



NATIONAL ENDOWMENT FOR THE HUMANITIES

OFFICE OF INSPECTOR GENERAL



SEMIANNUAL REPORT TO CONGRESS

October 1, 2002 to March 31, 2003

REPORT NO. 28

**"Democracy demands wisdom and vision in its citizens"
National Foundation on the Arts and Humanities Act of 1965**

THE OFFICE OF INSPECTOR GENERAL

serves American taxpayers
by investigating reports of waste, fraud,
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unethical conduct involving federal funds.

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involving NEH programs, operations, or employees

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Office of Inspector General-Hotline
National Endowment for the Humanities
1100 Pennsylvania Ave. N.W., Room 419
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Fax: (202) 606-8329

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NATIONAL ENDOWMENT FOR THE HUMANITIES

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WASHINGTON, D.C. 20506

OFFICE OF INSPECTOR GENERAL

April 30, 2003

Honorable Bruce Cole
Chairman
National Endowment for the Humanities
Washington, D.C. 20506

Dear Chairman Cole:

I am pleased to provide you with the Office of Inspector General's Semiannual Report to Congress for the first half of fiscal year 2003. The report is submitted in accordance with the Inspector General Act of 1978, as amended. Section 5 of the Act requires that you submit this report, with your Report of Final Action, to the appropriate committee or subcommittee of the Congress within 30 days of its receipt. The report provides a summary of the activities of the OIG during the six-month period ended March 31, 2003.

During this period, we completed one internal review, three grantee reviews, and two quality control reviews of independent public accounting firms. Reports were issued on these reviews. An additional six reviews are in various stages of completion. In the investigations program, we received several "Hotline" contacts. However, our inquiries into these matters did not lead to the opening of any new investigations.

I appreciate your support and look forward to working with you and all agency staff to help ensure that NEH delivers grant awards in an economical, effective and efficient manner.

Sincerely,

Sheldon L. Bernstein
Inspector General

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INTRODUCTION

THE NATIONAL ENDOWMENT FOR THE HUMANITIES

In order to promote progress and scholarship in the humanities and the arts in the United States, Congress enacted the National Foundation on the Arts and the Humanities Act of 1965. This Act established the National Endowment for the Humanities as an independent grant-making agency of the federal government to support research, education, and public programs in the humanities. Grants are made through four divisions - Research Programs, Education Programs, Preservation and Access, and Public Programs -- and two offices -- Challenge Grants and Federal-State Partnership.

The Act that established the National Endowment for the Humanities says "The term 'humanities' includes, but is not limited to, the study of the following: language, both modern and classical; linguistics; literature; history; jurisprudence; philosophy; archaeology; comparative religion; ethics; the history, criticism, and theory of the arts; those aspects of social sciences which have humanistic content and employ humanistic methods; and the study and application of the humanities to the human environment with particular attention to reflecting our diverse heritage, traditions, and history and to the relevance of the humanities to the current conditions of national life."

THE OFFICE OF INSPECTOR GENERAL

The NEH Office of Inspector General was established on April 9, 1989, in accordance with the Inspector General Act Amendment of 1988, (Public Law 100-504). In this legislation, Congress established Offices of Inspector General in several departments and in thirty-three agencies, including the NEH. The NEH Inspector General (IG) is appointed by the Chairman. The independence of the IG is an important aspect of the Act. For example, the IG:

- cannot be prevented from initiating, carrying out, or completing an audit or investigation, or from issuing any subpoena;
- has access to all records of the agency;
- reports directly to the Chairman, and can only be removed by the Chairman, who must promptly advise Congress of the reasons for the removal; and

- reports directly to Congress.

The Act states that the Office of Inspector General is responsible for (1) conducting audits and investigations; (2) reviewing legislation; (3) recommending policies to promote efficiency and effectiveness; and (4) preventing and detecting fraud, waste, and abuse in the operations of the agency. The Inspector General is also responsible for keeping the Chairman and Congress fully and currently informed of problems and deficiencies in the programs and operations.

The OIG staff consists of the Inspector General, a Deputy Inspector General, two auditors, and a secretary. The OIG and the Office of the General Counsel (OGC) have a Memorandum of Understanding detailing the procedures for the OIG to be provided with OGC legal services. Investigations are handled by the Inspector General, an auditor and as required by the agency's Assistant General Counsel.

AUDIT AND REVIEW ACTIVITIES

This office is responsible for external and internal audits. External auditing includes grants, pre-award accounting system surveys, review of OMB Circular A-133 reports, and on-site quality control reviews of CPA work papers. Internal efforts consist of audits, inspections, and

reviews/evaluations of the NEH administrative, programmatic, and financial operations. During this reporting period, the OIG received and processed 83 OMB Circular A-133 audit reports, (see Single Audit Act Reviews).

LIST OF REPORTS ISSUED

The following is a list of reports issued by the OIG during this reporting period. The Act requires us to report on the "Dollar Value of Recommendations that Funds Be Put to Better Use" and the "Total Dollar Value of Questioned

Costs" (including a separate category for the "Dollar Value of Unsupported Costs"). None are reported during this period.

	Report Number	Date Issued
INTERNAL AUDITS/REVIEWS		
Fiscal Year Ended September 30, 2002 Consolidated Review of the Federal Managers' Integrity Act (FMFIA)	OIG-03-01 (IR)	01/08/03
EXTERNAL AUDITS/REVIEWS/SURVEYS		
Review of Mississippi Action for Community Education (MACE) Audited Financial Statements for the Fiscal Year Ended December 31, 2001	OIG-03-01 (ER)	01/07/03
Review of the Books and Records of James Agee Film Project/ Ross Spears	OIG-03-02 (ER)	01/08/03
Telephone Survey -Social Media Productions	OIG-03-01 (TS)	03/31/03
QUALITY CONTROL REVIEWS		
Quality Control Review of the Financial Statement and Compliance Audit of New York Foundation for the Arts Fiscal Year Ended June 30, 2001	OIG-03-101 (QCR)	03/19/03
Quality Control Review of the Financial Statement and Compliance Audit of Virginia Foundation for the Humanities and the Public Policy for the Year Ended October 31, 2000	OIG-03-102 (QCR)	03/31/03

SUMMARY OF REPORTS ISSUED

INTERNAL REVIEWS

Fiscal Year Ended September 30, 2002 Consolidated Review of the Federal Managers' Integrity Act (FMFIA) January 8, 2003, OIG-03-01 (IR)

We performed a limited review of the information submitted by each office head/division director and the chairman's letter sent to President Bush. Our review covered fiscal year ended September 30, 2002. We found that the agency generally complied with the Act.

EXTERNAL AUDITS/REVIEWS

Review of Mississippi Action for Community Education (MACE) Audited Financial Statements for the Fiscal Year Ended December 31, 2001, January 7, 2003, OIG-03-01 (ER)

The objectives of our review were to determine if MACE was viable as a going concern and that it would have the ability to manage and account for NEH grant funds. In November 2000, the NEH's chairman approved a challenge grant award to MACE, (Application No. CH-20781).

The OIG learned shortly thereafter that MACE and the executive director were being investigated by federal law enforcement agencies. Therefore, the NEH OIG requested that NEH postpone making the award pending the outcome of the investigation.

The former executive director was indicted in January 2002, however, the organization was not included in the indictment. From October 2001, NEH had been working with the new executive director to obtain adequate documentation that MACE was a viable organization. The December 31, 2000 audit report disclosed internal control weaknesses. Therefore, we informed MACE that we needed additional documentation and the December 31, 2001 audited financial statements. In the latter part of December 2002, we received sufficient information to opine that NEH could release the funds for the NEH challenge grant.

Review of the Books and Records of James Agee Film Project/ Ross Spears January 8, 2003, OIG-03-02 (ER)

The James Agee Film Project (Project) and the project director Mr. Ross Spears were previously audited by an independent public accountant (IPA). The IPA questioned costs and working with the OIG, eventually cleared all costs. Therefore, the OIG asked NEH to place the Project and Mr. Spears on the "Problem Grantee List—Organizations and Individuals Requiring a Pre-Award Survey," maintained by the NEH Office of Grant Management. The OIG performed a telephone

survey of the Project's accounting and management system and opined that the Project could receive a chairman's grant. However, the OIG stated that before the Project could be allowed to receive a project production grant, we would have to audit/review the final costs of the chairman's grant. Our review revealed that the Project accounted for and managed grant funds adequately. We had NEH remove the Project and Mr. Spears from the "Problem Grantee List."

EXTERNAL REVIEWS (continued)

Telephone Survey - Social Media Productions March 31, 2003, OIG-03-01 (TS)

The objective of this review was to obtain information to determine the adequacy of the organization's accounting system, management controls, and policies and procedures designed to administer grant funds. Social Media Productions was selected for this review because the organization has received substantial support from NEH and since it had not expended \$300,000 or more of federal funds in a single year, it has not been subject to the audit requirements of OMB Circular A-133.

Based on the information obtained, we concluded that the accounting system, management controls, and administrative policies and procedures implemented by Social Media Productions provide assurance that the organization can adequately manage and account for NEH grant funds. However, we found several conditions that should be addressed to ensure compliance with federal regulations.

Social Media Productions agreed with our recommendations. The OIG is monitoring the corrective action plan.

QUALITY CONTROL REVIEWS

Quality Control Review of the Financial Statement and Compliance Audit of New York Foundation for the Arts (NYFA) Fiscal Year Ended June 30, 2001 March 19, 2003, OIG-03-101 (QCR)

The objectives of the QCR were to (1) ensure that the audit was conducted in accordance with Government Auditing Standards (GAS) and meets single audit requirements; (2) identify any follow-up work needed; and (3) identify issues that may require the attention of NEH management.

We found that the audit was generally conducted in accordance with applicable standards. However, the audit did not, in all respects meet single audit requirements. Several exceptions were noted:

- The working papers did not evidence the independent public accountant's (IPA) efforts to understand and test internal controls related to subrecipient

monitoring. Furthermore, the working papers did not adequately document the IPA's efforts to test NYFA's compliance with subrecipient monitoring requirements.

- The IPA incorrectly determined that program income was not an applicable compliance requirement. Consequently, the IPA did not test internal controls related to program income or NYFA's compliance with program income requirements.

We made recommendations to the IPA on how to correct these exceptions.

QUALITY CONTROL REVIEWS (continued)

Quality Control Review of the Financial Statement and Compliance Audit of Virginia Foundation for the Humanities and the Public Policy for the Year Ended October 31, 2001 March 31, 2003, OIG-03-102 (QCR)

The objectives of the QCR were to (1) ensure that the audit was conducted in accordance with Government Auditing Standards (GAS) and meets single audit requirements; (2) identify any follow-up work needed; and (3) identify issues that may require the attention of NEH management.

We found that the audit was generally conducted in accordance with applicable standards. However, the audit did not, in all respects meet the single audit requirements. Several exceptions were noted:

- There was no evidence in the working papers that testing had been performed on disbursement informa-

tion reported on both the Federal Cash Transactions Report and the last two Financial Status Reports.

- The IPA's internal control testing did not include the Foundation's regrant program.
- Federal expenditures reported on the Schedule of Expenditures of Federal Awards and the Data Collection Form for three NEH programs were overstated.

We made recommendations to the IPA on how to correct these exceptions.

SINGLE AUDIT ACT REVIEWS

We receive audit reports on NEH grantee organizations from other federal agencies (mainly the Department of Health and Human Services), state and local government auditors, and independent public accountants (IPA). These reports are the result of OMB Circular A-133 audits and they cover financial activity, compliance with laws and regulations, and grantee management (internal) controls over federal expenditures.

During the six-month period ended March 31, 2003, we reviewed 83 OMB Circular A-133 audit reports. Eight of the reports contained audit findings. Seven of the reports with findings were associated with state humanities councils. However, we did not issue any reports to the Endowment during this period.

AUDITS/REVIEWS IN PROGRESS

Review of the NEH Purchase Card Program

The General Accounting Office and other federal Inspectors General have been reporting that weak internal controls has created situations where improper purchases can go undetected. The NEH OIG is reviewing the NEH controls to determine if improper purchases would be detected or prevented.

Review of the NEH Timekeeping Process

The OIG was requested to review the timekeeping process because several NEH offices continually receive Leave Error Reports (LER) from the National Finance Center (the processing agency). Our objective is to identify the reasons for the LERs and to recommend procedures to assist the timekeepers in avoiding future problems.

Review of Cost-Sharing Claimed on Final Financial Status Reports by State Humanities Councils

State Humanities Councils have a legal duty to cost-share an amount equal to the general operating grants awarded by NEH. The OIG has found that independent public accountants are not adequately testing cost-sharing records. Since the cost-sharing requirement is based on a provision in the NEH legislation, the amounts reported to NEH should be tested. Our review will determine if the underlying records support amounts claimed on final Financial Status Reports.

Accounting System/Internal Control Telephone Survey of NEH Grantee—Ways of Knowing

The objective of this review is to obtain information to determine the adequacy of the grantee's accounting system, management controls, and policies and procedures designed to administer grant funds.

Accounting System/Internal Control Review of Catticus Corporation

The objective of this review is to determine the adequacy of the grantee's accounting system, internal controls, and monitoring procedures related to two subrecipients. In addition, we are reviewing the adequacy of the two subrecipients' accounting system and internal controls. The grantee was selected for this review because the grantee received a substantial award from NEH and was not required to have an OMB Circular A-133 audit.

Feasibility of Negotiating an Indirect Cost Rate for the Louisiana Endowment for the Humanities (LEH)

The objective of this review is to determine if LEH's accounting records are adequate as a basis for negotiating an indirect cost rate. The LEH has received multiple project grants during the past several years. In accordance with NEH policy, the LEH has been charging an administrative fee of 10 percent of modified direct costs to project grants. However, NEH policy limits such administrative fees to \$5,000 per year for each project grant. State council organizations are allowed up to \$20,000 in administrative fees in any one year. (This is necessary because a few state councils may have several projects outstanding in any particular year.)

We initiated this review since LEH receives multiple project grants from NEH and a negotiated rate could allow LEH to recover more of its actual overhead expenses (in excess of the current \$20,000 annual limitation). In addition, LEH may be able to charge general administrative costs to project grants from other federal agencies and the State of Louisiana.

INVESTIGATIVE ACTIVITIES

BACKGROUND

The Inspector General Act provides the authority for the Office of Inspector General to investigate possible violations of criminal or civil laws, administrative regulations, and agency policies, which relate to the programs and operations of the NEH. The OIG Hotline, e-mail address, and regular mail are efficient and effective means of receiving allegations or complaints from employees, grantees, contractors, and the general public. The OIG has obtained assistance from other OIGs, the Federal Bureau of Investigation, the Postal Inspection Service, and other investigative entities as necessary.

When the OIG receives a complaint or allegation of a criminal or administrative violation, we make a determination of the appropriate action to take. This can be an audit, an investigation, a referral to another NEH office or division, or a referral to another federal agency.

As of October 1, 2002, two cases were open. During the six months ended March 31, 2003, we received four Hotline" contacts. We are holding one matter open at March 31, 2003.

OPEN AT OCTOBER 1, 2002

- Allegation that a grantee organization was having financial problems and NEH would not receive a final product. Our inquiry revealed that the organization was indeed in dire straits; however, there was no indication that NEH funds were not properly spent and accounted for. The grantee has raised sufficient funds to have an independent public accountant perform an audit. We are continuing to monitor this matter.
- Allegation that a state humanities council was directing a subrecipient to involve a church in a proposed project. The subrecipient thought this was a violation of the church-state doctrine. The NEH General Council, with the limited information we had at the time, did not believe this particular situation violated the Constitution. The OIG has determined from a review of the facts provided that there was not a church-state constitution matter. Therefore, we closed our file.

CONTACTS DURING THIS PERIOD

We received one internal contact during this period and it was referred to the Office of Human Resources. Two contacts concerning grantees were received and our review

determined that no investigation was warranted. One contact was referred to the Office of General Council.

MATTERS REFERRED TO PROSECUTIVE AUTHORITIES

No new cases were referred for criminal prosecution.

HOTLINE AND PREVENTION ACTIVITIES

We maintain a local Hotline phone number, agency e-mail address, and an Internet address to provide additional confidentiality for those persons bringing matters to the attention of the OIG. We continue to issue agency-wide e-mail messages to NEH staff

informing them of violations that should be reported to the OIG. We also send e-mail messages several times during the year to inform NEH staff about the OIG operations. Posters advising staff to contact the OIG are displayed throughout the agency building.

ANONYMOUS E-MAIL

We have on the NEH Intranet and the Internet a system for staff, grantees, contractors, etc., to report

waste, fraud, abuse, and mismanagement in an anonymous manner.

SUMMARY OF INVESTIGATION ACTIVITY

Open at beginning of period	2
Matters brought to the OIG during the reporting period	4
Total investigative contacts	6
Closed or referred during the reporting period	5
Open at end of period	1

OTHER ACTIVITIES

INDIRECT COST RATE NEGOTIATIONS/REVIEWS

Grantees are entitled to recover total project costs, both direct and indirect. Indirect costs are those costs of an organization or institution that are not readily identifiable with a particular project or activity but are nevertheless necessary to the general operation of the organization or institution and the conduct of the activities it performs.

The cost of office supplies, general telephone, postage, accounting, and administrative salaries are types of expenses usually considered as indirect costs. In theory, all such costs might be charged directly; practical difficulties, however, preclude such an approach. Therefore, they

are usually grouped into a common pool(s) and distributed to those organizational or institutional activities that benefit from them through the expedient of an indirect cost rate(s).

Cognizant federal agencies approve rates after reviewing cost allocation plans submitted by grantees. The approved rates are generally recognized by other federal agencies.

During this period, we negotiated an indirect cost rate with one grantee.

<u>Grantee</u>	<u>Report Number</u>	<u>Date Issued</u>
Boston Athenaeum	OIG-03-01 (IDC)	12/06/02

PARTICIPATION ON THE EXECUTIVE COUNCIL ON INTEGRITY AND EFFICIENCY

The Executive Council on Integrity and Efficiency (ECIE) was established by the President in 1992 to coordinate and implement government-wide activities

to combat fraud and waste in federal programs and operations. OIG staff regularly attend ECIE meetings and provide information to the ECIE.

REGULATORY AND LEGISLATIVE REVIEWS

The Inspector General Act of 1978, as amended, requires the Office of Inspector General to review proposed legislation and regulations. The reviews are made to assess whether the proposed legislation or regulation (1) impacts on the economy and efficiency

of agency programs and operations, and (2) contains adequate internal controls to prevent and detect fraud and abuse. During this period we provided the ECIE with comments on various matters affecting the OIG community.

OIG INTERNET AND INTRANET

The OIG has listed several semiannual reports on the Internet. The reports are accessible through the NEH homepage and the Inspectors General homepage (<http://www.neh.gov/whoweare/OIG.html>).

To enhance the NEH staff's recognition of the OIG mission and responsibilities, we provide links to several other federal agencies such as the Office of Management and Budget, the General Accounting Office, the Office of Government Ethics, and the IGMET.

WORKING WITH THE AGENCY

In this period, OIG staff attended and engaged in various NEH meetings - panel meetings (where grant applications are reviewed by outside consultants), pre-council meetings (where program staff discuss panel review results with the chairman and his immediate staff), and the National Council meeting. In addition, the IG and Deputy IG attended the chairman's monthly policy group meetings. An OIG staff person attended

monthly NEH Employee Association meetings. The staff were also involved in the review of NEH administrative directives.

The Office of Inspector General contributes to the discussions; however, the office does not participate in policy making.

STRATEGIC PLAN

The OIG is currently revising our strategic plan.

TABLE I

REPORTING REQUIREMENTS

The Inspector General Act of 1978, as amended (Public Law 100-504), specifies reporting requirements for semiannual reports. The requirements are listed and cross-referenced to the applicable pages in this report.

<u>IG Act Reference</u>	<u>Reporting Requirements</u>	<u>Page</u>
Section 4(a)(2)	Regulatory and Legislative Reviews.....	*
Section 5(a)(1)	Significant Problems, Abuses, and Deficiencies.....	*
Section 5(a)(2)	Recommendations for Corrective Action	*
Section 5(a)(3)	Prior Significant Recommendations Unimplemented.....	*
Section 5(a)(4)	Matters Referred to Prosecutive Authorities.....	8
Section 5(a)(5)	Instances Where Information Was Refused or Not Provided.....	*
Section 5(a)(6)	List of Audit Reports Issued.....	2
Section 5(a)(7)	Summary of Significant Reports.....	3-5
Section 5(a)(8)	Audit Reports - Questioned Costs.....	*
Section 5(a)(9)	Audit Report - Funds To Be Put to Better Use.....	*
Section 5(a)(10)	Prior Audit Reports Unresolved.....	*
Section 5(a)(11)	Significant Revised Management Decisions.....	*
Section 5(a)(12)	Significant Management Decisions with which OIG Disagreed.....	*

* None this period

**TABLE II
INSPECTOR GENERAL-ISSUED REPORTS
WITH QUESTIONED COSTS**

	Number Of Reports	Questioned Cost	Unsupported Cost
A. For which no management decision has been made by the commencement of the reporting period.	- 0 -	\$ - 0 -	\$ - 0 -
B. Which were issued during the reporting period.	- 0 -	\$ - 0 -	\$ - 0 -
Subtotals (A+B)	- 0 -	\$ - 0 -	\$ - 0 -
C. For which a management decision was made during the reporting period.			
i. Dollar value of disallowed costs.	- 0 -	\$ - 0 -	\$ - 0 -
ii. Dollar value of costs not disallowed (grantee subsequently supported all costs).	- 0 -	\$ - 0 -	\$ - 0 -
D. For which no management decision has been made by the end of the reporting period.	- 0 -	\$ - 0 -	\$ - 0 -
E. Reports for which no management decision was made within six months of issuance.	- 0 -	\$ - 0 -	\$ - 0 -

**TABLE III
INSPECTOR GENERAL-ISSUED REPORTS
WITH RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE**

	Number Of Reports	Dollar Value
A. For which no management decision has been made by the commencement of the reporting period.	- 0 -	\$ - 0 -
B. Which were issued during the reporting period.	- 0 -	\$ - 0 -
C. For which a management decision was made during the reporting period.	- 0 -	\$ - 0 -
i. Dollar value of recommendations that were agreed to by management.	- 0 -	\$ - 0 -
ii. Dollar value of recommendations that were not agreed to by management.	- 0 -	\$ - 0 -
D. For which no management decision was made by the end of the reporting period.	- 0 -	\$ - 0 -

GLOSSARY OF AUDIT TERMINOLOGY

Questioned Cost - A cost that is questioned by the OIG because of an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds; because such cost is not supported by adequate documentation; or because the expenditure of funds for the intended purpose is unnecessary or unreasonable.

Unsupported Cost - A cost that is questioned because of the lack of adequate documentation at the time of the audit.

Disallowed Cost - A questioned cost that management, in a management decision, has sustained or agreed should not be charged to the government.

Funds Be Put To Better Use - Funds, which the OIG has disclosed in an audit report, that could be used more efficiently by reducing outlays, de-obligating program or operational funds, avoiding unnecessary expenditures, or taking other efficiency measures.

Management Decision - The evaluation by management of the audit findings and recommendations and the issuance of a final decision by management concerning its response to such findings and recommendations.

Final Action - The completion of all management actions, as described in a management decision, with respect to audit findings and recommendations. When management concludes no action is necessary, final action occurs when a management decision is made.

Source: Excerpt from Section 106(d) of the Inspector General Act Amendments of 1988 (P.L. 100-504).