
**APPALACHIAN REGIONAL COMMISSION
OFFICE OF INSPECTOR GENERAL
AUDIT OF GRANT AWARD**

**Southeast Educational, Inc.
Tennessee Appalachian Center for Higher Education Project
Knoxville, Tennessee**

**Project Number: TN-15808
June 2012**

**Prepared by
Leon Snead & Company, P.C.**



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June 19, 2012

Appalachian Regional Commission
Office of the Inspector General
1666 Connecticut Avenue, N.W.
Washington, D.C. 20009

Leon Snead & Company, P.C. has completed an audit of grant number TN-15808 awarded by the Appalachian Regional Commission (ARC) to the SouthEast Educational, Inc. (SEED). The audit was performed to assist the Office of the Inspector General in carrying out its oversight of ARC grant activities.

The primary objective of the audit was to determine if program funds were managed in accordance with the ARC and federal terms and requirements; grant funds were expended as provided for in the ARC approved budget; internal grant guidelines and internal controls were operating effectively; accounting and reporting requirements were implemented in accordance with generally accepted accounting principles and the goals and objectives of the grant were met.

The audit questioned costs totaling \$39,194 for indirect cost charges (\$38,627) and travel costs (\$567), and identified two other issues that need to be addressed to improve the financial management of the ARC grant. The first one deals with advance payments made to the grantee and the second deals with payments made to consultants and compensation to the SEED staff. In addition, the audit determined that SEED was making progress on achieving the goals of the project. A detailed discussion of the issues is presented in the "Results of Review" section of the report.

A draft report was provided to SEED on May 10, 2012. The Executive Director for SEED provided a response to the report on June 12, 2012, addressing our audit recommendations. These comments are included in their entirety in Appendix I.

Leon Snead & Company appreciates the cooperation and assistance received from the SEED and ARC staff during the audit.

Sincerely,

Leon Snead & Company, P.C.
Leon Snead & Company, P.C.

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Background

Leon Snead & Company, P.C. completed a review of grant number TN-15808 awarded by the Appalachian Regional Commission (ARC) to the SouthEast Educational, Inc. (SEED). The review was made at the request of the ARC, Office of the Inspector General, to assist the office in its oversight of ARC grant funds.

SEED is a non-profit organization located in Knoxville, Tennessee, which was established to assist school systems in developing programs to encourage and motivate students to continue in educational programs beyond secondary school. A board of directors consisting of nine individuals governs the organization. SEED had only two employees (the executive director and the associate director) during the period covered by our review; however, the associate director left SEED prior to the start of our review.

The grant was awarded in September 2007, to provide funding for the Tennessee Appalachian Center for Higher Education Project (TnACHE) to address the lack of opportunity for youth in Appalachian Tennessee. TnACHE works to increase the high school graduation and college-going rates in the region. The initial grant award was \$333,102, but subsequent amendments increased the ARC funding to \$1,212,867. The grant requires matching funds of \$466,000. The status of the grant, as of January 31, 2012, is summarized below.

Funding Source	Budget	Reported Expenditures	Balance
ARC	\$1,212,867	\$ 865,589	\$347,278
Local	<u>466,000</u>	<u>517,850</u>	(51,850)
Totals	\$1,678,867	\$1,383,439	-

As noted above, SEED had a grant balance of \$347,278 as of January 31, 2012, and it had exceeded its matching requirement. The grant period ends September 30, 2013.

Objectives, Scope, and Methodology

The review objectives were to determine whether: (1) program funds were managed in accordance with the ARC and federal grant terms and requirements; (2) grant funds were expended as provided for in the approved budget; (3) internal grant guidelines and best practices, including program (internal) controls, were appropriate and operating effectively; (4) accounting and reporting requirements were implemented in accordance with generally accepted accounting principles (or other applicable accounting and reporting requirements); and (5) the goals and objectives of the grant were met.

We reviewed the documentation provided and interviewed SEED's executive director to obtain an overall understanding of the project, the accounting process, and operating procedures. We reviewed the Requests for Advance or Reimbursement submitted to ARC and a sample of costs charged to the project to determine whether the charges were properly supported and allowable. In that regard, we focused the testing on expenditures for the two-year period of February 1, 2010 through January 31, 2012. The total reported expenditures for that period were \$271,262.

We reviewed SEED's administrative procedures and related internal controls to ensure they were adequate to manage and account for the ARC funds. In addition, we reviewed the most recent financial statements audit report (including the related report on internal controls) to determine whether there were any issues that affected the ARC grant.

As a basis for determining whether the costs charged to the grant were allowable and whether SEED had complied with applicable Federal requirements, we used the provisions of the grant agreement, applicable Office of Management and Budget Circulars, and the relevant parts of the ARC Code. The review was performed in accordance with the *Government Auditing Standards*. The fieldwork was performed at SEED's office in Knoxville, Tennessee, during the period of March 26-28, 2012.

Overall, SEED's accounting and financial management procedures and related internal controls need to be improved to effectively manage ARC grant funds. In that regard, the most recent financial statement audit, which covered the year ended December 31, 2009, identified several material weaknesses regarding SEED's accounting and financial management processes. The report, dated June 10, 2011, states that SEED did not engage a qualified accountant to prepare its financial statements and accordingly, the auditor has prepared such financial statements. The report concluded that SEED's auditor cannot be part of the internal control over financial reporting, and financial statement preparation by the auditor does not compensate for this material weakness. The report identified other material weaknesses regarding bank reconciliations, budget preparation and monitoring, board of directors' authorizations of major expenditure and approval of SEED budgets, and the preparation of requests for advances. According to the SEED executive director, those weaknesses will be addressed and corrected.

We identified questioned costs totaling \$39,194 for indirect cost charges (\$38,627) and travel costs (\$567), and identified two other issues that need to be addressed to improve the financial management of the ARC grant. In addition, we determined that SEED was making progress on achieving the goals of the project. The questioned costs, the areas needing improvement, and our recommended corrective actions are discussed in the Results of Review section of the report.

RESULTS OF REVIEW

A. Questioned Indirect Costs

We questioned the entire \$38,627 charged to the grant for indirect costs during the period February 1, 2010 through January 31, 2012, because the charges were not adequately supported.

2 CFR, Part 230, Appendix A, Section E.2.b. states, "...A non-profit organization which has not previously established an indirect cost rate with a Federal agency shall submit its initial indirect cost proposal immediately after the organization is advised that an award will be made and, in no event, later than three months after the effective date of the award...."

Unsupported Indirect Cost Rate - SEED computed indirect cost charges totaling \$28,611 for 5 of the 6 Requests for Advance or Reimbursement (SF-270) reviewed by applying a 15 percent rate to the total direct costs for the respective periods. Although SEED officials stated that the 15 percent rate had been authorized by ARC, there was no documentation showing the basis for the 15 percent rate or that it had submitted an indirect cost proposal to its cognizant organization for approval of an indirect cost rate.

Unsupported Indirect Cost Computation - The expenditures on the SF-270 for June 30, 2010, included indirect costs of \$10,016, which exceeded the amount based on the 15 percent rate (15% of \$41,893 = \$6,284) by \$3,732. SEED officials could not explain how the \$10,016 charge was computed.

Recommendation

SEED should submit an indirect cost proposal to its cognizant organization for approval of an indirect cost rate. Upon approval of an indirect cost rate, the charges to the grant should be adjusted.

Grantee Response

SEED stated in its response that its indirect cost rate was discussed via telephone with the ARC Education Manager, who agreed with the indirect cost rate based upon a written justification prepared by the SEED Executive Director. In addition, SEED stated that it will request a written approval letter from the ARC Education Manager and it will review the June 30, 2010, indirect cost charges and discuss the results with the ARC Education Manager.

Reviewer's Comments

ARC will determine whether the proposed or completed actions identified in the grantee's response are adequate to consider the recommendation resolved and implemented, or whether additional information or actions are needed.

B. Questioned Travel Costs

We questioned travel costs of \$567 because the information on the travel voucher was not consistent with the supporting receipts and other documentation.

The employee's claim for travel expenses indicated that the employee traveled from Knoxville, Tennessee to Decatur, Alabama on March 23, 2010 and returned March 31, 2010. Subsequent to our exit conference, SEED provided a revised claim form and itinerary, which indicated that the claim actually covered a trip to Atlanta, Georgia, and three trips to locations in Tennessee. However, the information on the revised claim form was not consistent with other documentation, as follows:

- The claim form showed that the last date of travel was March 29, but the rental car receipt submitted with the claim showed that the car was not returned until March 31.
- The employee's time records did not include charges to the ARC grant from March 25-28, although the rental car receipt included charges for those dates.
- The itinerary showed that the employee met with a representative of Eastman Chemical on March 26. It was not clear how this meeting was related to the ARC grant and, as noted above, the employee's time record did not include any charges to the ARC grant for that date.

Recommendations

SEED should:

1. Provide justification for the amounts charged to the ARC grant, which addresses the issues identified in the finding.
2. Reimburse ARC for any charges that ARC determines to be unallowable.
3. Establish controls to ensure that claims for travel expenses are accurate and are properly reviewed before payment.

Grantee Response

SEED stated in its response that it agrees that the travel reimbursement form in question lacked sufficient detail and that the travel should have been broken out into individual trips rather than multiple trips on one reimbursement form. In addition, SEED stated that: (1) justification and clarification have been provided by the employee; (2) no reimbursement to the ARC is necessary, as all costs are considered allowable; and (3) greater scrutiny of travel reimbursement forms is now in place and each trip will require a separate travel reimbursement form.

Reviewer's Comments

ARC will determine whether the proposed or completed actions identified in the grantee's response are adequate to consider the recommendations resolved and implemented, or whether additional information or actions are needed.

C. Requests for Advances

The Federal regulations (2 CFR, Part 215.22) require grantees that are paid in advance to minimize the time elapsing between the receipt of advance funds and the use of those funds. The regulations further state that cash advances shall be limited to the minimum amount needed to meet immediate cash requirements to carry out the purpose of the project. We identified deficiencies in SEED's preparation of Requests for Advance or Reimbursement (SF-270) that contributed to excessive advances and significant ARC funds on hand during the grant period.

ARC requires SEED to submit a SF-270 every four months. Because the ARC grant is its primary source of funding, SEED elected to receive advances rather than reimbursements for actual costs in order to ensure sufficient operating funds to cover grant expenses. We identified the following deficiencies in the preparation of the SF-270s:

1. The SF-270 provides a formula for computing the advance request. We found that the computation was incorrect on the last three forms submitted (June 2011, October 2011, and February 2012) because the amounts reported as "Federal payments previously requested" were incorrect. For example, our re-computation of the SF-270 dated October 31, 2011, showed that the advance requested was excessive by over \$12,000, as follows:

Line	Description	Per SF-270	Per Audit	Difference
g	Federal share of estimated cumulative expenditures through end of next reporting period (YTD expenditures plus forecasted expenditures for the next period)	\$892,218	\$892,218	-
h	Federal payments previously requested	839,893	851,922	-
i	Federal share now requested (Line g minus Line h)	\$ 52,325	\$ 40,296	\$12,029

Line h can be computed from the prior SF-270 (Line h: Federal payments previously requested plus Line i: Federal share now requested). However, SEED erroneously reported Year-to-Date Expenditures on this line on the last three SF-270s submitted. We noted the amounts reported on Line h on the SF-270s submitted prior to June 2011 were correct.

2. There was no documentation supporting the computation of the "Forecast" of expenditures used in the computation of the advance request. We found that the forecasted expenditures were significantly higher than the actual expenditure for five of the six SF-270s reviewed. For example, forecasted grant expenditures used to compute the advance request for the period October 1, 2011 through January 31, 2012, were \$61,813, while the actual expenditures for that period were only \$49,783.

Overall, these deficiencies resulted in excessive advances and excessive ARC funds on hand. The most recent financial statement audit report stated, "...As of December 31, 2009, [SEED] has received more funds than expended by \$177,950...." The report also identified deficiencies in the preparation of Requests for Advances.

While it appears that progress has been made to reduce excessive ARC funds on hand, the problem still exist. For example, funds of \$35,893 were on hand as of January 31, 2012; however, on February 29, 2012, SEED requested and received an advance of \$40,825 to cover expenses for the period February 1 through May 31, 2012; bringing funds available for expenses during that period to \$76,718; however, SEED's forecasted expenditures for that period were only \$40,825.

Recommendation

SEED should establish controls to ensure that Requests for Advances or Reimbursement are prepared accurately, that the computation of forecasted expenditures is adequately documented, and that advance requests are not excessive.

Grantee Response

SEED stated in its response that it agrees that there was an incorrect computation on the SF-270, which resulted in requesting an excessive advance payment and resulted in having too much cash on hand. In addition, SEED stated that: (1) no advance payment request will be made for June 1, 2012 - September 30, 2012; and (2) beginning in June 2012, a CPA firm will review future advance requests.

Reviewer's Comments

ARC will determine whether the proposed or completed actions identified in the grantee's response are adequate to consider the recommendation resolved and implemented, or whether additional information or actions are needed.

D. Personnel Costs

Personnel costs charged to the ARC grant included payments to consultants and compensation to the SEED staff. We found that there was no documentation showing the rates paid to those individuals were authorized.

SEED did not have formal written agreements with its consultants specifying the rate of compensation or the services to be provided. As such, we could not verify the basis for the daily rates of \$300 and \$400 on the six invoices totaling \$10,669 from three consultants included in our sample.

In addition, there was no documentation, such as the board of directors' approval, establishing the compensation for the executive director and the associate director. Annual salary charges to the ARC grant in 2010 were \$30,000 for each employee, based on a rate of \$500/day and an average of 5 days/month. The annual salaries for the ARC grant were increased to \$31,500 for 2011. There was no documentation showing the basis for the annual salary allocations.

SEED's most recent financial statement audit report recommended that the board of directors consider requiring major expenditures to be presented to the board for approval. In that regard, we noted that the consultant fees and personnel costs comprise significant expenditures on the ARC grant.

Recommendations

SEED should:

1. Obtain written contracts with all consultants. Those contracts should identify the scope of work, rate of compensation, and additional costs (such as travel) that are reimbursable. The proposed contracts should be provided to the board of directors for approval before they are signed.
2. Implement procedures to obtain the board of directors' approval of the compensation for the SEED staff.

Grantee Response

SEED stated in its response that:

1. Contracts are now being prepared for all consultants, which identify the scope of work, rate of compensation and any additional costs that are reimbursable and that a board meeting is scheduled to approve the contract language and rates.
2. At the board meeting, the compensation rate for the SEED staff will be on the agenda for a vote.

Reviewer's Comments

ARC will determine whether the proposed or completed actions identified in the grantee's response are adequate to consider the recommendations resolved and implemented, or whether additional information or actions are needed.

Appendix I
Grantee Response



SouthEast

EDUCATIONAL, INC

To: Whom it May Concern

From: Terry L. Lashley, Ph.D. *Terry Lashley*
Executive Director
SouthEast Educational, Inc.
Knoxville, TN 37922

Re: Response to Audit Questions

Date: June ^{12, 2012} 22, 1012

Accompanying this memo is a two-page response to questions as requested by Leon Snead and Company, PC.

Please let me know if you need more information.

Response to Results of Review Questions

I. Questioned Indirect Costs

Unsupported Indirect Cost Rate – The TnACHE-SEED Executive Director addressed this concern via telephone with the ARC Education Manager, Dr. Jeffrey Schwartz. Dr. Schwartz stated that he did agree with the increase in the indirect rate based upon a written justification prepared by the TnACHE-SEED Executive Director and then Dr. Schwartz passed the approval paperwork along at the ARC for processing. Dr. Schwartz recommended “spending out” the excess indirect costs by not requesting additional advances in upcoming reporting periods.

Resolution:

1. The TnACHE-SEED Executive Director will request a written approval letter from the ARC Education Manager.

Unsupported Indirect Cost Computation

Resolution:

1. The TnACHE-SEED Executive Director will review the June 30, 2010 indirect charges and discuss the results with the ARC Education Manager, Dr. Jeffrey Schwartz.

II. Questioned Travel Costs

TnACHE-SEED agrees that this travel reimbursement form in question lacked sufficient detail and travel should have been broken out into individual trips rather than multiple trips on one reimbursement form.

TnACHE-SEED believes that this question was answered by Mr. English via email. The travel costs for Mr. Chuck English were re-submitted with additional explanations. Mr. English provided a more detailed explanation which was forwarded to Leon Snead and Company, PC, however, if additional information is needed, it will be requested from him.

In terms of the employee time, Mr. English did not charge time for all work within this period, as his compensation was capped at \$30,000 per year and both Mr. English and Dr. Lashley consider themselves part-time exempt.

Also the business trip spanned a weekend because the car was used until Friday and then needed again on Monday morning before the Enterprise opened.

Resolution:

1. Justification and clarification have been provided by Mr. English.
2. No reimbursement to the ARC is necessary as all costs are considered allowable.
3. Greater scrutiny of travel reimbursement forms is now in place and each trip will require a separate travel reimbursement form.