STATE OF TEXAS

AUDIT OF DIRECT AND INDIRECT COSTS

CHARGED TO

U.S. DOL GRANTS ADMINISTERED BY

TEXAS WORKFORCE COMMISSION

SEPTEMBER 1, 1997, THROUGH AUGUST 31, 2001

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.

Elliot P. Lewis

Assistant Inspector General for Audit
U.S. Department of Labor

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ACRONYMS

DOL	U.S. Department of Labor
ETA	U.S. Department of Labor, Employment and Training Administration
FCAT	Financial Cost Allocation Table
FY	Fiscal Year
HHS	U.S. Department of Health and Human Services
OIG	U.S. Department of Labor, Office of Inspector General
OMB	U.S. Office of Management and Budget
SFY	State Fiscal Year (September 1 to August 31)
TWC	Texas Workforce Commission
UI	Unemployment Insurance

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INDEPENDENT ACCOUNTANT'S REPORT ON AUDIT

Tichenor & Associates, LLP, 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 awarded to the Texas Workforce Commission (TWC) for State Fiscal Years (SFYs) 1998, 1999, 2000, and 2001. The objective was to determine whether such costs were reasonable, allowable, and allocable under the Federal cost principles set forth in Office of Management and Budget (OMB) Circular A-87.

Our initial audit of Federal Fiscal Year (FY) 2000 direct labor costs (the predominant direct cost) charged to the Unemployment Insurance (UI) grant program indicated there were problems with labor costs and certain indirect costs allocated directly to UI and other DOL programs without being adjusted from estimated to actual costs. Therefore, we expanded our audit to include additional years: SFYs ended August 31, 1998, 1999, 2000, and 2001. Also, we interviewed TWC officials and determined that the salaries of officials appeared to be reasonable.

Based on the results of our audit, we determined that TWC did not establish and implement internal controls to ensure that adjustments were made for indirect and direct labor costs for employees who worked on more than one job, as required by OMB Circular A-87. Specifically, we found that:

(1) TWC did not adjust “estimated” costs for certain indirect cost pools allocated to DOL grants using Financial Cost Allocation Tables (FCATs) to actual costs, at least annually, as required by Federal cost principles; and

(2) TWC did not ensure that direct labor and fringe benefits charged to DOL grant awards were based on actual hours worked for employees who worked on more than one project or cost objective, as required by Federal cost principles.

This audit was performed in accordance with applicable standards established by the American Institute of Certified Public Accountants and the *Government Auditing Standards* issued by the Comptroller General of the United States. Our detailed findings, conclusions, and recommendations are contained in the accompanying report.

This report is intended solely for the use of the U.S. Department of Labor; however, the final report is a matter of public record, and its distribution is not limited.

Tichenor & Associates, LLP

TICHENOR & ASSOCIATES, LLP
Louisville, KY
April 21, 2004

EXECUTIVE SUMMARY

Tichenor & Associates, LLP, under contract to the DOL/OIG, audited the direct and indirect costs charged to DOL grants awarded to the TWC. TWC records revealed that it claimed approximately $439.8 million for direct labor and fringe benefits charged to DOL grants and $40.4 million for FCAT indirect costs for the SFYs ended August 31, 1998, 1999, 2000, and 2001.

The initial audit objective was to determine whether direct and indirect costs charged to the DOL Unemployment Insurance (UI) grants awarded to TWC for the period October 1, 1999, through September 30, 2000 (FY 2000), were reasonable, allocable, and otherwise allowable under the Federal cost principles set forth in OMB Circular A-87 and the terms and conditions of the UI grants awarded to TWC.

Our initial audit disclosed problems with labor costs and certain indirect costs allocated directly to UI and other DOL programs without being adjusted from estimated to actual costs. Therefore, we expanded the scope of the audit to include additional years and other Federal grant programs. Specifically, we focused our audit on two types of charges made to all DOL grants administered by TWC for SFYs ending August 31, 1998, 1999, 2000, and 2001. The two types of charges include TWC claims for, and recovery of, (1) $40.4 million of FCAT indirect costs, and (2) $228.7 million of direct labor and fringe benefits.

To accomplish our audit objectives, we reviewed FCAT costs and allocation data for the SFYs 1999, 2000, and 2001. For direct and indirect labor costs, we reviewed data concerning the adequacy of supporting documentation. We also reviewed audit reports by the TWC internal audit staff for SFYs 1997, 1998, and 2000 that contained findings related to the adequacy of supporting documentation for labor costs. TWC internal auditors completed a report for SFY 1999; however, we did not review the report results. Also, we interviewed TWC officials and determined that the salaries of officials appear to be reasonable. We also performed limited testing of the supporting documentation for SFY 2000.

Audit Results

We concluded that TWC did not establish and implement internal controls to ensure that adjustments to actual costs were made for the FCATs and direct labor costs for employees who worked on more than one job as required by OMB Circular A-87. Specifically, we determined that:

1. FCAT costs, part of TWC's indirect costs, were charged to DOL and other programs on the basis of historical data for SFYs 1999, 2000, and 2001. FCATs started in SFY 1999. Any allocation base using historical data caused the allocation to be a cost estimate. OMB Circular A-87 allows the interim use of estimated costs provided they

are adjusted to actual costs at the end of the year. However, TWC officials informed us that TWC did not adjust the $40.4 million in estimated FCAT costs charged to DOL grants to actual costs for the period audited as required by OMB Circular A-87. This occurred because TWC did not establish or implement internal controls to ensure that the adjustments to actual costs were made when FCATs were implemented. Subsequent to our audit fieldwork, TWC planned to adjust the estimated costs to actual costs. (Finding No. 1)

2. During SFYs ending August 31, 1998, 1999, 2000 and 2001, TWC charged direct labor and fringe benefits of approximately $228.7 million to DOL grants for those employees working on more than one project. TWC internal audits of direct labor costs incurred during SFYs 1997, 1998, and 2000 found that many employees working on more than one project were preparing time reports based on predetermined budget estimates, rather than actual time worked on each program/cost objective as required by OMB Circular A-87. TWC internal auditors completed a report for SFY 1999; however, we did not review the report results. To gain an understanding of the magnitude of the problem, we tested time charges for a judgmental sample of 43 employees working on more than one project in the indirect cost centers for SFY 2000. We concluded the problem continues to exist, and it occurred because TWC did not establish or implement internal controls to ensure that the adjustments to actual costs were made when the time distribution system was implemented. (Finding No. 2)

RECOMMENDATIONS

We recommend DOL, Employment and Training Administration (ETA) officials, and DOL Grant Officers take the following action:

1. We recommend the DOL Assistant Secretary for Employment and Training ensure the cognizant DOL Grant Officer(s) adjust the FCAT costs charged to DOL based on actual costs and refund any overcharges to DOL for SFYs 1999 through 2003.

2. We recommend the DOL Assistant Secretary for Employment and Training direct TWC to implement internal control policies and procedures to ensure that estimated costs charged to DOL grant awards, based on FCATS, are adjusted to actual costs at least annually as required by Federal cost principles.

3. We recommend the DOL Assistant Secretary for Employment and Training ensure the cognizant DOL Grant Officer(s) adjust the direct labor costs and fringe benefits charged to DOL for SFYs 1998 through 2003 based on actual costs and refund any overcharges to DOL.

4. We recommend the DOL Assistant Secretary for Employment and Training ensure that TWC:

    a. Assure adequate reporting of actual time worked by monitoring the implementation of its newly revised timekeeping procedures, thus assuring the correction of longstanding problems with its time reporting system.

    b. Conduct monthly audits of time charges being reported by employees working on more than one DOL project until less than 1 percent of sampled time activity reports contain discrepancies, and submit copies of the monthly audit results to DOL's Office of Cost Determination.

AUDITEE'S RESPONSE

In its response to our draft report, TWC officials agreed to the report's recommendations. TWC officials stated they plan to fully implement the process of using actual amounts in determining FCAT percentages each month. Therefore, there will no longer be a need for any "after the fact" adjustments of estimated costs. Also, they completed determining the adjustment of estimated allocated costs to actual for SFYs 1999 through 2002. The adjustments showed that DOL grants were undercharged $1,370,795. Subsequent to responding to the draft report, TWC officials provided us a spreadsheet that showed an additional $1,358,568 was undercharged to DOL grants for SFY 2003. An e-mail from a TWC official stated that DOL and other Federal grants were either charged or refunded their appropriate share based on actual benefiting services, in accordance with OMB Circular A-87.

Also, in its response to our draft report, TWC officials stated that action was taken to improve controls over timekeeping. Time distribution procedures have been updated and made available to all employees. Monthly reminders are sent to all employees to ensure that accurate time charges are being reported. TWC continues to reinforce the importance of reporting actual time worked. An audit recently completed by TWC internal auditors found that only 3 percent of timesheets had errors resulting in a Federal program net overcharges of $2.48.

The response also stated that TWC's finance staff is currently completing a review of all multi-funded time charges reported in SFY 2003. Any incorrect time charges identified in this review will be adjusted based on actual worked programs. Additional training and monthly random sampling of multi-funded time charges reported will be done.

A copy of TWC's complete draft report response is included in this report as an Exhibit.

AUDITOR'S CONCLUSION

The report recommendations will be resolved in ETA's formal audit resolution process. We cannot make a conclusion as to the accuracy of TWC's adjustment of FCAT estimated allocated costs to actual until they are reviewed as part of the audit resolution process.

INTRODUCTION

BACKGROUND

The TWC was formed on September 1, 1995. It was given responsibility to administer and monitor over 28 programs such as the Job Training Partnership Act, Employment Services, UI, Food Stamp Employment and Training, and Child Care Services. In addition, 28 local workforce areas were designated. The purpose of TWC was to create a single agency managing workforce initiatives and to have an employer-driven system with local control over workforce training programs.

For the SFY ended August 31, 2000, TWC employed 3,637 people and reported expenditures of about $233.2 million (excluding funds that passed through to the 28 local workforce areas and capital equipment costs). The DOL grants, primarily awarded by the ETA, accounted for $198.5 million of the reported expenditures, or about 85 percent.

TWC has five administrative support and operating divisions that carry out its various programs. A brief discussion of each division follows.

Workforce Development Division

This division is responsible for establishing and maintaining local workforce development boards. The local boards are responsible for the delivery of integrated workforce services to employers and people seeking employment. Specifically, the services provided include helping employers find qualified workers, helping job seekers with the opportunity or necessary skills to fill job openings, providing child care for low-income parents, career counseling, and job training for welfare recipients.

Unemployment Insurance Division

This division administers the UI program, providing temporary economic security for workers separated from their jobs through no fault of their own. This program is State-administered and federally funded, except for the UI benefits that are provided and collected through unemployment taxes on employers by the State.

Welfare Reform Initiatives Division

The mission of this division is to move Texans off welfare and into self-sufficiency through employment. This division is responsible for developing policies, program improvements, and new initiatives that support its mission. Success is measured in terms of those who leave the welfare rolls due to employment.

Technology and Facilities Management Division

This division furthers the goals of TWC by providing access to the automated services by agency employees and the public. It also is responsible for TWC's maintenance and construction of facilities, supply distribution and warehouse management, and the procurement system.

Administrative Support Division

The Administrative Support Division provides the overall framework within which TWC operates to meet the mission of the organization. The division provides financial services, contract monitoring, human resources management, communications and customer outreach, legal support, information dissemination, contract services, and accumulating and publishing labor market statistics.

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The indirect costs for administrative, support, and technical services used for operating TWC are segregated into several different cost pools. All cost pools except one are called FCATs, and each FCAT allocates its indirect costs directly to those projects that use that particular service. For example, the mainframe computer costs are allocated solely to projects using the computer, and the allocation base is "seconds of mainframe computer time" used. TWC established FCATs for allocating certain costs directly to projects because the inclusion of those costs in the TWC indirect cost pool resulted in inequitable allocations, i.e., some projects received little if any indirect costs, but they used many indirect resources. Each of these FCATs uses a basis for allocation other than that used by the TWC indirect cost pool. Each FCAT indirect cost pool includes labor, fringe benefits, and non-personnel costs. Since each FCAT allocates its indirect costs directly to benefiting projects, direct labor portions of the FCAT absorbs a fair share of TWC indirect costs. FCAT costs are allocated to benefiting projects monthly.

The basic departmental TWC cost pool that contains indirect costs that generally benefit all cost objectives within the agency is not a FCAT. The costs in this pool are allocated directly to projects based on the proportion of direct salaries related to time spent on each project. The TWC indirect cost pool rate is computed monthly, which results in actual indirect costs charged monthly to projects.

TWC employees in many cost centers work only on direct projects such as UI or employment services. In other instances, employees working in the same cost center may be working on both direct projects and indirect cost objectives. TWC requires all employees to report their time spent on direct and indirect projects so the time distribution system can assure that salaries and wages are charged to the appropriate cost objective, either direct or indirect. After eliminating "pass through" funds, salaries and wages constituted more than 53 percent of TWC's operating costs for SFY 2000. Other costs, such as rent, supplies, utilities, etc., are charged directly to the appropriate cost objective, either direct or indirect. All direct costs are recorded and charged to projects monthly.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our initial objectives were to conduct an audit of direct and indirect costs charged to the UI program for FY 2000, the period October 1, 1999, through September 30, 2000, to determine whether such costs were reasonable, allocable, and otherwise allowable under the Federal cost principles set forth in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments* and the implementing guidelines set forth in ASMB C-10, *Cost Principles and Procedures for Establishing Cost Allocation Plans and Indirect Cost Rates for Agreements with the Federal Government*. Further, the audit objectives provided that, depending on the results of our audit of direct and indirect costs charged to the UI program, the scope of the audit could be expanded to include additional years and other Federal grant programs.

Our initial audit work disclosed problems with the allowability of all FCAT and direct labor costs not being adjusted from estimated to actual costs. Accordingly, we focused our audit on two types of costs that TWC charged to DOL grants for SFYs ending August 31, 1998, through 2001. The types of charges were (1) $40.4 million of FCAT indirect costs for SFYs 1999, 2000, and 2001; and (2) $228.7 million of approximately $439.8 million of total direct labor and fringe benefits charged to DOL programs. The $228.7 million was for employees working on more than one project during SFYs 1998, 1999, 2000, and 2001.

To achieve our objectives, we examined (1) the processes used by TWC to assure that those FCAT costs charged to DOL projects were allocated on the basis of "relative benefits received," and (2) the adequacy of supporting documentation for claiming and recovering direct and indirect labor costs.

For FCAT costs, our scope of work included (a) determining the nature of the various indirect services provided by TWC administrative groups that were charged to programs through use of FCATs and the extent to which they benefited DOL-funded programs, and (b) evaluating the bases used to allocate indirect costs to the various cost objectives to determine whether the allocations were based on "relative benefits received." In our attempt to evaluate management controls of FCAT indirect costs, we interviewed a TWC official to determine if the costs were adjusted to actual, compiled total FCAT costs from TWC records, and determined the portion applicable to DOL programs. However, since TWC had no policies and procedures to adjust the FCAT costs to actual, there were no management controls to review for adjusting costs to actual.

For direct labor costs, our scope of work included determining the TWC processes for documenting direct labor costs, including the time distribution system used for claiming and recovering direct labor costs. Specifically, we reviewed the Time Distribution Procedure Manual to determine the procedures used in reporting employee time and the adequacy of supporting documentation. We also reviewed audit reports by the TWC internal audit staff for SFYs 1997, 1998, and 2000 that contained findings related to the adequacy of supporting documentation for labor costs. TWC internal auditors completed a report for SFY 1999; however, we did not review the report results. Additionally, we interviewed TWC officials to determine whether the salaries of officials appear to be reasonable. Further, we interviewed TWC employees and reviewed timesheets for a judgmental sample of 43 employees in SFY 2000 to determine if the labor costs were allowable in accordance with OMB Circular A-87. However, since TWC had no policies and procedures to adjust the labor costs to actual, there were no management controls to review for adjusting costs to actual.

This engagement was performed in accordance with auditing standards established by the American Institute of Certified Public Accountants and with the *Government Auditing Standards* (1994 Revision) issued by the Comptroller General of the United States. Audit fieldwork was performed at TWC offices in Austin, Texas.

FINDINGS AND RECOMMENDATIONS

FINDING 1. TWC Did Not Adjust Estimated FCAT Costs Allocated to DOL Grants to Reflect Actual Costs as Required by Federal Cost Principles

Our audit found that FCAT costs were directly charged to DOL and other programs on the basis of historical data. Any allocation base using historical data causes the allocation to become a cost estimate, which is not allowable under Federal cost principles. In response to our inquiries, we were informed that TWC did not adjust the $40.4 million in estimated FCAT costs charged to DOL/ETA grants to actual costs for the period audited, i.e., SFYs 1999, 2000, and 2001, as required by OMB Circular A-87. This occurred because TWC did not establish and implement internal controls to ensure the adjustments were made when FCATs were implemented.

OMB Circular A-87, Attachment B, paragraph 11.h. (5)(e), states that budget estimates or other distribution percentages determined before the services are performed do not qualify as support for charges to Federal awards. However, estimates may be used for interim accounting purposes, provided that actual costs are compared to the budgeted cost distributions quarterly and are adjusted to actual costs at least annually.

According to TWC officials, the FCATs were created to more fully comply with OMB Circular A-87 guidelines, which require that costs be allocated solely on the basis of "relative benefits received." Each FCAT uses a different allocation base than the one used in TWC's indirect cost rate agreement.

TWC began using FCATs in SFY 1999 to allocate certain departmental overhead costs (previously recovered through the TWC departmental indirect cost rate) directly to the benefiting cost objectives. TWC officials stated that they developed the FCATs because certain categories of departmental overhead costs included in its indirect cost rate agreement with DOL were not being allocated to the various cost objectives on the basis of "relative benefits received," as required by the Federal cost principles. Specifically, some cost objectives and programs were being allocated very little indirect costs under the TWC indirect cost rate agreement but were using substantial indirect cost resources. TWC officials said this situation was caused by two factors: (1) TWC absorbed several programs from other State agencies as well as those of its predecessor (the Texas Employment Commission); and (2) TWC was required to establish 28 geographically dispersed local workforce development boards.

Substantial amounts of funding in U.S. Department of Health and Human Services (HHS) and State programs are "pass through" funds to these local boards. Many TWC programs are currently operated primarily at the local level through the workforce development boards, but most administrative costs at the local level are contracted out. TWC believes this situation caused a distortion about which programs were absorbing the indirect costs. TWC officials said they were able to transfer certain indirect costs directly to the main users of those particular services through the establishment of several FCATs. For example, contract-monitoring costs are now mainly allocated to State and HHS programs. However, if this function had been left in the TWC indirect cost pool as was previously done, DOL grant awards would have absorbed 80 to 85 percent of these costs. TWC believes that the use of FCATs keeps its indirect cost rate low and is consistent with A-87 guidelines requiring that costs be allocated solely to the beneficiaries of the services.

We agree with TWC that using FCATs is an improvement over the methodology used in prior years. However, our audit disclosed that (1) the data used to develop the allocation base for each FCAT were estimates based on historical data from prior years, rather than actual current year data; and (2) TWC failed to adjust its cost distributions to actual costs, as required by Federal cost principles, when the FCATs were implemented and in subsequent years. For SFYs 1999, 2000, and 2001, TWC allocated estimated costs of $40,373,745 out of $49,952,260 of cumulative departmental overhead costs to DOL grants.

During our exit conference, the Chief Financial Officer stated TWC had already started the process of accumulating data so it can adjust the FCAT costs charged to DOL for SFYs 1999, 2000, and 2001 to actual costs.

RECOMMENDATIONS

1. We recommend the DOL Assistant Secretary for Employment and Training ensure the cognizant DOL Grant Officer(s) adjust the FCAT costs charged to DOL based on actual costs and refund any overcharges to DOL for SFYs 1999 through 2003.

2. We recommend the DOL Assistant Secretary for Employment and Training direct TWC to implement internal control policies and procedures to ensure that estimated costs charged to DOL grant awards, based on FCATS, are adjusted to actual costs at least annually as required by Federal cost principles.

AUDITEE’S RESPONSE

In response to our draft report, TWC officials stated they plan to fully implement the process of using actual amounts in determining FCAT percentages each month. Therefore, there will no longer be a need for any "after the fact" adjustments of estimated costs. Also, they completed determining the adjustment of estimated allocated costs to actual for SFYs 1999 through 2002. The adjustments showed that DOL grants were undercharged $1,370,795. Subsequent to responding to the draft report, TWC officials provided a spreadsheet that showed an additional $1,358,568 was undercharged to DOL grants for SFY 2003. An e-mail from a TWC official stated that DOL and other Federal grants were either charged or refunded their appropriate share based on actual benefiting services in accordance with OMB Circular A-87.

AUDITOR'S CONCLUSION

The recommendations will be resolved as part of ETA's audit resolution process. We cannot make a conclusion as to the accuracy of TWC's adjustment of FCAT estimated allocated costs to actual for SFYs 1999 through 2003 until the adjustments are reviewed as part of the audit resolution process.

FINDING 2. Employees' Activity Reports Used to Support Direct Labor and Fringe Benefit Costs Were Not Adjusted to Actual as Required by Federal Cost Principles

OMB Circular A-87 requires that labor charges be based on the actual time worked, especially by those employees working on more than one project, not estimated time worked. Our audit disclosed that TWC does not always have adequate supporting documentation for direct labor costs for employees who worked on more than one program/cost objective. TWC was aware of this problem because TWC's internal auditors reported the situation repeatedly during audits of SFYs 1997, 1998, and 2000. TWC internal auditors completed a report for SFY 1999; however, we did not review the report results. TWC corrective actions over the past few years have not eliminated the problem. Based on our review of a judgmental sample of 43 employee Daily Personnel Activity Reports for SFY 2000, the problem continues to exist. As a result, TWC cannot ensure that direct labor costs were properly charged to DOL/ETA grants. TWC was reimbursed approximately $228.7 million by DOL in direct salaries and fringe benefits for employees working on more than one project during SFYs 1998, 1999, 2000, and 2001.

In order for costs to be allowable, they must be adequately documented. In the case of salaries and wages, OMB Circular A-87 mandates very detailed and specific documentation requirements that must be met in order for such costs to be allowable under Federal grant awards. The Federal cost principles state that where employees work on multiple activities or cost objectives, a distribution of their salaries or wages must be supported by personnel activity reports or equivalent documentation. In addition, these personnel activity reports must

- reflect an after-the-fact distribution of the actual activity of each employee,
- account for the total activity for which each employee is compensated,
- be prepared at least monthly and coincide with one or more pay periods, and
- be signed by the employee.

OMB Circular A-87 further states that "Budget estimates or other distribution percentages determined before the services are performed do not qualify as support for charges to Federal awards. . . ."

Some examples of TWC's failure to meet various Commission and OMB Circular A-87 requirements include the following. Specifically, TWC reports for SFYs 1997, 1998, and 2000 stated the following:

1. A TWC internal audit report dated August 14, 1997, on the TWC cost allocation process agency-wide, covering the period October 1996 through April 1997, found that 80 percent of the personnel activity reports tested, for employees charging more than one project code, reported time incorrectly. Specifically, the auditors found employees were reporting hours based on budgeted percentages of how their positions were funded instead of the actual time spent on

identifiable projects. The audit report stated that this practice resulted in actual effort not being properly charged against identifiable benefiting programs. The internal auditors noted in the report's Executive Summary that, as a result of not reporting actual time spent on programs and activities, some costs might be disallowed by DOL for salary costs inappropriately charged.

2. In a follow-up report, issued on July 22, 1998, the auditors found the problem still existed after testing activity reports for the period November 1997 through April 1998. Specifically, the auditors found 89 percent of the multiple activity employees had not reported actual time spent on programs, 9 percentage points higher than previously reported. The audit report stated that the testing showed that employees had continued to report their daily hours based on budget percentages rather than actual daily activity hours worked on specific programs. The auditors also noted that in some cost centers the situation still existed where one employee was completing time sheets for all office employees.

3. The TWC internal audit report entitled "A Performance Audit of Budget/Cost Allocation Process" for SFY 2000 also indicated that there were instances every month where the hours on the activity report and the Automated Time Distribution System did not agree. This demonstrates that budget estimates, rather than actual time, were used to charge projects.

We tested a judgmental sample of employees to determine whether the problem still existed, and, if so, to gain some understanding of the magnitude of the problem. Based on our review of a judgmental sample of 43 employee Daily Personnel Activity Reports for SFY 2000, we concluded the problem continues to exist because TWC did not establish or implement internal controls to ensure that the adjustments to actual costs were made when the time distribution system was implemented.

We believe that continuing to not adequately support direct labor costs is evidence that TWC did not establish and implement internal control policies and procedures to ensure direct labor costs are documented and estimated time worked is adjusted to reflect actual time worked.

RECOMMENDATIONS

3. We recommend the DOL Assistant Secretary for Employment and Training ensure the cognizant DOL Grant Officer(s) adjust the direct labor costs and fringe benefits charged to DOL for SFYs 1998 through 2003 based on actual costs and refund any overcharges to DOL.

4. We recommend the DOL Assistant Secretary for Employment and Training ensure that TWC:

a. Assure adequate reporting of actual time worked by monitoring the implementation of its newly revised timekeeping procedures, thus assuring the correction of longstanding problems with its time reporting system.

b. Conduct monthly audits of time charges being reported by employees working on more than one DOL project until less than 1 percent of sampled time activity reports contain discrepancies, and submit copies of the monthly audit results to DOL's Office of Cost Determination.

AUDITEE'S RESPONSE

In its response to our draft report, TWC officials stated that action was taken to improve controls over timekeeping. Time distribution procedures have been updated and made available to all employees. Monthly reminders are sent to all employees to ensure that accurate time charges are being reported. TWC continues to reinforce the importance of reporting actual time worked. An audit recently completed by TWC internal auditors found that only 3 percent of timesheets had errors resulting in a net overcharge to Federal programs of $2.48.

The response also stated that TWC's finance staff is currently completing a review of all multi-funded time charges reported in SFY 2003. Any incorrect time charges identified in this review will be adjusted based on actual worked programs. Additional training and monthly random sampling of multi-funded time charges reported will be done. The response stated that TWC is also developing a new time reporting system that will enhance internal controls over employee reported time charges.

AUDITOR'S CONCLUSION

The recommendations will be resolved as part of ETA's audit resolution process.

AUDITEE'S RESPONSE