

APPALACHIAN REGIONAL COMMISSION

INSPECTOR GENERAL'S

SEMIANNUAL REPORT

TO CONGRESS

OCTOBER 1, 1997 - MARCH 31, 1998



April 30, 1998

MEMORANDUM FOR THE FEDERAL CO-CHAIRMAN

SUBJECT: Semiannual Report to Congress

In accordance with the requirements of the Inspector General Act Amendments of 1988, Public Law 100-504, I am pleased to submit the semiannual report of the Office of Inspector General (OIG) for the period October 1, 1997, through March 31, 1998.

During this reporting period, 19 reports were issued, including 13 individual grant reviews, a survey of infrastructure project results, an evaluation of ARC's new financial management system, 2 J-1 visa waiver compliance reviews, and followup summaries in 2 instances. At the end of the reporting period, 23 grant reviews were in process. Recommendations in grant reviews were directed at improved accounting and financial systems and controls, including eligibility of expenditures and identification and support for matching contributions. During the reporting period, ARC management continued to emphasize timely followup and review of expired grants. This action resulted in management actions to deobligate about \$4 million during the reporting period, which included about \$136,000 applicable to cases noted in prior OIG reports.

An evaluation of ARC's new financial management system was completed. The evaluation disclosed that ARC's decision to bring accounting functions in-house has provided the Commission with more efficient and effective fiscal control and has enhanced overall financial management. Recommendations were made with respect to improving system functionality, especially reporting capabilities, obtaining OMB and Treasury clarification about ARC reporting responsibilities for nonexpenditure fund transfers and periodic evaluations of systems controls.

A survey of job creation attributable to 105 infrastructure projects approved between 1989 and 1993 disclosed that roughly twice as many jobs were created than were projected in the original project application estimates. For about 65 percent of the projects, job creation was substantially in excess of original estimates and job creation to date was limited in about 10 percent of the projects.

We participated with ARC management in a successful followup with J-1 visa waiver physicians who had not provided required information to ARC with respect to their employment status. During this reporting period, our field surveys did not disclose any serious problems related to noncompliance with program provisions; and we attributed this primarily to ARC and State agency actions to educate and monitor health care providers and participating physicians.

ARC management continued actions to improve grant implementation and administration, including the drafting of grantee guidance pertaining to key provisions of OMB guidance, including conditions reported in prior OIG reports. This guidance, which was provided in question and answer form,

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EXECUTIVE SUMMARY

During this reporting period, 19 reports were issued, including 13 individual grant reviews, a survey of infrastructure project results, an evaluation of ARC's new financial management system, 2 J-1 visa waiver compliance reviews, and followup summaries in 2 instances. At the end of the reporting period, 23 grant reviews were in process. Recommendations in grant reviews were directed at improved accounting and financial systems and controls, including eligibility of expenditures and identification and support for matching contributions. During the reporting period, ARC management continued to emphasize timely followup and review of expired grants. This action resulted in management actions to deobligate about \$4 million during the reporting period, which included about \$136,000 applicable to cases noted in prior OIG reports.

An evaluation of ARC's new financial management system and related accounting and systems controls was completed during this reporting period. The evaluation disclosed that the financial management system was generally meeting intended purposes, provided more efficient and effective fiscal control than was achieved through a service bureau, and enhanced overall financial management. Conditions and recommendations were noted as respects improving system functionality, especially reporting capabilities, obtaining OMB and Treasury clarification about ARC reporting responsibilities for nonexpenditure fund transfers and periodic evaluations of systems controls. Management responded positively to the recommendations.

A survey of job creation attributable to 105 infrastructure grants approved between 1984 and 1993 disclosed that roughly twice as many jobs were created than were projected in the original project application estimates. Grantee information and field observations indicated that, for about 65 percent of the grants, job creation was substantially in excess of original estimates and job creation to date was limited for about 10 percent of the grants. The survey, which emphasized industrial site improvement projects for which ARC contributed funds (including water and sewer infrastructure and access roads), concluded that the projects produced about 28,000 jobs at an ARC investment of about \$1,000 per job. Additional benefits resulting from retention of jobs were also reported by grantees. The results of this survey were essentially similar to a prior survey of 41 other industrial site development grants.

We continued to work with first-time and smaller grantees with respect to the implementation of practical accounting and financial systems and controls sufficient to ensure compliance with grant agreements, identification of eligible costs, maintenance of records and preparation of reports. Primary areas in need of improvement with respect to grantee financial operations included identification and support of matching contributions and program expenditures.

We participated with ARC management in a successful followup with J-1 visa waiver physicians who had not provided required information to ARC with respect to their employment status. During this reporting period, our field surveys did not disclose any serious problems related to noncompliance with program provisions; and we attributed this primarily to ARC and State agency actions to educate and monitor health care providers and participating physicians.

ARC management continued actions to improve grant implementation and administration including the drafting of grantee guidance pertaining to key provisions of OMB circulars, including conditions reported in prior OIG reports. This guidance, which is in question and answer form, deals with financial management, reporting, and audit requirement issues and should be of particular benefit

PURPOSE AND REQUIREMENTS OF THE OFFICE OF INSPECTOR GENERAL SEMIANNUAL REPORT

The Inspector General Act of 1978 requires the IG to keep the Federal Co-Chairman and Congress fully and currently informed about problems and deficiencies in the Commission's operations and the necessity for corrective action. In addition, the Act specifies that semiannual reports will be provided to the Co-Chairman by April 30 and October 31 and to Congress 30 days later.

The Co-Chairman may transmit comments to Congress along with the report but may not change any part of the report. The specific requirements prescribed in the Act, as amended (Public Law 100-504), are listed below.

Reporting Requirements

Section 4(a)(2)	Review of legislation and regulations	Page 7
Section 5(a)(1)	Problems, abuses, and deficiencies	Page 3
Section 5(a)(2)	Recommendations with respect to problems, abuses, and deficiencies	Page 3
Section 5(a)(3)	Prior significant recommendations not yet implemented	*
Section 5(a)(4)	Matters referred to prosecutive authorities	*
Section 5(a)(5) and 6(b)(2)	Summary of instances where information was refused	*
Section 5(a)(6)	Listing of audit reports showing number of reports and dollar value of questioned costs	App A
Section 5(a)(7)	Summary of each particularly significant report	**
Section 5(a)(8)	Statistical table showing number of reports and dollar value of questioned costs	App B
Section 5(a)(9)	Statistical table showing number of reports and dollar value of recommendations that funds be put to better use	App C
Section 5(a)(10)	Summary of each audit issued before this reporting period for which no management decision was made by end of the reporting period	*
Section 5(a)(11)	Significant revised management decisions	*
Section 5(a)(12)	Significant management decisions with which the Inspector General disagrees	*

* None.

** See references to Sections 5(a)(1) and 5(a)(2) for discussion of significant reports.

I. INTRODUCTION

The Inspector General Act Amendments of 1988 (P.L. 100-504) provided for the establishment of an Office of Inspector General (OIG) at 30 designated Federal entities, including the ARC. The ARC OIG became operational on October 1, 1989, with the appointment of an IG and provision of budgetary authority for contracted audit and/or investigation activities.

II. BACKGROUND

A. APPALACHIAN REGIONAL COMMISSION

The ARC was established by the Appalachian Regional Development Act of 1965 (P.L. 89-4). The Act authorizes a Federal/State partnership designed to promote long-term economic development on a coordinated regional basis in the 13 Appalachian States. The Commission represents a unique experiment in partnership among the Federal, State, and local levels of Government and between the public and private sectors. It is composed of the Governors of the 13 Appalachian States and a Federal representative who is appointed by the President. The Federal representative serves as the Federal Co-Chairman with the Governors electing one of their number to serve as the States' Co-Chairman.

- Through joint planning and development of regional priorities, ARC funds are used to assist and encourage other public and private resources to address Appalachia's unique needs. Program direction and policy is established by the Commission (ARC Code) by the vote of a majority of the State members and the affirmative vote of the Federal Co-Chairman. Emphasis has been placed on highways, infrastructure development, business enterprise, and human resources programs.
- Administratively, the Office of the Federal Co-Chairman, with a staff of 10, and the Commission, with a staff of 51, are responsible for ARC operations. The States maintain an Office of States' Representative (3 persons) that has primarily liaison responsibilities. All personnel are located in Washington, DC. The Commission staff's administrative expenses, including salaries, are funded jointly by Federal and State funds; the States' Representative staff is funded entirely by the States; and the Federal Office staff is funded entirely from Federal funds.
- The Commission's appropriation for FY 1998 is \$170 million, which is divided approximately \$102.5 million for highway projects, \$63.9 million for non-highway projects, and \$3.6 million for administrative expenses. ARC is authorized through its current appropriation. Also, the Department of Transportation and Related Agencies Appropriation Act for Fiscal Year 1998 (Public Law 105-66) appropriated \$300 million for carrying out the provisions of section 1069(y) of Public Law 102-240 relating to the construction of, and improvements to, corridors of the Appalachian Development Highway System (ADHS). The funding will be distributed among the states with unfinished ADHS segments as determined by ARC.
- Program funds are distributed to State and local entities in line with an allocation formula intended to provide fair and reasonable distribution of available resources. ARC staff have

8 percent, for all other activities (training, equipment, space, supplies, etc.). The OIG funding level represents about .24 percent of the total funds available to the Commission.

Initial OIG operations included authorization for an Inspector General and a Confidential Assistant. A senior auditor was employed in the latter half of FY 1991; no additional staff have been employed. Grant review activities will continue to emphasize use of contracted services (e.g., independent public accounting firms or other OIG offices) supplemented by programmatic and performance reviews directed by OIG staff. Investigative assistance is provided by other OIG offices on an as-needed basis. This approach has been deemed the most appropriate to date in view of the nature of ARC operations and limited resources. However, we would welcome initiatives that would facilitate sharing of investigative resources in order to strengthen this aspect of OIG operations.

III. OIG ACTIVITY

A. AUDITS

During the reporting period, 19 reports were issued, including 13 individual reviews, 2 program surveys, 2 J-1 visa waiver compliance reviews, and 2 followup summaries. At the end of the reporting period, 23 grant reviews were in process. The division of OIG resources results in audit work being performed by a combination of permanent and contractor staff. Emphasis continues to be placed on surveys of ARC operations and programs, completion of grant audits, audit planning, and audit resolution and followup.

During the term of the OIG operations at ARC, various recommendations, based on audit testing, have been made to ARC management with respect to improving operations in such areas as accountability, financial management, fund obligations and deobligations based on project activity, implementation of cost principles, and audit followup. Programmatic issues, with respect to grant administration, project results, and internal control systems, have been addressed.

OIG followup tests and reviews of statistical information have reflected positive ARC actions to address these issues and resulting improvements in program operations. For example, timely use of funds and project closings continue to be emphasized; and the number of funded projects with large unobligated balances has been substantially reduced. ARC conferences, training, and seminars continue to emphasize accountability, financial management systems, and allowable costs. Additionally, ongoing ARC actions, such as revisions of accounting systems and service agreements; strategic planning, including assessment of appropriate internal and external performance measures; and issuance of revised policies and procedures and guidance to grantees, are in line with OIG recommendations and executive and legislative initiatives to improve Government operations.

The ARC OIG will continue to address these issues, including periodic followup on the extent of actions initiated and results obtained, and, as noted below, will report on issues needing continued attention.

- Of particular significance was ARC's continued emphasis on identifying and closing old and inactive grants, including substantial deobligations to ensure that unused funds are made available for other economic development activities in the Appalachian Region. ARC actions on contracts/grants resulted in recoveries of approximately \$4 million from project

- New employment objectives were noted as met in 2 cases, 12 grantees reported achieving 50 to 100 percent of objectives, and 8 responses indicated accomplishment of 20 to 50 percent of employment objectives.
- In 4 cases, the grantees reported little or no job creation to date; and in 3 cases, achievement of less than 20 percent of job creation goals were noted. In these cases, the grantees indicated that development efforts were continuing and positive results were expected in most cases. We will followup to ascertain the status of these projects.
- In 4 instances, project completion had been delayed by various factors, including late starts, litigation about faulty construction, and bad weather. In each case, the grantee indicated that a successful outcome would be achieved when the project was completed. We will followup to ascertain the status of these projects.
- In 62 cases, responses noted that additional job creation was expected within the next 2 years. An analysis of the information provided indicated that the applicants had estimated creation of about 15,000 jobs when submitting grant requests and that about 30,000 jobs had been created in the project areas since grant approval. Based on project funding, the cost per estimated job noted in grant applications was approximately \$10,000, of which the ARC portion was about \$2,000 per job; and the cost of each reported job creation was about \$5,000, including an ARC portion of \$1,000 per job.

With respect to project results, we did not request information about the extent of job retention resulting from the projects. However, information supplied by some grantees identified substantial job retention, which we concluded indicated that job retention was an important project result.

Grantee comments, where provided, unanimously cited the importance of the ARC project approval and funding as critical for development in the applicable location; and in many cases, the questionnaire was annotated to identify the number of jobs that were retained because of project implementation. For example, in one case, a grantee, while noting creation of 199 new jobs, also noted an overall net loss of 226 jobs from 12 businesses between 1993 and 1997 but a retention of 2,393 jobs that would have been lost without the project.

Grantees also noted, especially with respect to sewer and water projects, that these projects, in addition to assisting with commercial economic development, were essential for residential development and improvement, including assistance to poverty population areas.

- We conducted J-1 visa waiver program reviews in two States and disclosed that participating physicians were complying with program requirements to provide 40 hours of primary care per week in medical shortage or underserved areas. We also participated with ARC management in a successful followup effort to obtain required information from participating J-1 visa waiver physicians about their employment status. Such information is necessary in connection with ARC and State agency responsibilities for ensuring the program is implemented effectively.

Of particular importance is maintaining the flexibility of the audit plan to address changing needs and priorities. Coordination with ongoing ARC efforts to implement an entity-wide strategic plan are considered an important element of planning, and discussions with ARC management have identified several areas for review.

The OIG's strategies and objectives for the next 5 years are defined in a strategic plan. The FY 1998 Annual Plan provides the operational details for OIG activities planned during FY 1998 to implement this strategic plan. We expect to revise this strategic plan periodically until our experiences validate our planning assumptions and we have achieved a comfort level with how we have programmed activities over this extended time period.

FY 1998 audit work includes about 40 individual grant audits in the Appalachian States; additional followup on grants with completed budget periods, grant extensions, and project results; and tests of the J-1 visa waiver program. Continued emphasis will be placed on audit followup and corrective action plans, including working with agency management to address open issues and achieve audit resolution and closure.

In order to maximize use of available resources directed at reviewing ARC activities, emphasis will continue to be placed on nonstandard reporting formats including memorandum, letter, and survey reports. Although such reporting formats reduce the time and resources necessary for review completion, the results and information included in such reports is based on evidence and supporting documentation consistent with generally accepted auditing standards.

V. OIG HOTLINE

A regionwide toll-free Hotline was previously established to enable direct and confidential contact with the ARC OIG in line with governmental and longstanding OIG initiatives as identified in the IG Act of 1978 to afford opportunities for identification of areas subject to fraud, waste, or abuse. Efforts continue to publicize the hotline by notifications to contractors and grantees, and field visits evaluate the extent to which employees were made aware of this system. However, contacts with the ARC OIG relative to public complaints or concerns continue to be primarily received through ARC staff, on regular OIG phone lines, or from other OIG offices.

Also, numerous hotline calls were received with respect to matters for which other agencies have jurisdiction. This resulted primarily from the ARC OIG hotline apparently being the first such OIG listing in some telephone directories, resulting in ARC OIG being contacted by citizens who did not know the appropriate agency for handling their concerns. The ARC OIG facilitated the complaint process by identifying the applicable agency based on complainant information and providing the correct OIG hotline number.

VI. LEGISLATIVE AND REGULATORY REVIEW

Primary efforts in this area continued to be related to potential legislative initiatives with respect to OIG operations. The ARC OIG continues to support legislation that would provide improved protections for IGs, including designated and career IGs, by consideration of alternatives such as removal for cause criteria and term limits. Also, the ARC OIG continues to support extension of the Program Civil Fraud Penalties Act to include designated entities.

APPENDIX A

SCHEDULE OF REPORTS ISSUED OCTOBER 1, 1997 TO MARCH 31, 1998

Report No.	Entity and Title	Program Dollars or Contract/Grant Amount	Questioned/Unsupported Costs*	Funds to Better Use**
98-1(H)	Jacksonville State University Manufacturing Technology Consortium	\$ 144,000		
98-2(H)	Auburn University Leadership for Economic Development	200,000	\$ 2,742	
98-3(H)	ARC Financial Management System	393,000		
98-4(H)	Infrastructure Job Creation Survey	30,317,000		
98-5(H)	Tri-County Technical College Equipment Utilization	200,000		
98-6(H)	Enterprise Development, Inc. of South Carolina--Incubator	250,000		
98-7(H)	Frostburg State University--Microscope Facility	55,710	370	
98-8(H)	Frostburg State University--High Performance Computing Equipment	156,372	40,858	
98-9(H)	Frostburg State University--Business School Technology	62,500	13,740	
98-10(H)	Marshall University--Health Care Project	95,435	2,500	
98-12(H)	Frostburg State University--Distance Learning	68,465	10,686	
98-15(H)	Kemper County, Mississippi--Lake Access Road	113,384		
98-16(H)	Kemper County, Mississippi--Solid Waste Landfill	75,000	54,984	
98-17(H)	Pennsylvania Technical Assistance	350,000	27,858	\$ 38,198
98-18(H)	Tennessee Technical Assistance	210,000		
98-20(H)	Tennessee Quality Award--Business Development	150,000		9,377
98-22(H)	Georgia Tech Research Corporation--Demonstration Project	199,470		
98-28(H)	J-1 Visa Waiver Program--Georgia			
98-35(H)	J-1 Visa Waiver Program--Tennessee			
TOTALS		\$ 33,040,336	\$ 153,738	\$ 47,575

* A cost the Office of Inspector General has questioned because of an alleged violation of law, regulation, contract, or other agreements governing the expenditure of funds; such cost is not supported by adequate documentation; or the expenditure of funds for the intended purpose is unnecessary or unreasonable. Includes required matching contributions.

** Funds the Office of Inspector General has identified in an audit recommendation that could be used more efficiently by reducing outlays, deobligating program or operational funds, avoiding unnecessary expenditures, or taking other efficiency measures, such as timely use of funds.

**SCHEDULE OF AUDIT REPORTS WITH
RECOMMENDATIONS THAT FUNDS BE PUT TO BETTER USE**

	No. of Reports	Dollar Value (\$ in thousands)
A. For which no management decision was made by the commencement of the reporting period	-	-
B. Which were issued during the reporting period	<u>2</u>	\$ <u>48</u>
Subtotals (A + B)	2	\$ 48
C. For which a management decision was made during the reporting period	-	-
(i) dollar value of recommendations that were agreed to by management	-	-
--based on proposed management action	1	\$ 136 ^{1/}
--based on proposed legislative action	-	-
(ii) dollar value of recommendations that were not agreed to by management	-	-
D. For which no management decision has been made by the end of the reporting period	2	\$ 48
E. Reports for which no management decision was made within 6 months of issuance	-	-
^{1/} Includes continued management action to resolve issues for which management decisions were previously made.		

