifying potential excessive drawdowns made by formula grantees, these Federal funds are at risk for being misused. Grantees may be drawing down funds in excess of their immediate cash needs for each grant and using the funds for inappropriate purposes.

Recommendations

We recommend that the Chief Financial Officer, in conjunction with the Deputy Secretary's Grants Improvement Project:

- 4.1 Ensure GAPS reports applicable to monitoring formula grant activity, such as the Excessive Drawdown Report, are also developed and implemented for these grants.

OCFO Comments:

OCFO did not concur with this finding and recommendation. OCFO stated that it has no authority to oversee formula grants, including developing policy for their administration. OCFO said it miscommunicated a statement regarding GPOS' oversight role for formula grants during the audit and that the applicable statement in our draft report was inaccurate.

OCFO also stated that, under 31 CFR, interest penalties are imposed on any state that makes excessive drawdowns under a formula grant program subject to the Cash Management Improvement Act. These interest penalties encourage states to follow appropriate cash management policies. In addition, OCFO said states are frequently late in disbursing funds to their vendors and subgrantees, and incur substantial interest penalties payable to the Federal government under the State administered programs of the Department. As a result, OCFO stated there does not appear to be a significant risk of loss to the Federal government.

OIG Comments:

Although OCFO indicated it has no authority to oversee formula grants, it is our understanding the Deputy Secretary's Grants Improvement Project, headed by OCFO, has been tasked to develop a Handbook for the Formula Grants Process. This handbook will include policies and procedures related to the fiscal management of formula grants. OIG believes the development and implementation of the GAPS reports for formula grants, such as the Excessive Drawdown Report, would be a useful tool for fiscal oversight. It will assist POs in their requirement to monitor grantees' fiscal activities to ensure funds are drawn in accordance with statutory and regulatory requirements. As such, we added to the recommendation that the Chief Financial Officer work in conjunction with the Deputy Secretary's Grants Improvement Project.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of our audit was to determine whether the Department's controls identify and prevent excessive cash drawdowns by grantees. To accomplish our objective, we performed a review of internal control applicable to the Department's monitoring of excessive drawdowns. We reviewed applicable laws and regulations, and Department policies and procedures. We conducted interviews with Department officials to gain an understanding of how the Excessive Drawdown Report is generated in GAPS and used by program staff to monitor excessive cash draws by grantees. In each PO reviewed, we conducted interviews with program staff responsible for researching and resolving grant drawdown activity. We also reviewed documentation provided by Department staff to support the resolution of excessive drawdowns included in our review. In addition, we evaluated the process used to generate the Excessive Drawdown Report in GAPS to identify the selection of grants included and excluded from the FY 2005 reports.

The universe for our audit was identified as excessive cash drawdowns made by grantees that appeared on the FY 2005 Excessive Drawdown Reports. We obtained the reports from GPOS and determined the reports included a total of 495 potentially excessive drawdowns made by 330 different grantees. We determined that OII and OPE had the largest number of potentially excessive drawdowns on the reports, with 236 and 189 drawdowns, respectively. Together, OII and OPE represented 425 of the 495 total drawdowns on the reports (86 percent). As such, we limited our detailed review to the drawdowns for these two POs. We selected sample drawdowns to review in each PO as follows:

- We stratified the universe of OII and OPE drawdowns by the thresholds reached on the excessive drawdown reports. We evaluated in three strata all grantees that exceeded the threshold level of 50 percent or more drawn in the first quarter, 80 percent or more drawn in the second quarter, and 100 percent in the third quarter. We randomly selected grants in each stratum in proportion to the universe of grants in each stratum, for a total random sample of 30 grants for each PO.
- We reviewed the PO justifications for all drawdowns on the exception reports and also judgmentally selected additional drawdowns with responses we deemed to require additional followup or for which the resolution provided appeared vague. In total, we judgmentally selected an additional 17 drawdowns for OII, and 21 drawdowns for OPE.
- After further review, we eliminated duplicate drawdowns, those for which PO staff did not provide a response (to be reported separately), and one grant for which the file had been archived and was no longer available for review. In total we eliminated 18 drawdowns from OII's sample, and 11 from OPE's sample.
- In total, our sample for detailed review included 29 OII drawdowns (30 random + 17 judgmental – 18 eliminated), and 40 OPE drawdowns (30 random + 21 judgmental – 11 eliminated), for a total of 69 excessive drawdowns.

We reviewed grant files for each of the 69 excessive drawdowns. In cases where we could not find appropriate documentation in the grant files, we referred our findings to OII and OPE staff to determine whether any additional documents existed to support the responses provided to GPOS. The results presented include consideration of additional documentation provided by OII or OPE.

To evaluate the appropriateness of the query used to generate the Excessive Drawdown Reports, we obtained text file extracts from GAPS of grants having excessive drawdown conditions identified in the reports that were generated by GPOS during FY 2005. A total population of 4,568 drawdowns was noted, representing 720 unique grant numbers. We obtained three detail data extract files from the GAPS Reports Team staff, which consisted of grant specific data, budget period date change records, and financial transaction postings. The detail extract files of grant/budget period level data along with summarized financial transactions were utilized to evaluate drawdown activity for FY 2005. For evaluation of grants with excessive drawdown conditions, we identified grant/budget period records that were either funded with FY 2005 funds or had some portion of an active current grant budget period during FY 2005. We identified a total population of 12,767 grants, comprised of 1,418 unique grantees, which met the excessive drawdown thresholds during FY 2005. To evaluate the analysis that produces the report, we used the extracts of GAPS drawdown data and compared this data to the text file extracts for the Excessive Drawdown Reports provided by GPOS.

We relied upon computer-processed data in GAPS and the Excessive Drawdown Reports generated through the GAPS software. We attempted to obtain the source code used to generate the report, but it was not available. We did obtain a copy of the source code for a different version of the Excessive Drawdown Report. We also obtained transactional data and repeated the process used to generate the report, based on descriptions in Department policy documents. As discussed in Finding 1, we found that the Excessive Drawdown Reports for FY 2005 did not include all appropriate grants, and did include some grants that should not have appeared on the report. As a result, we determined that that Excessive Drawdown Reports generated through GAPS were not accurate or complete. The most significant issue noted with the report was in completeness as we identified 1,379 grants that should have appeared on the reports, but did not. Less significant was the fact that the report included 166 grants that it should not have included because the grant period and funding was not current.

Through our sample of 69 responses provided by the POs to GPOS based on the potentially excessive drawdowns listed on the report, we found that PO staff generally did not disagree with the grants that were listed as having potentially excessive drawdowns. In 4 of the 69 responses (5.8 percent), PO staff stated that the grant period was over – a condition that was found in our review and reported as part of Finding 1.

While we found the Excessive Drawdown Report was significantly incomplete, and in some cases included grants it should not have included, we concluded that the issues were due to the method in which the report was generated, not the underlying data in GAPS. Testing the accuracy and completeness of the report was part of our objective to evaluate the Department's controls to prevent and detect excessive drawdowns. We reported issues noted in Finding 1 and made recommendations to the Department to correct the issues noted.

We conducted fieldwork at Department offices in Washington, DC, during the period October 2005 through August 2006. We held an exit conference with Department staff on August 10, 2006. Our audit was performed in accordance with generally accepted government auditing standards appropriate to the scope of the review described above.



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF THE CHIEF FINANCIAL OFFICER

THE CHIEF FINANCIAL OFFICER

NOV - 2 2006

TO: Helen Lew
Assistant Inspector General for Audit Services

FROM: Lawrence A. Warder

SUBJECT: Draft Audit Report
Controls Over Excessive Cash Drawdowns by Grantees
Control Number ED-OIG/A19F0025

Thank you for giving us the opportunity to review the subject draft audit report. We concur with your first three findings and provide the attached Corrective Action Plan (CAP) addressing each recommendation. As you can see from our corrective actions, OCFO is committed to improving policy and monitoring responsibilities for discretionary grants. We have already corrected several of the deficiencies identified in your draft audit report. Below is a general discussion of each finding in the draft report.

Finding No. 1 – Excessive Drawdown Reports Did Not Effectively Identify All Potentially Excessive Cash Drawdowns.

We concur with this finding and three recommendations. We have already taken immediate action and corrected the six query deficiencies noted in your first recommendation and the modified Excessive Drawdown Report was implemented on October 10, 2006. This report will ensure that all potentially excessive drawdowns are identified for all active grants, and ensure that grants that are no longer active are not included.

The remaining two recommendations under this finding require database enhancements and are included in the Phase I requirements for the new grants management system, G5. G5 Phase I implementation is to occur during the first quarter of fiscal year (FY) 2008. In the interim, we have developed a temporary work process, providing the necessary information to the Principal Offices (PO) starting in the first quarter of FY 2007.

Finding No. 2 – GPOS Did Not Ensure Program Offices Monitored Excessive Drawdowns

We concur with this finding and two recommendations. We will develop internal procedures to ensure follow up with PO staff on grants where the principal office

did not initially respond to reports referred for research and resolution. PO staff will be reminded that any unresolved excessive drawdowns will be reported to Department senior management. The development of an excessive drawdown summary report is currently underway. Once approved for dissemination, the report will be provided to senior management on a periodic basis to alert them about the responsiveness of PO staff to the monthly excessive drawdown reports. These procedures will be implemented by January 31, 2007.

Finding No. 3 – Improvements Are Needed in Use of Payment Flags to Prevent Inappropriate Drawdowns

We concur with this finding and will establish the necessary policies and procedures to address the first two recommendations. These policies and procedures will be implemented in concert with the completion of Phase I of G5 during the first quarter of FY 2008.

In anticipation of the third recommendation under this finding, we completed a review of the payment reporting functionality in GAPS and modified the Payment Flag History Report to include reimbursement flags. The revised report was implemented on August 25, 2006. In addition, the inconsistencies you noted in your draft audit report have also been reviewed and corrected. Therefore, reports are now displaying consistent information.

Finding No. 4 – The Department Did Not Monitor Formula Grants Through the Excessive Drawdown Reports

We do not concur with this finding and accompanying recommendation for various reasons. The CFO has no authority to oversee formula grants, including developing policy for their administration. The report's paragraph on page 11 regarding GPOS' statement on its oversight role for formula grants is inaccurate. We regret any miscommunication that you may have received during your audit on this issue.

Formula grant drawdowns, unlike discretionary grant drawdowns, are governed by U. S. Treasury regulations for Federal-State fund transfers stipulated in 31 CFR, which the draft cites. Under this statute, interest penalties are imposed on any state that makes excessive draws under a formula grant program subject to the Cash Management Improvement Act (CMIA). These interest penalties encourage states to follow appropriate cash management policies.

In addition, a number of states' constitutions require that states only issue payment orders when funds are available in the account charged for the payment. Thus, these states must draw funds before they can issue payments to vendors and subgrantees. These states are frequently late in disbursing funds to their vendors and subgrantees, and incur substantial interest penalties payable to the Federal

government under the State administered programs of the Department. There does not appear to be a significant risk of loss of to the Federal government as a result of these state constitutional requirements.

With your recommendations, we are confident that the delivery and monitoring of discretionary grants will benefit the entire Department. I appreciate your staff's effort in this area and look forward to working with them regarding the specifics of each finding.

We are providing our comments electronically to Michele Weaver-Dugan, Director, Operations Internal Audit Team, per the instructions in your September 19, 2006 email. If you have any questions concerning our response or CAP, please contact Constance Davis at (202) 401-3892 regarding GAPS or G5 issues and Blanca Rodriguez at (202) 245-6121 regarding policy and procedure issues.

Attachment