



OFFICE OF INSPECTOR GENERAL

Catalyst for Improving the Environment

Quick Reaction Report

City of Bad Axe, Michigan - Unallowable Costs Claimed Under EPA Grant XP98578301

Report No. 08-2-0095

February 27, 2008



Report Contributors:

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Abbreviations

EPA	U.S. Environmental Protection Agency
Grant	Grant XP98578301
Grantee	City of Bad Axe, Michigan
OIG	Office of Inspector General

Cover photo: The building pictured is a pumping station installed along the pipeline between the City of Bad Axe and the Water Treatment Plant in Port Austin, Michigan.
(EPA OIG photo)



At a Glance

Catalyst for Improving the Environment

Why We Did This Review

The U.S. Environmental Protection Agency (EPA) Office of Inspector General (OIG) conducted a review of earmarked grants known as Special Appropriation Act Projects issued to local and tribal governments. We selected the City of Bad Axe, Michigan, for review.

Background

The City of Bad Axe received an EPA Special Appropriation Act Project grant, XP98578301. The purpose of the grant was to provide Federal assistance for engineering, planning, and constructing a 17-mile drinking water pipeline from Port Austin, Michigan, to the City of Bad Axe.

For further information, contact our Office of Congressional and Public Liaison at (202) 566-2391.

To view the full report, click on the following link:
www.epa.gov/oig/reports/2008/20080227-08-2-0095.pdf

City of Bad Axe, Michigan – Unallowable Costs Claimed Under EPA Grant XP98578301

What We Found

The City of Bad Axe (grantee) purchased two parcels of land totaling \$51,297 without obtaining prior approval as required by Federal regulations. The grantee also paid an engineering firm \$211,143 to design a water treatment facility but did not use the design. As a result, EPA needs to recover \$262,440 under Grant XP98578301.

What We Recommend

We recommend that the Regional Administrator, EPA Region 5, recover the unallowable land purchase and design costs totaling \$262,440.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

OFFICE OF
INSPECTOR GENERAL

February 27, 2008

MEMORANDUM

SUBJECT: City of Bad Axe, Michigan – Unallowable Costs
Claimed Under EPA Grant XP98578301
Report No. 08-2-0095

FROM: Melissa M. Heist *Melissa M. Heist*
Assistant Inspector General for Audit

TO: Mary A. Gade
Regional Administrator
EPA Region 5

This report contains time-critical issues the Office of Inspector General (OIG) identified and recommends recovery of Federal funds drawn down by the recipient. This report represents the opinion of the OIG and does not necessarily represent the final position of the U.S. Environmental Protection Agency (EPA). EPA managers will make final determinations on matters in this report.

The estimated cost of this report – calculated by multiplying the project's staff days by the applicable daily full cost billing rate in effect at the time – is \$73,616.

Action Required

In accordance with EPA Manual 2750, Chapter 3, Section 6(f), you are required to provide us your proposed management decision for resolution of the findings contained in this report before any formal resolution can be completed with the recipient. Your proposed decision is due in 120 days, or on June 26, 2008. To expedite the resolution process, please email an electronic version of your proposed management decision to kasper.janet@epa.gov.

We have no objections to the further release of this report to the public. This report will be available at <http://www.epa.gov/oig>. If you have any questions, please contact Janet Kasper, Director, Assistance Agreement Audits, at 312-886-3059 or the email address above.

Purpose

The Office of Inspector General is reviewing Special Appropriation Act Project grants to identify issues warranting further analysis. This includes reviewing the total project costs incurred by selected grant recipients. During our review of the Special Appropriation Act Project grant awarded to the City of Bad Axe, Michigan (grantee), we identified the following conditions that we believe require immediate attention. The grantee claimed and was reimbursed for unallowable land purchase and design costs under Grant XP98578301.

Background

U.S. Environmental Protection Agency (EPA) Region 5 awarded Grant XP98578301 (grant) on May 13, 1998. The purpose of the grant was to provide Federal assistance for engineering, planning, and constructing a 17-mile drinking water pipeline from Port Austin, Michigan, to the City of Bad Axe. In 2002, the grantee and Port Austin formed the Huron Regional Water Authority (Authority). In 2004, EPA transferred the grant to the Authority because the grantee could not provide the required matching contribution. As a match to the grant, the Authority funded the design and construction of the water treatment plant that connects to the pipeline. The grant's project period was from June 1, 1998, to September 30, 2005. The grantee received \$4,573,751 in EPA funds for the pipeline before EPA transferred the grant.

Scope and Methodology

We performed our examination in accordance with generally accepted government auditing standards, issued by the Comptroller General of the United States, with the exception of understanding information control systems as required under Section 7.23 and a complete understanding of internal controls as required under Section 7.16. We did not obtain an understanding of information control systems since the review of general and application controls was not relevant to the assignment objectives. We also did not obtain a complete understanding of the internal control system. Instead, we gained a general understanding of the processes the recipient used to account for funds and focused our review on the source documents that support costs claimed under the grant. We did not test the recipient's grant drawdown process or process for entering information into its accounting system.

We conducted our field work between November 13 and December 21, 2007. We made a site visit to the grantee and performed the following steps:

- Reviewed the grantee's accounting records, supporting documentation for drawdowns, invoices, bank statements, and cancelled checks.
- Conducted telephone interviews of current and former engineering firms' personnel.
- Conducted interviews with grantee personnel.
- Visited the pumping stations and pipeline hydrants constructed under the grant.
- Toured the drinking water treatment plant connected to the pipeline.
- Discussed issues related to this grantee with the Region 5 project officer.

Findings

The grantee purchased two parcels of land totaling \$51,297 without obtaining prior approval as required by Federal regulations. The grantee also paid an engineering firm \$211,143 to design a water treatment facility but did not use the design. As a result, EPA needs to recover \$262,440 under Grant XP98578301.

Unallowable Cost of Land Purchases

The grantee claimed costs for two land purchases without obtaining prior approval from EPA. The land was purchased for two of the three pumping stations along the pipeline between Bad Axe and the water treatment facility in Port Austin. According to Office of Management and Budget Circular A-87, Section 15.b.(1):

Capital expenditures for general purpose equipment, buildings, and land, are unallowable as a direct cost except with the prior approval of the awarding agency.

The grantee incurred \$51,297 for the land purchases without obtaining EPA approval. Therefore, that cost is unallowable under the grant.

Unallowable Cost of Plant Design

The grantee paid an engineering firm \$211,143 to design a water treatment plant. However, this design was not used in the final construction of the plant. The introductory paragraph of Office of Management and Budget Circular A-87, Attachment B, states:

A cost is allowable for Federal reimbursement only to the extent of benefits received by Federal awards and its conformance with general policies and principles....

The Federal award and the grantee did not receive any benefits from the design. When the grant was transferred over to the Authority, the Authority funded the design and construction of the water treatment plant as a match to the EPA funds. The Authority did not use the design the grantee purchased with grant funds because the Authority selected a different plant location and a different design. As a result, the costs totaling \$211,143 for the unused design are unallowable.

Recommendation

1. We recommend that the Regional Administrator, EPA Region 5, recover the unallowable land purchase and design costs totaling \$262,440.

Grantee Comments

On January 23, 2008, we held an exit conference with the grantee and EPA Region 5. The grantee agreed to the factual accuracy of the costs questioned. However, the grantee said that it

informed EPA of these costs through the supporting documentation it had submitted to EPA for reimbursements. The grantee said that since EPA reimbursed the costs the grantee considered the costs approved under the grant.

OIG Response

EPA did not provide any documentation or rationale to change our position. We followed up with EPA Region 5 regarding the reimbursement requests, and the Region referred us to the EPA Finance Center. The Finance Center had no supporting invoices associated with reimbursement requests from this grantee. We continue to believe that EPA Region 5 should recover the unallowable land purchase and design costs totaling \$262,440.

Status of Recommendations and Potential Monetary Benefits

RECOMMENDATIONS						POTENTIAL MONETARY BENEFITS (in \$000s)	
Rec. No.	Page No.	Subject	Status ¹	Action Official	Planned Completion Date	Claimed Amount	Agreed To Amount
1	2	Recover the unallowable land purchase and design costs totaling \$262,440.	O	Regional Administrator, EPA Region 5		\$262.4	

¹ O = recommendation is open with agreed-to corrective actions pending;
 C = recommendation is closed with all agreed-to actions completed;
 U = recommendation is undecided with resolution efforts in progress

