

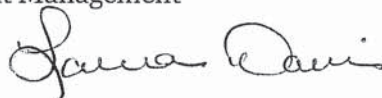
OFFICE OF INSPECTOR GENERAL

MEMORANDUM

Date: July 13, 2012

To: James A. Leach, Chairman
Carole Watson, Deputy Chairman
Adam Wolfson, Assistant Chairman for Programs
Jeff Thomas, Assistant Chairman for Planning and Operations
Steve Ross, Director ~ Office of Challenge Grants
Susan Daisey, Director ~ Office of Grant Management

From: Laura Davis, Acting Inspector General



Subject: Accounting System Survey Memorandum Report: OIG-12-02 (TS)
American Association for State and Local History
Nashville, TN

As discussed in the attached report, the NEH-OIG assisted the Institute of Museum and Library Services (IMLS) with an accounting system survey of the American Association for State and Local History (the "Association"). The Association recently suffered a major fraud (perpetrated by the prior accountant) and currently administers both IMLS and NEH grants. The purpose of our survey was to assist IMLS in determining whether the Association adopted corrective measures and improved its financial management system and related controls.

Conclusion

The Association's Board and management are working closely with IMLS, NEH-OIG, and its outside auditor to strengthen the organization's financial management system and related controls. During the most recent Board meeting, a new *Finance Policies and Procedures* manual was approved with an effective date of July 1, 2012. Once these new procedures and the recommendations resulting from this accounting system survey are implemented, we believe that the Association's upgraded accounting system, management controls, Governance oversight, and formalized policies/procedures should allow the nonprofit to sufficiently manage and account for Federal grant funds moving forward. As the Association undergoes this transitional period, we recommend that the organization be notified and treated as a high-risk entity¹.

¹ As defined by OMB Circular A-110, Subpart B-Pre-Award Requirements_.14 Special award conditions.

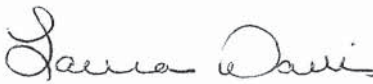
OFFICE OF INSPECTOR GENERAL

MEMORANDUM

{E-MAIL ONLY}

Date: July 13, 2012

To: Michael Jerger, IMLS Chief Financial Officer
Nancy Weiss, IMLS General Counsel

From: Laura Davis, Acting Inspector General 

Subject: Accounting System Survey: OIG-12-02(TS)
American Association for State and Local History (AASLH)
Nashville, TN

Background

The National Endowment for the Humanities Office of Inspector General (NEH-OIG) agreed to perform an accounting system survey of the American Association for State and Local History (AASLH) due to 1) a recent fraud that transpired at AASLH and the Institute of Museum and Library Services (IMLS) currently lacks an Inspector General's Office; 2) repeated errors noted with recent SF-270 reimbursement requests submitted to the IMLS; and 3) NEH also provides this non-profit organization with Federal grant funding. Since AASLH management recently instituted sweeping changes to include the hiring of a new fiscal officer and the implementation of updated policies and procedures, this survey was conducted to determine the adequacy of the organization's recently revised fiscal policies/procedures and internal controls.

IMLS has three active grants/cooperative agreements with AASLH totaling approximately \$3.1 million. Additionally, NEH has awarded two challenge grants (CH-20734-01: \$246,000 and CH-50594-09: \$118,000) and one digital humanities start-up grant (HD-50420-08: \$35,000) to this organization. The Association represents a Section 501(c)(3) tax-exempt organization and receives a significant portion of its annual revenues from Federal grant awards.

Scope

Our efforts were limited to a review of certain documents provided by IMLS [AASLH internal reconciliation of IMLS grant expenditures report, sample of the outstanding SF-270 reimbursement requests, and recent correspondence between IMLS and AASLH], review of AASLH's newly drafted accounting policies and procedures, review of prior OMB Circular A-133 audit reports (FY2008 and FY2009), and a conference call with both the Association's President/CEO and the Finance and Business Manager (FBM), who was hired after the fraud was discovered. The survey focused on the organization's key accounting and Federal compliance systems and related financial management controls. The survey was conducted during the week of June 11 - 15, 2012.

Conclusion

Once the NEH-OIG recommendations are implemented, we believe that the Association's upgraded accounting system, management controls, Governance oversight, and formalized

policies/procedures should allow the nonprofit to sufficiently manage and account for Federal grant funds moving forward. The identified areas, in which existing financial management controls must be improved, are as follows:

- The Association has not adopted formal, written procurement policies and procedures that conform to Federal requirements. To ensure compliance with OMB Circular A-110, such a policy needs to be developed immediately. Areas to be covered include competitive bidding procedures, sole source justification (if applicable), contract file documentation requirements, suspension/debarment monitoring, and conflict of interest guidelines (see detailed guidance below - item #3).
- The revised *Financial Policies and Procedures* manual does not address the Federal compliance requirements. The manual is silent concerning core compliance elements and the related OMB Cost Circulars (A-110, A-122 and A-133). Specifically, the manual needs to incorporate language addressing Federal compliance requirements related to payroll, travel, procurement (per above), cash management, subrecipient monitoring, and Federal reporting.
- Although an “after-the-fact” time and effort reporting system that utilizes timesheets exists, payroll costs are only allocated to the various functional areas/projects (in the Peachtree accounting software) on an annual basis. We strongly recommend that AASLH begin performing this process on a monthly basis. At the very minimum it should be performed on a quarterly basis, as required by the IMLS General Terms and Conditions manual (Section 12-Financial Management Standards-Accounting System), to ensure that financial reports provided to the Board are accurate and complete.
- The current Peachtree accounting structure is not currently designed to separately capture unallowable costs related to federally-sponsored projects. In fact, recent SF-270 reviews performed by IMLS resulted in the identification of various unallowable costs (alcohol, etc.). We strongly recommend that AASLH create a unique natural expense account to capture any unallowable costs and link the account(s) to each Federal project code. By creating these accounts, AASLH will be in a better position to identify and capture these costs during the initial disbursement/accounts payable review process.
- Several suggestions to further segregate duties and ultimately improve internal controls are as follows:
 - a. Cash Receipting Process: Presently, incoming checks are forwarded to the FBM. This individual is then responsible for making copies of the checks, preparing and making the bank deposit, and inputting the cash receipt entry into the Peachtree accounting software.

Ideally, incoming checks should be logged by two individuals when the mail is opened. The use of a log interjects additional employees into the process and generates a record of all checks received. To ensure all checks have been properly deposited, the check log should then be reconciled against actual deposits made during the month on a periodic basis.
 - b. Bank and Investment Reconciliations: The Association enacted a new procedure in which the Board Treasurer will begin reviewing the bank and investment reconciliations performed by staff. The Treasurer will receive a PDF copy of the bank/investment statements and the associated reconciliations via email.

To guard against fraudulent activity and the possible tampering with bank/investment statements, we recommend that the Board Treasurer be provided with read-only access to these accounts. This will allow the individual to quickly verify that the bank/investment statements included in the reconciliation packages have not been modified in any manner.

- Since the AASLH Board was scheduled to review the revised *Financial Policies and Procedures* manual during the June board meeting, several other comments (that do not rise to the level of separate identification in this report) were provided directly to both the Association's President/CEO and Board Treasurer for immediate consideration. A copy of the related email is enclosed (see Attachment A).
- The independent auditor (IPA) plans to issue a detailed management letter in conjunction with the pending FY2011 financial statement audit report. This letter will document multiple internal control deficiencies and highlight accounting/finance process flows that lack a proper segregation of duties. AASLH must ensure any IPA comments that extend above and beyond the aforementioned comments resulting from this accounting survey are addressed in a timely fashion.

Furthermore, we identified a potential cash flow issue that warrants further scrutiny and continuous monitoring. At the end of calendar year 2010, the organization's unrestricted net assets had a negative balance of approximately \$ [REDACTED] (see attached excerpt from the FY2010 IRS Form 990-Attachment B). The FY2011 audited financial statements have not yet been issued. If this situation is not resolved shortly, the Association may encounter going concern issues in the near term. Based upon this fact, the NEH-OIG believes that the Association's liquidity situation needs to be actively monitored by IMLS management and may require the inclusion of certain safeguards in future grant awards, as suggested by OMB Circular A-110, Subpart B, Paragraph .14, *Special award conditions*¹. Some suggestions include drafting language requiring the Association to immediately alert IMLS of any "going concern" comments or adverse audit opinions; or treating the grantee as a high-risk organization and therefore administering future awards on a cash reimbursement basis, until the situation improves.

Association management has also been advised of several core compliance requirements that directly impact the aforementioned Federal awards and, therefore need to be monitored on an ongoing basis to ensure proper implementation.

1. The organization's accounting system must provide accurate, current, and complete disclosure of all financial transactions related to each federally-sponsored project. Unallowable expenditures should be separately tracked in the general ledger and excluded from charges to Federal awards. The organization must also ensure a system is in place to capture and track cost sharing data. Cash contributions to the project from third parties must be accounted for in the general ledger with other award funds. Third party in-kind contributions (non-cash) are not required to be recorded in the general

¹ OMB Circular A-110, Subpart B-Pre-Award Requirements_.14 Special award conditions: If an applicant or recipient: (a) has a history of poor performance, (b) is not financially stable, (c) has a management system that does not meet the standards prescribed in this Circular, (d) has not conformed to the terms and conditions of a previous award, or (e) is not otherwise responsible, Federal awarding agencies may impose additional requirements as needed, provided that such applicant or recipient is notified in writing as to: the nature of the additional requirements, the reason why the additional requirements are being imposed, the nature of the corrective action needed, the time allowed for completing the corrective actions, and the method for requesting reconsideration of the additional requirements imposed.

ledger, but must be under accounting control, possibly through the use of a memorandum ledger.

2. Charges to awards for salaries and wages, whether treated as direct costs or indirect costs, must be based on documented payrolls approved by a responsible official(s) of the organization. The distribution of salaries and wages to awards must be supported by personnel activity reports, except when a substitute system has been approved in writing by the cognizant agency.

Reports reflecting the distribution of activity of each employee must be maintained for all staff members whose compensation is charged, in whole or in part, directly to awards. In addition, in order to support the allocation of indirect costs, such reports must also be maintained for other employees whose work involves two or more functions or activities if a distribution of their compensation between such functions or activities is needed in the determination of the organization's indirect cost rate.

Salaries and wages of employees used in meeting cost sharing or matching requirements on awards must be supported in the same manner as salaries and wages claimed for reimbursement from awarding agencies.

3. The Association shall establish written procurement procedures that provide for, at a minimum, the following procedural requirements:
 - a. The Association must ensure that all parties with whom they contract for goods or services are not debarred or suspended from doing business with the Federal government (see Excluded Parties List System) when (1) the amount of the contract is \$25,000 or more; or (2) the contract requires the Federal agency's consent; or (3) the contract is for federally-required audit services. A term or condition must be included in the contract that requires the contractor's compliance with Subpart C of 2 CFR Parts 180 and 3369.
 - b. Some form of price or cost analysis should be made in connection with every procurement action. Price analysis may be accomplished in various ways, including the comparison of price quotations submitted, market prices, and similar indicia, together with discounts. Cost analysis is the review and evaluation of each element of cost to determine reasonableness, allocability, and allowability.
 - c. Procurement records and files for purchases in excess of the simplified acquisition threshold (currently \$100,000) shall include the basis for contractor selection, justification for lack of competition when competitive bids or offers are not obtained, and the basis for award cost or price.
 - d. The type of procurement instrument used, e.g., fixed price contracts, cost reimbursable contracts, incentive contracts, purchase orders, will be determined by the Association, but must be appropriate for the particular procurement and for promoting the best interests of the program involved. The "cost-plus-a-percentage-of-cost" or "percentage of construction cost" methods shall not be used.

1. Administrative, contractual, or legal remedies in instances where contractors violate or breach contract terms, and such remedial actions as may be appropriate.
 2. Termination for cause and for convenience by the Association, including the manner by which it will be effected and the basis for settlement. In addition, these contracts shall also contain a description of the conditions under which the contract may be terminated for default as well as conditions where the contract may be terminated because of circumstances beyond the control of the contractor.
 3. Access by the Association, the Federal awarding agency, the Comptroller General of the United States, or any other duly authorized representatives to any books, documents, papers, and records of the contractor which are directly pertinent to that specific contract for the purpose of making audit, examination, excerpts, and transcriptions.
4. Arrangements with consultants must be documented in writing. The written consultant agreement should include (at a minimum):
- a. A clear description of all services to be rendered and/or products (written reports, etc.);
 - b. Fees to be paid;
 - c. Method of payment (submission of invoices, payment schedule, etc.);
 - d. Allowable expenses for reimbursement;
 - e. An explanation of who will provide materials, equipment, and office space;
 - f. A statement that the consultant pays applicable state and Federal income taxes;
 - g. An acknowledgement by the consultant that he/she is not entitled to any of the benefits provided to employees of the organization;
 - h. A description of the term of the agreement, (one week, one season, or until the project is completed); and
 - i. A description of the circumstances under which the organization or the consultant can terminate the agreement.
5. Financial records, supporting documentation, statistical records, and all other records pertinent to the Federal award must be retained by the Association for three years from the date of submission of the final *Federal Financial Report*.

cc: NEH Senior Leadership Team
cc: [REDACTED] AASLH President/CEO

Attachment A

Elsberg, Stephen

From: Elsberg, Stephen
Sent: Friday, June 15, 2012 11:28 AM
To: [REDACTED]
Subject: New Financial Policies and Procedures Manual

Importance: High

[REDACTED]

I've had a chance to review the new Financial Policies & Procedures manual. Wanted to share my initial thoughts with you so we could discuss on the phone later today:

- Section I - Compliance (p.1): This section ignores Federal grant compliance issues. For example, OMB Circulars A-110, A-122 & A-133 are not mentioned.
- Section 1 - Budget Preparation (p.5) and Purchase Authority – Section 4 (Contracts - item #2; p.13): AASLH does not prepare a stand-alone capital budget. Appears that any capital purchases expected for the upcoming year are incorporated into the operating budget and any unexpected capital outlays require separate approval from Treasurer. AASLH may want to reconsider this approach.
- Separation of Duties - Cash Receipts (p.6): Two comments: 1) Ideally, the mail s/b opened by two individuals and 2) the Receptionist should enter all checks received into a check log (something as simple as an Excel spreadsheet) when opening the mail. This log could then be reconciled back to the actual deposits made. Under the current scenario, the receptionist and possibly the accountant could steal checks without leaving any trail.
- Separation of Duties - Bank Reconciliations (p.6 & p.14 - item #7): Since the AASLH Treasurer will be performing top level oversight, I strongly recommend this individual have direct, read-only access to both the bank and investment statements. This way he/she can confirm that the PDF reconciliations provided by the CEO/Accountant have been prepared using the actual statements. This is a very cost-effective I/C procedures used by smaller non-profit org's.
- Separation of Duties - Timesheets (p.8): Appears that the methodology used conforms to Federal requirements. However, recommend that the manual incorporate the time and effort requirements articulated in A-122, Section 8m (at least for payroll costs charged to the Federal gov't).
- Separation of Duties - Maintenance of Records (p.8): P&P manual references the AASLH record retention policy. Before manual is finalized, management should review the AASLH record retention policy to ensure that it conforms to the Federal requirements stipulated in A-110 (i.e. 3 years from submission of final FSR).
- Chart of Accounts (p.10) & review of PeachTree COA printout: 1) Why have revenue accounts in the 4xxx range? Confuses issue since this natural account range reserved for expenses. For example, 400.000.4250 represents website sponsorships but 402.xxx.4250 represents planning facilitator expense. 2) Dep't 420 appears to break with the standard numbering convention used with all other dep'ts.
- Purchase Authority – Section 1: Purchases (p.11): Section does not discuss the Federal purchasing requirements. Furthermore, policy emphasizes the use of preferred vendors and is silent concerning the use of competitive bidding requirement and EPLS searches, etc. This section needs to be reworked to comply with Federal rules.

- Travel (p.12) - Need to incorporate language relating to Federal Travel Reg's.
- Insurance (p.18): States that the association's ST disability plan is self-funded. Probably not a concern due to limited number of employees and nature of insurance; however, may represent a potential liability risk that the Board hasn't considered.
- Other General Comments: 1) The approval process for journal entries is not discussed. 2) The audit committee may want to consider a required auditor rotation timeframe (every 5 years or so). Current draft calls for a review of auditor performance every three years by the Board but no requirement to rotate firms.

Steve

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Attachment B