

CORPORATION

FOR NATIONAL

 SERVICE

OFFICE OF THE INSPECTOR GENERAL

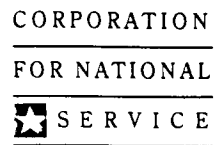
Audit of

**Commission on National and Community Service
Award Number 92NMSTPA0007 to PennSERVE**

This report is issued to CNS Management. According to OMB Circular A-50, *Audit Follow Up*, the Corporation must make final management decisions on the report's findings and recommendations no later than May 24, 1997. Consequently, the reported findings do not necessarily represent the final resolution of the issues presented or the amount of disallowed costs.

The Inspector General must approve any request for public release of the report.

Office of the Inspector General
Audit of
Commission on National and Community Service
Award Number 92NMSTPA0007 to PennSERVE



Leonard G. Birnbaum and Company, under contract to the Office of Inspector General, performed an audit of the funds awarded by the former Commission on National and Community Service to PennSERVE for the period August 1, 1992 to December 31, 1995 (award number 92NMSTPA0007).

The audit included an examination to determine whether financial reports prepared by the auditees presented fairly the financial condition of the award and the award costs reported to CNS were documented and allowable in accordance with the terms and conditions of the award. We have reviewed the report and workpapers supporting its conclusions and agree with the findings and recommendations presented.

Leonard G. Birnbaum and Company found that PennSERVE lacked adequate

- controls over its financial management system;
- controls for monitoring subrecipients; and
- segregation of duties.

In addition, PennSERVE incurred administrative costs in excess of the maximum allowed under the terms of the award. Based on Leonard G. Birnbaum and Company's audit, we are questioning \$874,971 in costs claimed under the award. These and other matters are discussed in detail in this report.

A draft of this report was provided to PennSERVE and CNS for comment. PennSERVE's comments (excluding attachments) are included as Appendix 1. Copies of the attachments were provided to CNS' Office of Grants Management Services for their consideration during the resolution process. CNS did not provide a response.

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Getting Things Done.
AmeriCorps, National Service
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National Senior Service Corps

**Commission on National and Community Service
Award Number 92NMSTPA0007**

to

PennSERVE

**1304 Labor and Industry Building
7th and Forster Streets
Harrisburg, PA 17120**

Financial Schedules

and

Independent Auditor's Reports

For the Period

August 1, 1992 to December 31, 1995

Leonard G. Birnbaum and Company

Certified Public Accountants

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PennSERVE

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REPORT SUMMARY AND HIGHLIGHTS

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1201 New York Avenue, NW
Washington, DC 20525**

PURPOSE AND SCOPE OF AUDIT

We have performed an audit of the funds awarded by the Commission on National and Community Service¹ (Commission) to PennSERVE as follows:

<u>Award Number</u>	<u>Award Period</u>	<u>Audit Period</u>
92NMSTPA0007	August 1, 1992 to December 31, 1995	August 1, 1992 to December 31, 1995

The objectives of our audit were to determine whether:

1. Financial reports prepared by the auditee presented fairly the financial condition of the award;
2. The system of internal control structure was adequate to safeguard Federal funds;
3. The auditee had adequate procedures and controls to ensure compliance with Federal laws, applicable regulations and award conditions; and

¹ On December 14, 1993, the Corporation for National and Community Service established audit responsibility for all programs administered by the Corporation as well as grants awarded by the former Commission on National and Community Service in its Office of Inspector General.

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4. The award costs reported to the Commission were documented and allowable in accordance with the award terms and conditions.

We performed the audit in accordance with generally accepted auditing standards, and *Government Auditing Standards* (1994 Revision) issued by the Comptroller General of the United States. Those standards required that we plan and perform the audit to obtain reasonable assurance about whether the amounts claimed against the grant award as presented in the schedule of award costs (Exhibit A), are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in Exhibit A. An audit also includes assessing the accounting principles used and significant estimates made by the auditee, as well as evaluating the overall financial schedule presentation. We believe our audit provides a reasonable basis for our opinion.

SUMMARY OF AUDIT RESULTS

An audit was performed on the financial reports submitted by PennSERVE to the Commission. These reports are summarized in Exhibit A as follows:

<u>Award Number</u>	<u>Award Budget</u>	<u>Claimed Costs</u>	<u>Questioned Costs</u>
92NMSTPA0007	<u>\$5,800,000</u>	<u>\$4,350,331</u>	<u>\$874,971</u>

As a result of our audit of the aforementioned award, we are questioning costs totaling \$874,971. Questioned costs are costs for which there is documentation that the recorded costs were expended in violation of the law, regulations or specific conditions of the award or those costs which require additional support by the grantee or which require interpretation of allowability by CNS.

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The following summarizes the costs questioned on the above award by reason:

<u>Explanation</u>	<u>Amount</u>
• Lack of support documentation	\$1,749
• Unallowable costs	141
• Misallocation of common costs	4,731
• Excess claimed cost over incurred cost:	
Post Service Benefits	264,105
Other	<u>156,197</u>
	420,302
• Excess advance funds over claimed cost	1,292
• Administrative costs exceeds maximum Federal share	430,945
• Insurance premiums incurred for terminated participants	15,368
• Incurred costs for participants of another program	<u>443</u>
Total Questioned Costs	<u>\$874,971</u>

We used a judgmental sampling method to test the costs claimed by the auditee. Based upon this sampling plan, questioned costs in this report may not represent total costs that may have been questioned had all expenditures been tested. In addition, we have made no attempt to project such costs to total expenditures claimed, based on the relationship of costs tested to total costs.

The following is a brief description of the various findings which resulted from our audit. For a complete discussion of each finding, refer to the appropriate Independent Auditor's Report on Compliance or Independent Auditor's Report on Internal Control Structure.

COMPLIANCE FINDINGS

Our audit disclosed the following instances of noncompliance:

- The subrecipient did not maintain an adequate financial management system in accordance with OMB Circular A-110, Subpart C, Section .21 (b). (Finding No. 1)
- Administrative costs incurred exceeded the maximum share ratio (Finding No. 2)

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INTERNAL CONTROL STRUCTURE

Our audit disclosed the following matters which we consider to be a reportable condition in the internal control structure and its operation:

- The subrecipient lacks adequate segregation of duties. (Finding No. 1)
- The grantee lacks adequate controls for monitoring subrecipients. (Finding No. 2)
- The subrecipient lacks adequate controls over their financial management system (Finding No. 3)

MATTER REQUIRING RESOLUTION

Pennsylvania Association of Colleges and Universities, a subrecipient of PennSERVE, acquired equipment, at a cost of \$64,040, during its performance of the grant. The terms of the grant provide that title to the equipment vests with PennSERVE, but that CNS has a reversionary interest in the equipment and the right to direct the disposition upon completion of grant performance. As of the date of our audit, PennSERVE had not received any direction from CNS as to the disposition of the equipment. We observe that PennSERVE, prior to the conclusion of this grant, has been awarded other grants by CNS.

OTHER MATTERS

The Pennsylvania Service Corps (PSC), a component of the Pennsylvania Association of Colleges and Universities (PACU), which was subcontracted by PennSERVE to administer the program will be ceasing operations and dissolving prior to the end of calendar year 1996.

During the course of the audit, several issues came to our attention that PennSERVE and PACU have been unable to resolve. Each of these issues are summarized below along with our observations and recommendations concerning these issues.

- There have been some questions as to whether or not the post service benefits are includable or excludable from gross income which would affect whether or not the benefits are subject to FICA taxes. Paragraph 760, Scholarships and Fellowships, of the 1996 Commerce Clearing House, Inc. Payroll Management Guide; which is an

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interpretation of the Internal Revenue Code; states, in part, that "qualified scholarships (grants made to students to further their education) and fellowships (grants to any individual to pursue additional study or training) are excludable from gross income of the recipient and are not subject to income tax withholding, FICA, or FUTA.....The exclusion does not apply to any portion of amounts received as a grant or tuition reduction that represents payment for teaching, research, or other services required as a condition of receiving the grant." We observe that based on this interpretation, the post service benefits would be includable in gross income since the participant is not eligible to receive an education award unless the specified term of service has been completed.

- Questions have been raised as to whether PennSERVE or PACU has the responsibility of accounting for and disbursing the post service benefits after the grant period. Even though the grant period ended on December 31, 1995, the post service benefits can be paid to the eligible participants for several years to come. We recommend that the excess funds received for the payment of such benefits be returned to CNS via the Department of Health and Human Services and that interest be remitted on the excess funds in accordance with the Cash Management Improvement Act of 1990 which states that regulations shall be issued which require a State "to pay interest to the United States on funds from the time funds are deposited by the United States to the State's account until the time that funds are paid out by the State in order to redeem checks or warrants or make payments by other means for program purposes". We further recommend that CNS officially close the grant and establish a separate account for the payment of post service benefits earned as a result of this grant.
- The grant requires that 50 percent of the post service benefits be matched with non-Federal sources. PACU had agreements with each of the entities that the participants were providing services to fund the required match early in the participant's term of service. The agreements further stated that if the participant did not complete their term of service, the funds would be refunded on a pro rata basis in relation to the number of months services were provided by the participant to the entity. Since all of the participants did not complete the necessary requirements to earn an education award, PACU has received matching funds in excess of the amount needed to meet the match requirement for those participants that earned education awards. Based on our computations, PACU has received excess funds in the amount of \$33,539. Of this amount, \$7,465 has been refunded to the appropriate entities. PACU stated that it was unsure how the remaining excess funds should be handled. We recommend that the excess funds be refunded to the entities which provided the funds. In the event that

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the funds are not refunded to the appropriate entities, the funds would be considered program income thus subjecting the funds to the requirements of OMB Circular A-110, Subpart C, Section .24.

BACKGROUND

PennSERVE is an organizational unit of the Labor and Industry Department of the State of Pennsylvania. PennSERVE was established in 1988 with the mission of promoting community Service.

Award Number

Award Description

92NMSTPA0007

PennSERVE received a two year grant in 1992 in the amount of \$5,800,000 under Subtitle D of the National Community Service Act of 1990. The grant was made to establish a Pennsylvania Service Corps. PennSERVE subcontracted with the Pennsylvania Association of Colleges and Universities (PACU), a nonprofit organization, to administer the Pennsylvania Service Corps.

REPORT RELEASE

We provided a draft of this report to PennSERVE and CNS for comment. PennSERVE's comments (excluding attachments) are included as Appendix 1. We also provided CNS' Office of Grants Management Services copies of the attachments for their consideration during the resolution process. CNS did not provide a response. This report is intended for the information and use of the Corporation's management and its Office of Inspector General and PennSERVE's management and its subrecipient. However, this report is a matter of public record and its distribution is not limited.

INDEPENDENT AUDITOR'S REPORT

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INDEPENDENT AUDITOR'S REPORT

We have audited the costs claimed by PennSERVE to the Corporation for National Service and its predecessor, the Commission on National and Community Service, on the Financial Status Report - Federal Share of Outlays for the grant number listed below. These Financial Status Reports, as presented in the schedule of award costs (Exhibit A), are the responsibility of the Grantee's management. Our responsibility is to express an opinion on Exhibit A based on our audit.

<u>Award Number</u>	<u>Award Period</u>	<u>Audit Period</u>
92NMSTPA0007	August 1, 1992 to December 31, 1995	August 1, 1992 to December 31, 1995

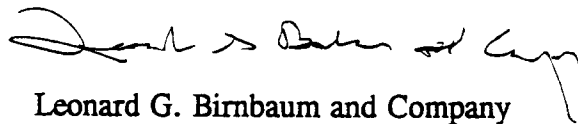
We conducted our audit in accordance with generally accepted auditing standards, and *Government Auditing Standards* (1994 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as, evaluating the overall financial schedule presentation. We believe our audit provides a reasonable basis for our opinion.

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The accompanying financial schedules were prepared for the purpose of complying with the requirements of the award agreement as described in Note 1, and are not intended to be a complete presentation of financial position in conformity with generally accepted accounting principles.

In our opinion, except for \$874,971 questioned costs (see Exhibit A), the financial schedules referred to above present fairly, in all material respects, the costs claimed in the Financial Status Report - Federal Share of Outlays as presented in the schedule of award costs (Exhibit A), for the period August 1, 1992 to December 31, 1995, in conformity with the award agreements.

We provided a draft of this report to PennSERVE and CNS for comment. PennSERVE's comments (excluding attachments) are included as Appendix 1. We also provided CNS' Office of Grants Management Services copies of the attachments for their consideration during the resolution process. CNS did not provide a response. This report is intended for the information and use of the Corporation's management and its Office of Inspector General and PennSERVE's management and its subrecipient. However, this report is a matter of public record and its distribution is not limited.


Leonard G. Birnbaum and Company

Alexandria, Virginia
August 2, 1996

FINANCIAL SCHEDULES

PennSERVE
 Commission on National and Community Service Award No. 92NMSTPA0007
 Schedule of Award Costs
 From August 1, 1992 to December 31, 1995
 Final

<u>Cost Category</u>	<u>Approved Budget</u>	(A) <u>Claimed Costs</u>	<u>Incurred As Reclassified</u>	<u>Questioned Costs</u>	<u>Reference</u>
Participant support costs -					
Full-time participants:					
Living allowance and benefits	\$2,151,296	\$	\$1,873,645	\$ 288	Exhibit B
Health insurance	220,000		168,720	15,523	Exhibit B
Post-service benefits	564,270		262,782		
In-service education	453,630		246,073	1,890	Exhibit B
Other	<u>285,694</u>		<u>6,482</u>		
Subtotal	<u>3,674,890</u>	<u>3,010,689</u>	<u>2,557,702</u>	<u>17,701</u>	
Participant support costs-					
Part-time participants:					
Living allowances and benefits	221,080		-		
Health insurance	40,000		-		
Post-service benefits	345,088		4,663		
In-service education	212,992		-		
Other	<u>209,374</u>		<u>-</u>		
Subtotal	<u>1,028,534</u>	<u>109,231</u>	<u>4,663</u>	<u>-</u>	
Training of supervisors and participants					
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	
Evaluation					
	<u>355,390</u>	<u>124,880</u>	<u>-</u>	<u>-</u>	
Other program costs					
Operating	158,000		267,311	2,703	Exhibit B
Capital	<u>110,000</u>		<u>64,040</u>	<u>528</u>	Exhibit B
Subtotal	<u>268,000</u>	<u>500,454</u>	<u>331,351</u>	<u>3,231</u>	
Administration					
	<u>290,000</u>	<u>186,460</u>	<u>626,325</u>	<u>430,945</u>	Exhibit B
Other					
	<u>183,186</u>	<u>418,617</u>	<u>409,988</u>	<u>1,500</u>	Exhibit B
Total	<u>5,800,000</u>	<u>4,350,331</u>	<u>3,930,029</u>	<u>453,377</u>	
Excess claimed over incurred				<u>420,302</u>	Exhibit B
Excess advanced over claimed				<u>1,292</u>	Exhibit B
TOTAL CNS FUNDS	<u>\$5,800,000</u>	<u>\$4,350,331</u>	<u>\$3,930,029</u>	<u>\$ 874,971</u>	

(A) The total representing costs claimed agrees with the expenditures reported on the Financial Status Report as of the quarter ended December 31, 1995. Claimed costs reported above are taken directly from the auditee's books of account.

The accompanying notes are an integral part of this financial schedule.

PennSERVE
 Commission on National and Community Service Award No. 92NMSTPA0007
 Schedule of Incurred Costs
 From August 1, 1992 to December 31, 1995
 Final

<u>Cost Category</u>	<u>Incurred Costs</u>	<u>Reclassified Costs</u>	<u>Incurred As Reclassified</u>	<u>Reference</u>
Participant support costs -				
Full-time participants:				
Living allowance and benefits	\$ 1,873,645	\$	\$ 1,873,645	
Health insurance	168,720		168,720	
Post-service benefits	262,782		262,782	
In-service education	246,791	(718)	246,073	Schedule B
Other	<u>6,482</u>		<u>6,482</u>	
Subtotal	<u>2,558,420</u>	<u>(718)</u>	<u>2,557,702</u>	
 Participant support costs-				
Part-time participants:				
Living allowances and benefits	-		-	
Health insurance	-		-	
Post-service benefits	4,663		4,663	
In-service education	-		-	
Other	<u>-</u>		<u>-</u>	
Subtotal	<u>4,663</u>	<u>-</u>	<u>4,663</u>	
 Training of supervisors and participants	<u>-</u>	<u>-</u>	<u>-</u>	
 Evaluation	<u>57,299</u>	<u>(57,299)</u>	<u>-</u>	Schedule B
 Other program costs				
Operating	265,811	1,500	267,311	Schedule B
Capital	<u>64,040</u>		<u>64,040</u>	
Subtotal	329,851	1,500	331,351	
 Administration	<u>217,134</u>	<u>409,191</u>	<u>626,325</u>	Schedule B
 Other	<u>762,662</u>	<u>(352,674)</u>	<u>409,988</u>	Schedule B
 TOTAL CNS FUNDS	<u>\$ 3,930,029</u>	<u>\$ -</u>	<u>\$ 3,930,029</u>	

The accompanying notes are an integral part of this financial schedule.

PennSERVE
Commission on National and Community Service Award No. 92NMSTPA0007
Schedule of Questioned Costs
From August 1, 1992 to December 31, 1995
Final

1. Living allowance

During the course of the grant, the grantee realized that the subrecipient had been claiming the cost of living allowances for participants on a different program under this grant. After this error was brought to the attention of the subrecipient, the subrecipient remitted funds in the amount of \$219,628 to the grantee. This amount was based on actual expenditures through April 28, 1995, and estimated expenditures for the period ended May 12, 1995. We computed the actual expenditures through May 12, 1995, claimed on this grant to be \$219,916. We have, therefore, questioned the difference of \$288.

2. Health insurance

As a result of the subrecipient's A-133 audit performed by its outside accountants, the subrecipient became aware of the fact that health insurance benefits had not always been terminated upon the participant's completion or dismissal from the program. The subrecipient then revisited its insurance policy and discovered that premiums in the amount of \$15,368 had been paid for such participants. Although the insurance company issued a credit on the subrecipient's account, it was not issued while any participants on this grant were still covered by the insurance policy, thereby, resulting in the credit being applied against another grant's expenses. We have, therefore, questioned this amount. We have questioned an additional \$155 because the amount paid (check no. 1334) and recorded as an expenditure of this grant included the health premium for a participant of another grant.

The accompanying notes are an integral part of this financial schedule.

PennSERVE
Commission on National and Community Service Award No. 92NMSTPA0007
Schedule of Questioned Costs
From August 1, 1992 to December 31, 1995
Final

3. In-service education

We have questioned \$1,749 and \$141 for lack of supporting documentation and unallowability of costs, respectively, for a total of \$1,890.

<u>Check no.</u>	<u>Amount</u>		
1491	\$ 550		
1433	167		
1614	400		
1832	366		
10335	<u>266</u>		
Subtotal	<u>1,749</u>		
1925	63	Lost pillow cases	} Unreasonable
10167	52	Lost keys, swimming/ bowling guards	
10226	<u>26</u>	Flowers	
Subtotal	<u>141</u>		
Total	<u>\$1,890</u>		

4. Operating

In August 1994, the subrecipient began operating another Federally funded program of a similar nature. At this point, it was necessary to allocate certain common costs as between the two programs. The costs were to have been allocated on the basis of the number of participants in each program. Our testing of transactions indicated that certain expenditures (check nos. 11201, 11003, and 11143) were not distributed between the two programs even though they benefited both. We applied the cost allocation percentages to these costs and have questioned \$2,703.

The accompanying notes are an integral part of this financial schedule.

PennSERVE
Commission on National and Community Service Award No. 92NMSTPA0007
Schedule of Questioned Costs
From August 1, 1992 to December 31, 1995
Final

5. Capital

As discussed in note 4, the subrecipient allocates common program costs. We noted, however, that check no. 11201 had not been distributed between the two programs. Application of the allocation plan yielded \$528 which should have been recorded as an expense of the other program, therefore, we have questioned this amount.

6. Other

As discussed in note 4, the subrecipient allocates common program costs. We noted, however, that certain expenditures (check nos. 10784, 10857, and 10936) were not distributed between the two programs even though they benefited both. Application of the allocation plan yielded \$1,500 which should have been recorded as an expense of the other program, therefore, we have questioned this amount.

7. Administration

We have questioned \$430,945 of the amount incurred for administration. The amount was questioned because the incurred cost exceeded the maximum Federal share. According to Provision 9 of the National and Community Service Programs, Special Provisions "not more than 5% of funds received under this grant shall be used for administrative costs."

The amount questioned was calculated as follows:

Total Administration Costs Incurred		\$ 217,134
Reclassifications From:		
Evaluation	\$ 50,799	
PSC Training	718	
Other:		
Salaries	247,540	
FICA	18,937	
Benefits	55,930	
Accounting	<u>35,267</u>	
Net		<u>409,191</u> <u>\$ 626,325</u> A

The accompanying notes are an integral part of this financial schedule.

PennSERVE
Commission on National and Community Service Award No. 92NMSTPA0007
Schedule of Questioned Costs
From August 1, 1992 to December 31, 1995
Final

7. Administration - continued

Total Incurred Cost		\$3,930,029
Questioned Costs		
PSC	17,701	
Other Program Costs	3,231	
Other	<u>1,500</u>	
		<u>22,432</u>
Net		\$3,907,597
Five Percent Limitation		<u>195,380</u> B
Excess Over Limitation (A-B)		<u>\$ 430,945</u>

8. Excess claimed costs over incurred costs

As discussed in finding no. 1 of the Independent Auditor's Report on Compliance the subrecipient does not have an adequate financial management system which has resulted in the subrecipient claiming costs in excess of the costs incurred by an amount of \$420,302. We have, therefore, questioned this amount. We were able to determine that of this amount, \$264,105 was associated with post service benefits. We were not, however, able to identify the remaining amount of \$156,197 to a particular budget line item.

9. Excess advanced funds over claimed costs

The final Financial Status Report (FSR) submitted by the grantee indicated that the total claimed costs were \$4,350,331 while the Federal Cash Transaction Report (FCTR) for the period ended March 31, 1996, reported that cumulative advances for this grant were \$4,351,623. This results in a difference of \$1,292 which we have questioned.. The grantee indicated that it would be processing a refund check in this amount in the near future.

The accompanying notes are an integral part of this financial schedule.

PennSERVE
Commission on National and Community Service Award No. 92NMSTPA0007
Schedule of Reclassified Costs
From August 1, 1992 to December 31, 1995
Final

1. Participant Support Cost - Full-Time

We have reclassified \$718 (check nos. 1919 and 10071) of the amount incurred for in-service education to administration. Our review of the support documentation disclosed that the expenditure was for temporary help whose duties were of a clerical nature.

2. Evaluation

The grant general provision, paragraph 8 (b), states, "all funded programs will be evaluated based on their effectiveness in achieving any or all goals set forth in Chapter 25 of 45 CFR, National and Community Service Grant Program." Based on our review of the documents produced as a result of the expenditures incurred for evaluation, we do not consider the services provided to be an evaluation of the program. Some of the documents produced were the quarterly progress reports, a staff policy and procedures manual, community partner policy manual, corps member policy and procedure manual, annual Pennsylvania Service Corps directories and various other pamphlets about the program based on surveys from the participants, supervisors, etc. We have, therefore, reclassified all of the costs incurred as evaluation (\$57,299) from evaluation to administration with the exception of \$5,000 (check nos. 10784, 10857, and 10936) which we reclassified to Other and \$1,500 (check no. 11033) which we reclassified to Operating since these expenditures were for a consultant to provide program training services and travel expenses for a consultant, respectively.

3. Other

We have reclassified \$357,674 from Other to Administration since these costs represent the salaries of administrative personnel along with related fringe benefits and accounting fees. The Grant General Provisions define administrative costs or expenses, in part, as "costs associated with overall program administration; salaries and benefits for director and administrative staff of existing organizations that sponsor a funded program; and insurance that protects the grantee (e.g., liability insurance)."

The accompanying notes are an integral part of this financial schedule.

PennSERVE
Commission on National and Community Service Award No. 92NMSTPA0007
Notes to Financial Schedules

1. **Summary of Significant Accounting Policies**

Accounting Basis

The accompanying financial schedules, Exhibits A and B, have been prepared from the reports submitted to CNS and the Commission. The basis of accounting utilized in preparation of these reports differs from generally accepted accounting principles. The following information summarizes these differences.

A. **Equity**

Under the terms of the award, all funds not expended according to the award agreement and budget at the end of the award period are to be returned to CNS. Therefore, the auditee does not maintain any equity in the award and any excess of cash received from CNS over final expenditures is due back to CNS.

B. **Equipment**

Equipment is charged to expense in the period during which it is purchased instead of being recognized as an asset and depreciated over its useful life. As a result, the expenses reflected in the statement of award costs include the cost of equipment purchased during the period rather than a provision for depreciation.

The equipment acquired is owned by PennSERVE while used in the program for which it is purchased or in other future authorized programs. However, CNS has the reversionary interest in the equipment. Its disposition, as well as the ownership of any proceeds therefrom, is subject to Federal regulations.

C. **Inventory**

Minor materials and supplies are charged to expense during the period of purchase. As a result, no inventory is recognized for these items in the financial schedules.

2. **Income Taxes**

PennSERVE is a component of a state government and is exempt from income taxes.

INDEPENDENT AUDITOR'S REPORTS
ON
COMPLIANCE AND INTERNAL CONTROL STRUCTURE

LEONARD G. BIRNBAUM AND COMPANY

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE

We have audited the schedule of award costs, as presented in Exhibit A, which summarizes the financial reports submitted by PennSERVE to the Corporation for National Service and its predecessor, The Commission on National and Community Service for the award listed below, and have issued our report thereon dated August 2, 1996.

<u>Award Number</u>	<u>Award Period</u>	<u>Audit Period</u>
92NMSTPA0007	August 1, 1992 to December 31, 1995	August 1, 1992 to December 31, 1995

We conducted our audit in accordance with generally accepted auditing standards, and *Government Auditing Standards* (1994 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement.

Compliance with laws, regulations, and the provisions of the award is the responsibility of PennSERVE's management. As part of obtaining reasonable assurance about whether the financial schedules are free of material misstatement, we performed tests of compliance with certain provisions of laws, regulations, and the terms and conditions of the award. However, our objective was not to provide an opinion on overall compliance with such provisions.

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Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in statutes, regulations, and the provisions of the award that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial schedules. The results of our tests of compliance disclosed the following material instances of noncompliance:

Finding No. 1

The subrecipient does not maintain an adequate financial management system in accordance with OMB Circular A-110, Subpart C, Section .21 (b). Section .21 (b) states, in part, that:

“Recipients’ financial management systems shall provide for the following.

- (1) Accurate, current, and complete disclosure of financial results of each federally-sponsored project or program in accordance with the reporting requirements set forth in Section .52...
- (2) Records that identify adequately the source and application of funds for federally-sponsored activities...
- (3) Effective control over and accountability for all funds, property and other assets...
- (4) Comparison of outlays with budget amounts for each award...
- (5) Written procedures to minimize the time elapsing between the transfer of funds to the recipient from the U.S. Treasury and the issuance or redemption of checks, warrants or payments by other means for program purposes by the recipient...
- (6) Written procedures for determining the reasonableness, allocability and allowability of costs in accordance with the provisions of the applicable Federal cost principles and the terms and conditions of the award.
- (7) Accounting records including cost accounting records that are supported by source documentation.”

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The subrecipient's financial management system does not provide for the comparison of budget versus actual expenditures or comparison of actual expenditures versus advanced funds. Nor does the subrecipient have written procedures to minimize the time elapsing between the advance of funds and the expenditure of these funds. As a result of the lack of these comparisons and procedures, the subrecipient obtained cash advances which were not "limited to the minimum amounts needed" to meet "the actual, immediate cash requirements of the recipient organization in carrying out the purpose of the approved program or project" as required by Section .22 (b) of OMB Circular A-110. Not only did this lack of comparisons and procedures result in the advancement of funds significantly exceeding the incurred costs (approximately 10%), but it also resulted in the shifting of funds by cost category without prior approval as required by Section .25 (c) of OMB Circular A-110 since certain cost categories exceeded the approved budget. Furthermore, the subrecipient did not provide supervisory control over the preparation of Federal award records. Lastly, accounting records were not always supported by adequate source documentation as some of the supporting documentation was nothing more than purchase requests without receipts, invoices, etc.

Recommendation

We recommend that the subrecipient develop and implement policies and procedures for the establishment of an adequate financial management system.

Auditee's Comments

According to the grantee, the subrecipient was notified by letter on May 1, 1995, that it was in noncompliance with several provisions of the grant. The grantee further stated that when the problems in the subrecipient's financial management system "became apparent to the President of PACU, personnel changes were made in the staff of the grant" and "steps were taken to correct the problems with the financial management system and then to document the problems."

Auditor's Response

Although the grantee and subrecipient recognized that deficiencies existed in the financial management system of the subrecipient prior to the end of the grant, we do not feel that an adequate system existed by the end of the grant.

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Finding No. 2

The grantee incurred excessive administrative costs. According to Provision 9 of the National and Community Service Programs, Special Provisions, "not more than 5% of funds received under this grant shall be used for administrative costs." After consideration of total questioned costs, excluding administration and the differences between the claimed and incurred costs and the differences between the amount claimed per the Financial Status Report and the amount advanced per the Federal Cash Transaction Report, the incurred amount for administration represents approximately 16 percent of the total incurred costs.

Recommendation

We recommend that the claimed costs for administration be limited to the rate specified by the provisions.

Auditee's Comments

"PennSERVE and PACU strongly disagree with this finding. Documentation provided as Attachment B clearly supports PennSERVE's and PACU's understanding that the five percent limit on administrative costs apply only to the general administrative oversight provided by PACU, not to the costs associated with program staff hired specifically to operate the provisions of grant #92NMSTPA0007."

Auditor's Response

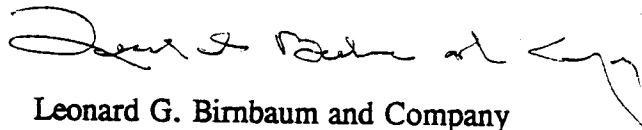
It is clear that PennSERVE and PACU disagree with our interpretation of the terms and conditions of the grant. We have reviewed the auditee's comments and are not persuaded that our interpretation is incorrect. Accordingly, this is a matter to be resolved by the Office of Grant Management Services.

We considered these material instances of noncompliance in forming our opinion on whether Exhibit A is presented fairly in all material respects, in conformity with Corporation for National Service policies and procedures, and this report does not affect our report dated August 2, 1996, on those financial schedules.

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Corporation for National Service
Washington, DC 20525

Except as described above, the results of our tests of compliance indicate that, with respect to the items tested, the grantee has complied in all material respects, with the provisions referred to in the third paragraph of this report.

We provided a draft of this report to PennSERVE and CNS for comment. PennSERVE's comments (excluding attachments) are included as Appendix 1. We also provided CNS' Office of Grants Management Services copies of the attachments for their consideration during the resolution process. CNS did not provide a response. This report is intended for the information and use of the Corporation's management and its Office of Inspector General and PennSERVE's management and its subrecipient. However, this report is a matter of public record and its distribution is not limited.



Leonard G. Birnbaum and Company

Alexandria, Virginia
August 2, 1996

LEONARD G. BIRNBAUM AND COMPANY

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL STRUCTURE

We have audited the schedule of award costs, as presented in Exhibit A which summarizes the financial reports submitted by PennSERVE to the Corporation for National Service and its predecessor, the Commission on National and Community Service, for the grant listed below, and have issued our report thereon dated August 2, 1996.

<u>Award Number</u>	<u>Award Period</u>	<u>Audit Period</u>
92NMSTPA0007	August 1, 1992 to December 31, 1995	August 1, 1992 to December 31, 1995

We conducted our audit in accordance with generally accepted auditing standards, and *Government Auditing Standards* (1994 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement.

In planning and performing our audit of Exhibit A for the period August 1, 1992 to December 31, 1995, we considered the grantee's internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the financial schedules and not to provide assurance on the internal control structure.

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The grantee's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs on internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial schedules in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- Cash Disbursements
- Cash Receipts
- Payroll/timekeeping
- Recordkeeping

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we have assessed control risk.

We noted the following matters involving the internal control structure and its operation that we consider to be a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure, that, in our judgment, could adversely affect the entity's ability to record, possess, summarize and report financial data consistent with the assertions of management in the financial schedules.

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Corporation for National Service
Washington, DC 20525

Finding No. 1

The subrecipient lacks adequate segregation of duties. Currently, almost all of the accounting functions are performed by one person. For the internal control structure to be effective, there needs to be an adequate division of duties among those who perform accounting procedures and handle assets. Such arrangements reduce the risk of error and limit opportunities to misappropriate assets. While we recognize that the subrecipient is a small organization and a lack of segregation of duties is inherent in small organizations, we feel that duties can be segregated more than they are presently.

Recommendation

We recommend that the accounting functions be reviewed and evaluated to determine whether it is possible to provide more segregation of duties.

Auditee's Comments

"The bookkeeper at PACU and the former fiscal officer prepared checks for the signature of the President of PACU. At no time did either the bookkeeper or fiscal officer sign checks. As a small organization, PACU does not have sufficient personnel to distribute these duties further. PACU is satisfied that the 'checks and balances' that are part of their policies are sufficient"

Auditor's Response

While the preparation and signing of checks is performed by separate persons this does not compensate for the fact that one individual receives receipts, makes deposits, prepares checks, reconciles the bank account and maintains the accounting records. Furthermore, during the audit a representative of the subgrantee acknowledged that there was a lack of segregation of duties and that it was in the process of reorganizing the duties of personnel with the intention of resolving this problem by January 1997. Our recommendation, therefore, still remains.

A material weakness is reportable conditions in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or regularities in amounts would be material in relation to the financial schedules being

Inspector General
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Washington, DC 20525

audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. We believe the reportable condition described above is not a material weakness. However, our study and evaluation and our audit disclosed the following conditions that we believe result in more than a relatively low risk that errors or irregularities in amounts that would be material to the CNS grant may occur and not be detected within a timely period.

Finding No. 2

The grantee lacks adequate controls for monitoring subrecipients. Our review of the grantee's and subgrantee's records and discussions disclosed that the grantee provided very little oversight or guidance of a financial nature to the subrecipient. For instance, the grantee did not require the subrecipient to submit invoices in the required format as outlined in Attachment 3 of the subcontract agreement between the grantee and the subrecipient. Attachment 3 states, in part, that "payments by the Department will be made by monthly estimated invoices submitted for anticipated expenses....Each month the Contractor shall submit to the Department an invoice of actual expenditures for the preceding month. The advance payment for that month shall be deducted from the invoice and the balance paid to the vendor." Furthermore, the grantee did not ensure that the subrecipient was not exceeding the cost categories for which the funds were budgeted, including the limit on administrative costs. As a result of the grantee's lack of controls, the grantee was unaware that the subrecipient had incurred administrative costs in excess of the maximum Federal share, the subrecipient did not stay within the approved budget categories, and the subrecipient was submitting invoices on an advance basis which well exceeded the subrecipient's immediate cash needs (refer to finding nos. 2, and 1, respectively in the Independent Auditor's Report on Compliance).

Recommendation

We recommend that the grantee develop and implement policies and procedures to adequately monitor subrecipients on any existing and future grants from Federal agencies.

Inspector General
Corporation for National Service
Washington, DC 20525

Auditee's Comments

The grantee stated that while it concurs with certain recommendations of the audit concerning monitoring of subrecipients, it still does not agree that PACU incurred excess administration costs. The grantee further stated that "PennSERVE instituted more stringent policies for monitoring federal grants in 1995. New personnel were hired to operate the PennSERVE office and were given definitive direction from the new Secretary of the Department of Labor and Industry to review all grants under PennSERVE's purview." As a result of the above, PACU was notified of its noncompliance with several provisions of the grant by letter on May 1, 1995, and PennSERVE's invoicing system was revised in July 1995. Lastly, the grantee indicated that "a quarterly site visit is made to each program which includes a review of their accounting system and financial standing."

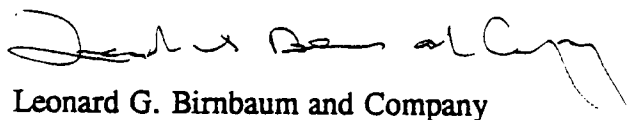
Auditor's Response

Our review of the grantee's and subgrantee's records and discussions during the audit support the auditee's comments that there was more oversight and guidance of a financial nature to the subgrantee prior to end of the grant. Unfortunately, the controls for monitoring subrecipients were not revised soon enough to correct deficiencies which already existed at the subrecipient.

Finding No. 3

The subrecipient lacks adequate controls over their financial management system. For complete details refer to finding no. 1 in the Independent Auditor's Report on Compliance.

We provided a draft of this report to PennSERVE and CNS for comment. PennSERVE's comments (excluding attachments) are included as Appendix 1. We also provided CNS' Office of Grants Management Services copies of the attachments for their consideration during the resolution process. CNS did not provide a response. This report is intended for the information and use of the Corporation's management and its Office of Inspector General and PennSERVE's management and its subrecipient. However, this report is a matter of public record and its distribution is not limited.


Leonard G. Birnbaum and Company

Alexandria, Virginia
August 2, 1996



COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF LABOR AND INDUSTRY
HARRISBURG 17120

OFFICE OF THE SECRETARY

November 8, 1996

Mr. Leslie A. Lieper
Leonard G. Birnbaum and Company
Certified Public Accountants
6285 Franconia Road
Alexandria, Virginia 22310

Dear Mr. Leiper

As requested in your letter of September 26, 1996, enclosed is the PA Department of Labor and Industry's response to the draft audit issued for Grant Number 92NMSTPA0007 awarded to PennSERVE by the Commission on National and Community Service.

Every effort has been made to completely address each finding and questioned cost, listing corrective action taken by the department to improve program effectiveness. However, there is insufficient information in the audit for PennSERVE to answer all of the findings. In order to provide a proper and adequate response to those findings cited, the department had requested a meeting with your organization to obtain additional clarification on certain findings and to explain improvements made to certain aspects of the program which could have reduced the number and /or substance of findings. As you know, this request was not granted. Also, we do not agree with the methodology used in determining the potential impact of some of the findings. Therefore, the department is placed at a disadvantage to respond to those findings cited and accurately defend our position.

Before any final determination is issued, we request a meeting with you to discuss your draft audit report and our response. Please contact Karen S. Fleisher, Executive Director of PennSERVE, at 717-787-1971 with a date for this meeting and any further questions you may have concerning our response to the draft audit report.

Sincerely,

A handwritten signature in black ink, appearing to read "Johnny J. Butler".

Johnny J. Butler
Secretary

PENNSERVE'S RESPONSE
to
FINANCIAL SCHEDULES
and
INDEPENDENT AUDITOR'S REPORT
GRANT AWARD NUMBER 92NMSTPA0007
NOVEMBER 8, 1996

PennSERVE, an agency of the Department of Labor and Industry, Commonwealth of Pennsylvania, was awarded grant #92NMSTPA0007. The grant period covered August 1, 1992, to December 31, 1995. The Pennsylvania Association of Colleges and Universities, PACU, was a subrecipient of the grant award.

SCHEDULE OF QUESTIONED COSTS

1. Living Allowance

The supporting documentation on file at PACU for reimbursement of living allowances does not support the \$223,696.00 figure referenced in the audit report. The documentation supporting the issuance of check number 10582 to the Commonwealth of Pennsylvania for \$219,628.00 reflected salaries of \$204,020.04, social security tax of \$12,572.29 and Medicare tax of \$2,928.86 (see Attachment A-1). This summary sheet was supported by a detailed listing of corpsmembers' names and amount.

The actual expenditures through May 12, 1995, were calculated (see Attachment A-2 through 4). The summary sheets document \$203,979.33 in actual salary. The page two document did not properly reflect the adjustment for \$5,231.25 shown on page one. (Stephanie Michael's salary from grant #92NMSTPA0007 was included in error.) The total revised amount is \$219,583.75 which equals salaries of \$203,979.33 plus social security and Medicare taxes of \$15,604.42.

The difference between the actual expenditure amount of \$219,583.75 and the amount paid to the Commonwealth of \$219,628.00 indicates an overpayment of \$44.25.

PACU is unable to identify the auditor's claim totaling \$223,696.00. Since PACU and PennSERVE were denied an exit conference and were unable to get clarification on this item, only the amounts above can be verified by PACU.

2. Health Insurance (page 15)

At the time that the audit was conducted, the allocation of the \$15,368.00 credit had not been made by PACU. The allocation of the credit has now been recalculated and \$15,367.89 has been applied to reduce the health insurance costs for grant #92NMSTPA0007. The auditor's report identifies \$168,720.00 as incurred health insurance costs, which agrees with the final report of PACU filed with PennSERVE before the receivable of \$15,368.00. It appears a revised report was not filed with PennSERVE to include this receivable. Based on the presentation of the health benefits, the amount should be \$15,368.00 less.

Auditor's Comments

During the audit fieldwork, we were given a summary schedule of the actual expenditures through May 12, 1995. This schedule reflected an amount of \$223,696. Subsequent to the receipt of these comments, we compared the two schedules and confirmed with PACU's bookkeeper that both schedules contained inaccurate information. Based on the revised information, we calculated the difference between the actual expenditures and the amount reimbursed to be \$288 and revised the report accordingly.

Check number 1334 for \$155.00 to the insurance company for corpsmember insurance for the period October 1, 1993, to October 31, 1993, was questioned in the audit as being paid on behalf of a participant of another grant. Since the only grant operated by PACU during that time period was grant #92NMSTPA0007 (the AmeriCorps grant did not begin until August 1994), PACU disagrees that this cost should be questioned.

3. In-Service Education (page 16)

PACU concurs in audit questions of check numbers 1491 (\$550), 1433 (\$167), 1832 (\$366), 1925 (\$63), 10335 (\$266), 10167 (\$52), and 10226 (\$26).

Check number 1614 (\$400) was a cash advance for the field coordinator to purchase lunch at \$5.00 per corpsmember. PACU concurs that no written invoice for the meal is available. However, PACU was responsible for the meals for the corpsmembers. It was more efficient and less costly to advance each member \$5.00 for the meals. This amount is definitely reasonable and is not excessive for the cost of a meal. If requested during the audit, PACU could have provided other documentation reflecting who was in attendance at the conference. Although there was no documentation attached to the voucher, the expense was documented in other ways.

PACU disagrees with the questioning of mileage reimbursements paid with check numbers 1742 (\$15), 1784 (\$34), 1878 (\$43), 1891 (\$21), 10091 (\$31), 10093 (\$14), and 10114 (\$25). OMB CIRCULAR A-122, "Cost Principles for Nonprofit Organizations", states that "travel costs may be charged on an actual basis, on a per diem or mileage basis in lieu of actual costs incurred, or on a combination of the two, provided the method used results in charges consistent with those normally allowed by the organization in its regular operations." The policy of PACU is to pay all employees based on the Internal Revenue Service's standard mileage rate; therefore, the rate used in 1994 was appropriate. This policy is applied consistently to federal as well as nonfederal employees. Also note that the new OMB CIRCULAR A-87, "Cost Principles for State, Local, and Indian Tribal Governments", adopts the same methodology.

4. Operating (page 17)

PACU concurs with the \$2,703 in operating costs questioned in the audit report.

5. Capital (page 17)

PACU concurs with \$528 in capital costs questioned in the audit report.

The individual in question was not included on the list of participants provided to us. Since neither a participant file nor any other records exist for this individual, the questioned amount remains unchanged.

Given that no documentation to support this amount was provided during the audit fieldwork or as an attachment to these comments, the questioned amount remains unchanged.

Even though PACU's written policy states that corps members will be reimbursed mileage at a rate of \$0.20 per mile, their actions indicate a policy of reimbursing mileage at a rate of \$0.29 per mile. We have reduced the questioned amount accordingly.

6. Other (page 17)

PACU concurs that funds should have been allocated between the two programs for payment to Mary Francis McLaughlin.

7. Administration (page 17)

The audit questions \$247,540 in salary and \$74,867 in payroll taxes and benefits stating that these should be administrative costs. These costs represent 100 percent of the salaries and benefits paid to certain staff members hired under grant #92NMSTPA0007 specifically to operate the program and, therefore, do not benefit other programs and are not "Administrative" costs. The amounts were paid in accordance with federal regulations and policy letters and guidelines from the Commission on National and Community Service. The federal government should not permit the reclassification of certain grant costs in a manner contrary to federal regulations or retroactively change these rules after the conclusion of the grant period. PennSERVE and PACU strongly disagree with this finding in its entirety.

Documentation has been provided which shows that these were correctly classified as "Other" costs rather than "Administration" costs. In this documentation it is clearly stated why the reclassified costs should remain "Other" costs: the expenditures are directly associated with the specifics of the program and not to contribute to the general program objective. Included in this document as Attachment 3 are definitions from the regulations governing this grant and other supporting documents covering administrative costs. It is evident from the documentation attached to this audit report response that the regulations support the position PACU took regarding what were administrative costs. References have also been attached from AmeriCorps regulations and literature because the new regulations provide further support and clarification on the administrative cost issue. This documentation also includes letters and guidelines from the Corporation stating that this classification of expenditures is appropriate. It appears clear to PennSERVE and PACU that these costs are appropriately classified as "Other" costs.

The five percent "Administration" limit should apply only to costs incurred by PACU in providing oversight for overall administration, not to costs involved in direct program implementation by staff hired specifically to perform duties required under grant #92NMSTPA0007. This interpretation is clearly articulated in Regulations at 45 CFR Section 2500.2(2) and explained by Corporation guidelines and letters.

PACU is a small, not-for-profit organization with four and one-half staff positions and a modest annual operating budget

It is clear that PennSERVE and PACU disagree with our interpretation of the terms and conditions of the grant. We have reviewed the comments and are not persuaded that our interpretation is incorrect. Accordingly, this is a matter to be resolved by the Office of Grants Management Services.

generated by members' dues. PACU agreed to accept the grant and to provide administrative oversight for grant #92NMSTPA0007 and based on the clear understanding with the Commission for National and Community Service that the salaries, benefits and other support costs required for all of the staff members who were hired to handle the day-to-day management of this grant would be paid from the overall grant funds, not from the five percent administrative overhead funds that were clearly designated for PACU. Under no circumstances would PACU have accepted this grant without the clear understanding from the Commission for National and Community Service that this was the case.

PACU's position on this issue is supported by formal documentation provided. All of the staff members hired specifically to operate grant #92NMSTPA0007 were hired only for that purpose and their employment has been terminated now that the grant period has ended. The annual budgets submitted by PACU to the Corporation were approved by the Corporation.

The responsibility of the existing PACU staff was to provide administrative support and guidance, including decisions involving funds, personnel, internal budgeting, office procedures and financial control of all income and expenditures. In addition, the existing PACU organization incurred legal, accounting, insurance, and surety fees associated with the administration of the program. PACU processed all program employees' payroll and benefits and provided the use of PACU's conference room, copying equipment, and other equipment as needed. The five percent administrative cost was paid to PACU to cover these costs.

Also, \$50,799 was reclassified in the audit from "Evaluation" to "Administration". Regulation at 45 CFR Section 2500.2(2) clearly states that non-administrative costs include: "evaluation of the program as required by the terms and conditions of the grant." These expenses were not for administration. Further discussion on this item will be covered in our response to the section of the audit titled "Schedule of Reclassified Costs".

8. Excess Claimed Costs Over Incurred Costs (page 19)

The audit identifies \$264,105.00 in excess claimed costs over incurred costs for post service benefits. These costs should not be considered questioned costs but are out of period costs. The financial status reports were prepared on a accrual basis not on a cash basis in accordance with generally accepted accounting principles. The final financial status report included post service benefits which are reasonable, allowable and properly allocable.

We do not feel that any action should have been taken until CNS had made a decision regarding this matter since Amendment No. 3, dated September 27, 1995, states that "Post-Service Benefit funds must remain in the custody of the U.S. Government while remaining available to you for payment."

PennSERVE sought clarification on how post service benefit costs should be handled at the end of the grant. The Corporation for National Service in a letter to PennSERVE dated February 8, 1996, (see Attachment C) states: "Whether all funds may be drawn down and held in a state account is a matter presently under discussion." In the absence of further guidance from the Corporation, PennSERVE instructed PACU to draw down all necessary post service benefit funds so those funds would not be lost by the program.

From August 1, 1996, through October 15, 1996, PACU has paid out \$43,963.21 (50% from federal and 50% from match funds) in post service benefit allowances. PACU currently has \$242,123.39 of federal funds for the post service benefit allowances and continues to administer this segment of the program. All federal post service benefit funds are maintained in a segregated account by PACU and can be returned to the Corporation for National Service.

Should the Corporation elect to employ the auditors' recommendation to this finding, PennSERVE is agreeable, in fact, all parties concerned are agreeable to the repayment of that amount referenced in the finding. However, PennSERVE does not agree that this finding should be considered an audit exception since PennSERVE did consult the Corporation, and consider their recommendations on this subject in an effort to insure propriety did not become an issue.

Of the remaining \$156,197.00 costs questioned as excess, \$124,880.00 is in the "Evaluation" category. Regulations at 45 CFR Section 2500.2(2) states that non-administrative costs include evaluations. Of the total \$35,571.00 in salary and benefits was paid to Mr. Aaron Hess who was employed under grant #92NMSTPA0007 from January through October of 1993 specifically to perform all evaluation requirements of the program. This included complying with the requirements outlined in the "Evaluation Systems Manual". His sole job responsibilities were to comply with the evaluation reporting requirements of grant #92NMSTPA0007 and, therefore, his \$35,571.00 salary and benefits was properly spent as part of the evaluation budget. After his departure in October 1993, the evaluation function was performed by Dr. Carl Fertman as an outside contractor. See item 2, "Schedule of Reclassified Costs", for discussion of \$57,299.00 in additional evaluation costs claimed. The total evaluation costs incurred were \$92,870.00. The excess costs over incurred costs for this category would then be \$32,010.00.

Finally, we are unable to accurately respond to the remainder of the amount documented as excess costs. The audit does not contain sufficient information for PennSERVE to reply. Therefore, additional information will be necessary to determine whether to accept this finding as a valid finding and if

The amount of \$420,302 identified as excess claimed over incurred costs is a function of the amount reflected on the Financial Status Report (FSR) as of the quarter ended December 31, 1995, (\$4,350,331) and the actual amount incurred based PennSERVE and PACU's records (\$3,930,331). We were able to identify that of this difference \$264,105 was associated with post service benefits. We were not able to identify the balance. It is the responsibility of PACU or PennSERVE to explain why the amount on the FSR does not agree with the amount reflected in their records. It is not the responsibility of the CNS OIG to do so.

PennSERVE should agree with the costs associated with this finding.

9. Excess Advanced Funds Over Claimed Costs (page 19)

The Commonwealth has issued a refund check in the amount of \$1,292.00.

SCHEDULE OF RECLASSIFIED COSTS

1. Participant Support Costs - Full-Time (page 20)

PACU disagrees with the reclassification from "In-Service Training" to "Administration". It may be appropriate to reclassify these costs as "Operations" or "Other", but it is not appropriate to reclassify them to "Administration". These costs clearly comply with federal regulations and policy guidelines and letters from the Commission on National and Community Service. The federal government should not permit the reclassification of grant costs in a manner contrary to federal regulations or retroactively change these rules after the conclusion of the grant period.

Included in this document as Attachment B are definitions from the regulations governing this grant and other supporting documents covering administrative costs. It is evident from the documentation attached to this audit report response that the regulations support PACU's position regarding what can be included as administrative costs and what can be included as non-administrative costs. References have also been attached from AmeriCorps regulations and literature because the new regulations provide further support and clarification on the administrative cost issue.

2. Evaluation (page 20)

PACU concurs that check numbers 10784, 10857 and 10936 (totaling \$5,000) should be reclassified from "Evaluation" to "Other" and that check number 11033 (\$1,500) should be reclassified from "Evaluation" to "Operating". However, PACU disagrees that the remaining \$50,799 should be reclassified from "Evaluation" to "Administration" for the following reasons:

Dr. Carl Fertman was paid \$43,200 from grant #92NMSTPA0007 as an outside contractor for the specific purpose of performing the evaluation requirements specified by the grant. A copy of Dr. Fertman's contract is included in this audit response as Attachment D. This cost was approved as "Evaluation" costs in PACU's budget. Dr. Fertman also participated

It is clear that PennSERVE and PACU disagree with our interpretation of the terms and conditions of the grant. We have reviewed the comments and are not persuaded that our interpretation is incorrect. Accordingly, this is a matter to be resolved by the Office of Grants Management Services.

It is clear that PennSERVE and PACU disagree with our interpretation of the terms and conditions of the grant. We have reviewed the comments and are not persuaded that our interpretation is incorrect. Accordingly, this is a matter to be resolved by the Office of Grants Management Services.

in a GAO study of the evaluation process, which was required to meet the evaluation requirements of this grant.

Under the grant, \$7,500 was paid to temporary employees hired to develop manuals and documents required for the corpsmembers and should be reclassified as either "Operating" or "Other". The \$99 expenditure for materials should also be reclassified as "Operating" or "Other". The total of these two expenditures of \$7,599 was not for "Administration" as stated in the audit and, therefore, PACU disagrees with the reclassification proposed in the audit report. Included in this document as Attachment B are definitions from the regulations governing this grant and other supporting documents covering administrative costs. It is evident from the documentation attached to this audit report response that the intent of the regulations supports the position PACU took regarding what were administrative costs. References have also been attached from AmeriCorps regulations and literature because the new regulations provide further support and clarification on the administrative cost issue.

These amounts were paid in accordance with federal regulations and policy letters and guidelines from the Commission on National and Community Service. The federal government should not permit the reclassification of grant costs in a manner contrary to federal regulations or retroactively change these rules after the conclusion of the grant period. Regulation at 45 CFR Section 2500.2(2) clearly states that non-administrative costs include: "evaluation of the program as required by the terms and conditions of the grant."

3. Other (page 20)

PACU disagrees with the reclassification from "Other" to "Administration". These expenses were properly classified as "Other". Attachment B includes definitions from the regulations governing this grant and other supporting documents covering administrative costs.

The amounts were paid in accordance with federal regulations and policy letters and guidelines from the Commission on National and Community Service. The federal government should not permit the reclassification of grant costs in a manner contrary to federal regulations or retroactively change these rules after the conclusion of the grant period.

It is clear that PennSERVE and PACU disagree with our interpretation of the terms and conditions of the grant. We have reviewed the comments and are not persuaded that our interpretation is incorrect. Accordingly, this is a matter to be resolved by the Office of Grants Management Services.

COMPLIANCE

Finding No. 1 (page 24)

PennSERVE notified PACU by letter on May 1, 1995, that it was in noncompliance with several provisions of grant #92NMSTPA0007. Included in this document as Attachment E is a copy of this letter.

When Problems in PACU's financial management systems of grant #92NMSTPA0007 became apparent to the President of PACU, personnel changes were made in the staff of the grant, including the termination of the employment of the grant fiscal officer. Before this employee was terminated, steps were taken to correct the problems with the financial managements systems and then to document the problems.

A bookkeeper was hired on a contractual basis to help correct the concerns that had been identified and members of the PACU staff increased the amount of time that was already devoted to the oversight of the financial operations of the grant.

The following steps are being taken to ensure that PACU's financial management system complies with the seven items listed on page 24 of the draft audit report:

- (1) The bookkeeper is in the process of insuring that all records are accurate, complete and up to date regarding the operations of this now closed program.
- (2) The bookkeeper is in the process of insuring that all records are accurate, complete and up to date regarding the operations of this now closed program.
- (3) This program is now closed. The remaining post service benefits account has been segregated from all other accounts and is maintained by PACU to insure compliance of the benefits.
- (4) The bookkeeper is in the process of insuring that all records are accurate, complete and up to date regarding the operations of this now closed program.
- (5) This program is now closed.
- (6) The cost allocation plan was developed after the closure of this program.
- (7) The bookkeeper is in the process of insuring that all records are accurate, complete and up to date regarding the operations of this now closed program.

Finding No. 2 (page 25)

PennSERVE and PACU strongly disagree with this finding. Documentation provided as Attachment B clearly supports PennSERVE's and PACU's understanding that the five percent limit on administrative costs apply only to the general administrative oversight provided by PACU, not to the costs associated with program staff hired specifically to operate the provisions of grant #92NMSTPA0007. The amounts were paid in accordance with federal regulations and policy letters and guidelines from the Commission on National and Community Service. The federal government should not permit the reclassification of certain grant costs in a manner contrary to federal regulations or retroactively change these rules after the conclusion of the grant period.

INTERNAL CONTROL STRUCTURE

Finding No. 1 (page 29)

The bookkeeper at PACU and the former fiscal officer prepared checks for the signature of the President of PACU. At no time did either the bookkeeper or fiscal officer sign checks. As a small organization, PACU does not have sufficient personnel to distribute these duties further. PACU is satisfied that the "checks and balances" that are part of their policies are sufficient.

Finding No. 2 (page 30)

PennSERVE instituted more stringent policies for monitoring federal grants in 1995. New personnel were hired to operate the PennSERVE office and were given definitive direction from the new Secretary of the Department of Labor and Industry to review all grants under PennSERVE's purview. PennSERVE notified PACU by letter on May 1, 1995, that it was in noncompliance with several provisions of grant #92NMSTPA0007. Included in this report is a copy of this letter as Attachment E. In July 1995, PennSERVE changed its invoice system. Invoicing for all other federal programs is done on a reimbursement basis. Programs must invoice by budget category (see Attachment F). After an invoice is processed, PennSERVE sends to each program a budget breakdown by category indicating how much has been drawn down in each category and the amount remaining. In addition, a quarterly site visit is made to each program which includes a review of their accounting system and financial standing.

Although we concur with certain recommendations of the audit concerning monitoring of subrecipients, we still do not agree that PACU incurred excess "Administration" costs.

Finding No.3 (page 30)

PACU's financial management systems was discussed in the response to Finding No. 1, "Compliance".