

**COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF LABOR AND
WORKFORCE DEVELOPMENT**

**AUDIT OF
DIRECT AND INDIRECT COSTS CHARGED TO
U.S. DEPARTMENT OF LABOR GRANTS
DURING THE PERIOD
JULY 1, 1998 THROUGH JUNE 30, 2001**

Final Report No: 03-02-001-03-315

Date Issued: March 29, 2002

**TICHENOR & ASSOCIATES, LLP
CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS**

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

**Acting Deputy Inspector General For Audit
U.S. Department of Labor**

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ACRONYMS AND GLOSSARY

CFR	Code of Federal Regulations
ES	Employment Services
DET	DLWD's Division of Employment and Training
DLWD	Massachusetts Department of Labor and Workforce Development
DOL	U.S. Department of Labor
DOS	DLWD's Division of Occupational Safety
JTPA	Job Training Partnership Act
OIG	U.S. Department of Labor, Office of Inspector General
OMB	U.S. Office of Management and Budget
SFY	State Fiscal Year
UI	Unemployment Insurance
WIA	Workforce Investment Act

GLOSSARY

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

EXECUTIVE SUMMARY

Tichenor & Associates, LLP, Certified Public Accountants and Management Consultants, under contract to the U.S. Department of Labor (DOL), Office of Inspector General (OIG), conducted an audit of direct and indirect costs charged to DOL grants by the Commonwealth of Massachusetts' Department of Labor and Workforce Development (DLWD).

The audit focused on: (1) indirect cost rate agreements between DOL and DLWD's Division of Employment and Training (DET) and Division of Occupational Safety (DOS); and (2) direct charges made by DLWD to Job Training Partnership Act (JTPA) and Workforce Investment Act (WIA) grant programs operated by the Commonwealth Corporation. The audit covered costs charged to these programs for State fiscal years (SFYs) 1999, 2000, and 2001.

Our audit disclosed that about \$1.34 million of the direct and indirect costs claimed and recovered by DLWD on DOL grants for SFYs 1999, 2000, and 2001, were unallowable because they were not "adequately documented," and were based on estimated rather than actual costs, contrary to Federal cost principles. Specifically, DLWD personnel, whose salary costs were charged both as direct and indirect costs to DOL grants, had failed to prepare the required personnel activity (time distribution) reports, and their salaries were charged directly to projects or to an indirect cost pool based on pre-established budget estimates. Accordingly, we have questioned a total of \$1.34 million in DLWD direct and indirect charges to DOL grants.

OMB Circular A-87, Attachment A, section C, states that "To be allowable under Federal awards, costs must . . . Be adequately documented." In addition, OMB Circular A-87, Attachment B, paragraph 11.h lists very specific documentation criteria which must be met in order to support salaries and wages, whether treated as direct or indirect costs (including all directly-associated costs such as fringe benefits). When employees work on more than one cost objective and/or indirect cost activity, the salary costs must be supported by personnel activity reports which must reflect an after-the-fact distribution of the actual activity of each employee. Further, the Circular states that budget estimates do not qualify as support for charges to Federal awards.

We recommend that DLWD refund to DOL the questioned indirect and direct costs and adjust its billings to DOL for SFY 2002 to preclude further overrecoveries of unsupported and unallowable costs. Additionally, DLWD must develop and implement a time distribution system for all Executive Office personnel who are involved in charging both direct and indirect costs to DOL grants. Finally, we recommend that DLWD develop and implement written internal control policies and procedures, required by 29 CFR § 97.20(b)(5), to ensure that all direct and indirect costs charged to DOL grants fully comply with the reasonableness, allocability, and allowability criteria mandated by OMB Circular A-87.

Auditee's Response

In its response to our draft report, DLWD conceded that it had not maintained personnel activity reports to support its direct and indirect costs charged to DOL grants in SFYs 1999, 2000 and 2001, as required by OMB Circular A-87, because it was not aware of this requirement prior to our audit. However, DLWD believes that the costs questioned were reasonable, and would be working with DOL's Regional Director and his staff to confirm with them that these costs were "reasonable."

DLWD indicated that it planned to develop for future use a time distribution system for Executive Office personnel who are involved in charging direct and indirect costs to DOL grants. In addition, it plans to develop internal control policies to ensure that all direct and indirect costs charged to DOL grants comply with OMB Circular A-87.

Auditor's Conclusion

DLWD has readily admitted, both in our exit conference and in its written response, that it had not maintained the required personnel activity reports mandated by OMB Circular A-87 which, in turn, must meet very strict documentation requirements in order for personnel services costs (and all directly associated costs) to be allowable. The fact that DLWD may not have been aware of these requirements does not make the questioned costs allowable, or otherwise ameliorate the findings. The Federal cost principles are very clear – to be **allowable**, costs must be "adequately documented." In the case of personnel services costs, OMB Circular A-87 spells out very detailed criteria that must be met in order for such costs to be considered "adequately documented." Therefore, we are making no changes in this finding or its related conclusions and recommendations.

INTRODUCTION

BACKGROUND

DOL's Employment Services (ES) and Unemployment Insurance (UI) grants are administered by DLWD's Division of Employment and Training (DET). Occupational safety grants are administered by DLWD's Division of Occupational Safety (DOS). And, finally, the Job Training Partnership Act (JTPA) and the Workforce Investment Act (WIA) grants are administered by the Commonwealth Corporation, a quasi-public agency, under the direct authority of DLWD.

Expenditures on DOL grants administered by DLWD totaled \$177,481,475 for SFYs 1999, 2000, and 2001.

OBJECTIVES AND SCOPE

The initial objective of this engagement was to conduct a "risk assessment" to determine whether direct and indirect costs charged to the UI program for SFY 2000 were reasonable, allocable, and otherwise allowable under the Federal cost principles set forth in U.S. Office of Management and Budget (OMB) Circular A-87 — *Cost Principles for State, Local and Indian Tribal Governments*, and the A-87 implementation guidelines set forth in ASMB C-10 — *Cost Principles and Procedures for Developing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*. The engagement objective further provided that, depending on the results of our "risk assessment," the scope could be expanded to include additional years and other DOL grant programs.

Based on the results of our "risk assessment," and in consultation with the DOL Task Monitor on this engagement, we expanded our scope to include additional years and other DOL grants. The audit focused on: (1) the indirect cost rate agreements between DOL and DLWD's DET and DOS; and (2) the direct charges made by DLWD to JTPA and WIA grant programs operated by the Commonwealth Corporation. The audit covered costs charged to these programs for SFYs 1999, 2000, and 2001.

The audit fieldwork was conducted from August 29, 2001, through September 11, 2001. A Statement of Facts summarizing the results of the audit was submitted to DLWD and Office of the Comptroller officials on September 10, 2001; however, our scheduled exit conference was not held because of the September 11 terrorist incidents. Subsequently, DLWD and Office of the Comptroller officials informed us that they preferred to not comment on the Statement of Facts, but would reserve their formal comments for our draft report.

This engagement was performed in accordance with auditing standards established by the American Institute of Certified Public Accountants, and with the *Government Auditing Standards* issued by the Comptroller General of the United States, except that the scope of our

engagement did not include expressing a formal written opinion on the reasonableness and allowability of the total claimed costs by DLWD, its system of internal controls, or its compliance with laws and regulations applicable to all Federal grants/contracts.

FEDERAL COST REIMBURSEMENT PRINCIPLES

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

General Principles for Determining Allowable Costs

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

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

- a. Be necessary and reasonable for proper and efficient performance and administration of Federal awards.
- b. Be allocable to Federal awards under the Circular (e.g., on the basis of relative benefits received).
- c. Be authorized (or not prohibited) under state or local laws and regulations.
- d. Conform to any limitations or exclusions set forth in these principles, Federal laws, the terms and conditions of the Federal award, or any other governing regulations as to types and/or amounts of cost items.
- e. Be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities/programs of the governmental unit.
- f. Be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost.

Similarly, a cost may not be allocated to a Federal award as an indirect cost if any other cost incurred for the same purpose in like circumstances has been charged to the award as a direct cost.

- g. Except as otherwise provided for in the Circular, costs must be determined in accordance with generally accepted accounting principles.
- h. Not be included as a cost or used to meet cost sharing or matching requirements of any other Federal award in either the current or a prior period, except as specifically provided by Federal law or regulation.
- i. Be the net of all applicable credits.
- j. Be adequately documented.

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

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

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

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

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

Specific Principles for Determining Allowability of Selected Items of Cost

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

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

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

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

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

- (a) They must reflect an after-the-fact distribution of the actual activity of each employee,
- (b) They must account for the total activity for which each employee is compensated,

- (c) They must be prepared at least monthly and must coincide with one or more pay periods, and
- (d) They must be signed by the employee.
- (e) Budget estimates or other distribution percentages determined before the services are performed do not qualify as support for charges to Federal awards

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

Our audit disclosed that about \$1.34 million of the direct and indirect costs claimed and recovered by DLWD on DOL grants for SFYs 1999, 2000, and 2001, were unallowable because they were not adequately documented. The claimed costs were based on estimated rather than actual costs, contrary to Federal cost principles. Specifically, we found that certain DLWD personnel, whose salary costs were charged both as direct and indirect costs to DOL grants, had failed to prepare personnel activity (time distribution) reports required by OMB Circular A-87. Further, the distribution of their salary costs and “directly associated” costs was charged directly to projects or to an indirect cost pool based on budget estimates rather than actual time as required by A-87.

Accordingly, we have questioned a total of \$1.34 million in DLWD direct and indirect charges to DOL grants in SFYs 1999, 2000, and 2001 because the costs were not supported as required by OMB Circular A-87, as follows:

1. Certain personnel within the DLWD Executive Office, who worked on both direct and indirect cost objectives, failed to maintain personnel activity reports showing the actual time spent on each of the cost objectives. Based on available data, we determined that about \$944,430 in unsupported salaries and “directly-associated” non-salary costs were included in DLWD’s indirect cost pools for SFYs 1999, 2000, and 2001, of which \$755,544 (or 80 percent) were allocated to DOL grants administered by DLWD’s DET and DOS.
2. In addition, a total of about \$585,000 in unsupported salaries of the above DLWD Executive Office personnel, plus “directly-associated” non-salary costs, was also charged as direct costs to the DOL JTPA/WIA grants administered by the Commonwealth Corporation (a quasi-public corporation) which is under the general supervision of DLWD.

Further, we believe that DOL grants were also charged for unsupported/estimated costs during SFY 2002 because the conditions disclosed by our audit had not changed as of the completion of our fieldwork in September 2001.

The details of our findings are presented in the following pages.

FINDING 1. Unsupported Departmental Salaries and Associated Costs Charged as Indirect Costs to DOL Grants Administered by DET and DOS

Our audit disclosed that some of the departmental salary costs and “directly associated” non-salary expenditures included in the DET and DOS indirect cost rate proposals were unallowable because they were not adequately documented, and were based on estimated rather than actual time spent on indirect functions. We determined that \$755,544 of these unallowable indirect costs were allocated to DOL grants.

As previously discussed in this report, the terms and conditions of DOL grants awarded to DLWD require that it comply with the cost reimbursement principles set forth in OMB Circular A-87. OMB Circular A-87, Attachment A, section C, states that “To be allowable under Federal awards, costs must Be adequately documented.” In addition, OMB Circular A-87, Attachment B, paragraph 11.h, lists very specific documentation criteria which must be met in order to support salaries and wages, whether treated as direct or indirect costs (including all directly-associated costs such as fringe benefits). When employees work on more than one cost objective and/or indirect cost activity, the salary costs must be supported by personnel activity reports which must reflect an after-the-fact distribution of the actual activity of each employee. Further, the Circular states that budget estimates do not qualify as support for charges to Federal awards.

The DET and DOS indirect cost proposals for SFYs 1999 through 2001 included the following DLWD Executive Office costs (based on actual 1997 costs), plus the non-salary expenditures and Statewide allocated costs which are directly attributable to and accompany the salary and wages.

1997 DLWD Executive Office Salaries and Associated Indirect Costs

Salary and Wages	\$235,043
Non-salary Expenditures	<u>88,395</u>
Total Direct Costs	\$323,438
Statewide allocated Costs	<u>201,245</u>
Total Indirect Costs	<u>\$524,683</u>

The \$524,683 was allocated to eight programs operated by DLWD, including the DOL grants administered by DET and DOS. DET and DOS operate only DOL programs. We found that DET programs were allocated 76.99 percent and the DOS programs were allocated 2.99 percent of the above costs. Thus, the total costs charged against DOL-funded programs amounted to about 80 percent of total departmental indirect costs.

We found that \$140,458 of the \$235,043 salaries and wages were applicable to those DLWD officials whose salaries and wages were charged as both direct and indirect costs, but who failed to prepare the required personnel activity reports to support the actual time spent on each of the direct and indirect activities. DLWD officials told us that they were not aware of this requirement. Instead, they simply estimated the amount of time to be charged directly to the

JTPA/WIA programs administered by the Commonwealth Corporation; the remainder of their time was charged to the indirect cost pool. We confirmed that these “estimates” were not periodically adjusted to reflect the actual effort. Likewise, the effort of the Director, DLWD, was only charged against the indirect cost pool, although his responsibilities clearly required some effort in managing the Commonwealth Corporation which administered the JTPA/WIA programs. His efforts were also unsupported as he did not prepare the required personnel activity reports.

Using the relationship between the unsupported salary expenditures of \$140,458 to total salaries of \$235,752 (60 percent), we found that \$314,810 per year ($\$524,683 \times 60\%$) of DLWD’s indirect costs were not adequately supported. Consequently, during the 3-year period of our audit ending June 30, 2001, the DLWD cost pool for allocation to the eight programs contained \$944,430 of questioned costs. Since 80 percent of the costs in the DLWD indirect cost pool were charged to DET and DOS programs, DOL grants were charged with \$755,544 ($\$944,430 \times 80\%$) in unsupported indirect costs.

FINDING 2. Unsupported Departmental Salaries and Associated Costs Charged as Direct Costs to JTPA and WIA Programs Administered by the Commonwealth Corporation

As stated earlier, a portion of the salary and wages of certain officials of the DLWD Executive Office were charged directly to JTPA and WIA programs, administered by the Commonwealth Corporation, without being supported by personnel activity reports as required by OMB Circular A-87. In addition, these costs were based on budget estimates rather than actual time spent. We determined that the unsupported salaries of these officials, and all directly-associated costs, charged to these programs totaled \$585,000 in SFYs 1999 through 2001.

DLWD officials told us that they were unaware of the requirement of OMB Circular A-87 regarding the need for formal time distribution sheets. They said they believed it was more beneficial to use the estimated charges, rather than having to resort to more complicated time reporting systems. In addition, DLWD officials told us that, in their opinion, more accurate time reporting would mean added charges against the JTPA and WIA grants.

This latter statement suggests that the amounts direct charged to the JTPA and WIA grants by DLWD were not determined on the basis of “relative benefits received” as required by OMB Circular A-87. Specifically, OMB Circular A-87, Attachment A, paragraph C.3.a states that “A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.” [Underscoring added.] The statement also tends to indicate that DLWD may be intentionally limiting the amount of departmental overhead charged to the JTPA and WIA grants in order to stay within a 5-percent statutory limitation on the amount of State administrative costs which may be charged to these grants. As a result, departmental overhead costs properly allocable to the JTPA/WIA grants in excess of the 5-percent statutory limitation (which would otherwise have to be paid for with State funds) are being shifted to other DOL grants which are not subject to a statutory limitation on the amount of State administrative costs for which DLWD may be reimbursed.

We believe the previous statement by DLWD officials tends to confirm that: (1) they do not have an adequate working knowledge of some of the more critical cost principles set forth in OMB Circular A-87; and/or (2) they may be trying to avoid having to use State funds to cover State administrative costs in excess of the statutory limitation.

* * * * *

Conclusions

For the 3-year period covered by our audit, we found that \$1.34 million in unallowable salaries and directly-associated costs were charged as direct and indirect costs to various DOL grants. These costs are unallowable because certain department-level officials who charged their time to both direct and indirect cost objectives failed to prepare personnel activity reports which meet very specific and detailed documentation standards mandated by OMB Circular A-87. In addition, these costs are also unallowable because they were based on “budget estimates,” rather than the mandatory “after-the-fact distribution of the actual activity of each employee.” [Note: We verified that these “estimates” were never adjusted to “actual” costs; in fact, DLWD could not have made such an adjustment because there was no record of the actual time spent on the various cost objectives.] Accordingly, we question the \$1.34 million in unallowable costs charged to DOL grants for the 3-year period ended June 30, 2001.

Recommendations:

We recommend that the Department of Labor:

1. Direct DLWD to refund \$755,544 in unsupported indirect costs questioned in this report.
2. Direct DLWD to refund \$585,000 in unsupported departmental salaries and associated costs charged as direct costs to JTPA and WIA programs.
3. Direct DLWD to adjust its billings to DOL for SFY 2002 direct and indirect costs to preclude further overrecoveries of unsupported and unallowable costs.
4. Direct DLWD to develop and implement a time-distribution system for all DLWD Executive Office personnel who are involved in charging both direct and indirect costs to DOL grants, which meet the criteria set forth in OMB Circular A-87, Attachment B, paragraph 11.h.
5. Direct DLWD to develop and implement written internal control policies and procedures to ensure that all direct and indirect costs charged to DOL grants fully comply with the reasonableness, allocability, and allowability criteria mandated by OMB Circular A-87.

* * * * *

Auditee's Response

In its response dated March 20, 2002, the Director of DLWD stated, in part, that:

The audit questions a total of \$1.34 million of the direct and indirect costs claimed and recovered by DLWD on DOL grants for SFYs 1999, 2000, and 2001. I believe that these costs were "reasonable" and my staff and I will be working closely with USDOL's Regional Director and his staff to confirm with them that these costs were "reasonable".

DLWD concedes that actual personnel activity reports showing the actual time spent on JTPA/WIA activities are not available. Prior to this audit, DLWD was unaware that personnel activity reports are required under the federal regulations for employees that are paid from multiple sources. However, we do maintain a weekly schedule (updated daily) that includes all WIA meetings, events etc. that are attended by DLWD staff. We also can produce fiscal reports indicating the number of fiscal transactions that have executed by DLWD fiscal staff. In addition, DLWD staff plays an intricate part in the production of the WEA Annual Report, WIA Policy and Informational Issuances; WIA contract negotiations and the State plan that is required under the grant.

DLWD agrees to develop for use from this point forward a time distribution system for Executive Office personnel who are involved in charging direct and indirect costs to USDOL grants. DLWD also agrees to develop internal control policies and procedures to ensure that all direct and indirect costs charged to USDOL grants comply with OMB Circular A-87.

A copy of DLWD's written response to a draft of this report is included in its entirety in an appendix to this report.

Auditor's Conclusion

DLWD readily admits that it did not maintain the required personnel activity reports mandated by OMB Circular A-87 which, in turn, must meet very strict documentation requirements in order for personnel services costs (and all directly associated costs) to be allowable. The fact that DLWD may not have been aware of these requirements does not make the questioned costs allowable, or otherwise ameliorate the findings. The Federal cost principles are very clear – to be **allowable**, costs must be "*adequately documented*." In the case of personnel services costs, OMB Circular A-87 spells out very detailed criteria that must be met in order for such costs to be considered "*adequately documented*."

In summary, DLWD's written response did not provide any new or compelling evidence which would warrant any change in these findings, or the related conclusions and recommendations.

AUDITEE'S RESPONSE



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March 20, 2002

Mr. Michael T. Hill, Regional Inspector General
For Audit
Office of Inspector General
The Wanamaker Building
100 Penn Square East, Suite 602-B
Philadelphia, PA 19107

RE: Draft Audit Report No: 03-02-001-03-315

Dear Mr. Hill:

As you are aware, on behalf of the U.S. Department of Labor (USDOL), Office of Inspector General, Tichenor Associates, LLP recently conducted a limited scope audit of indirect costs charged to USDOL grants by the Department of Labor and Workforce Development (DLWD). The purpose of the audit was to review indirect costs charged to USDOL grants by DLWD. The audit questions a total of \$1.34 million of the direct and indirect costs claimed and recovered by DLWD on DOL grants for SFYs 1999, 2000, and 2001. I believe that these costs were "reasonable" and my staff and I will be working closely with USDOL's Regional Director and his staff to confirm with them that these costs were "reasonable". The findings were based on the following conclusions made by the auditors:

Auditor's Finding #1

1. Certain personnel within the DLWD Executive Office, who worked on both direct and indirect cost objectives, failed to maintain personnel activity reports showing the actual time spent on each of the cost objectives. Based on available data, we determined that about \$944,430 in unsupported salaries and "directly-associated" non-salary costs were included in DLWD's indirect cost pools for SFYs 1999, 2000, 2001, or which \$755,544 (or 80 percent) were allocated to DOL grants administered by DLWD's DET and DOS.



Auditor's Finding #2

2. In addition, a total of \$585,000 in unsupported salaries of the above DLWD Executive Office personnel, plus "directly-associated" non-salary costs, was also charged as direct costs to the DOL JTPA/WIA grants administered by the Commonwealth Corporation (a quasi-public corporation) which is under the general supervision of DLWD.

DLWD's Response to Findings #1 and #2

DLWD concedes that actual personnel activity reports showing the actual time spent on JTPA/WIA activities are not available. Prior to this audit, DLWD was unaware that personnel activity reports are required under the federal regulations for employees that are paid from multiple sources. However, we do maintain a weekly schedule (updated daily) that includes all WIA meetings, events etc. that are attended by DLWD staff. We also can produce fiscal reports indicating the number of fiscal transactions that have been executed by DLWD fiscal staff. In addition, DLWD staff plays an intricate part in the production of the WIA Annual Report, WIA Policy and Informational Issuances; WIA contract negotiations and the State plan that is required under the grant.

DLWD agrees to develop for use from this point forward a time distribution system for Executive Office personnel who are involved in charging direct and indirect costs to USDOL grants. DLWD also agrees to develop internal control policies and procedures to ensure that all direct and indirect costs charged to USDOL grants comply with OMB Circular A-87.

I am committed to ensuring that DLWD continues to follow all rules and regulations governing the receipt of federal funds. I am equally committed to doing our best to avoid further erosion of our already limited resources to assist employers and employees across the Commonwealth of Massachusetts.

If you have any questions, or need any additional information, please contact Janice Tatarka, Chief of Staff or Joan Lenihan, Chief Financial Officer at 617-727-6573.

Sincerely,


Angelo Buonopane

cc: Janice Tatarka
Joan Lenihan