



NATIONAL ENDOWMENT FOR THE
Humanities

OFFICE OF INSPECTOR GENERAL

MEMORANDUM

Date: December 5, 2012

To: James A. Leach, Chairman
Carole Watson, Deputy Chairman
Jeff Thomas, Assistant Chairman for Planning and Operations
Adam Wolfson, Assistant Chairman for Programs
Nadina Gardner, Director ~ Division of Preservation and Access
Susan Daisey, Director ~ Office of Grant Management

From: Laura Davis, Acting Inspector General *Laura Davis*

Subject: Accounting System Survey Memorandum Report: OIG-13-01 (TS)
Educopia Institute
Atlanta, GA

We have completed our accounting system survey of the Educopia Institute (the "Institute"). The purpose of our survey was to obtain information to determine the adequacy of the organization's accounting system, management controls, and policies and procedures designed to administer NEH grant funds.

NEH awarded the Institute a \$300,000 Preservation and Access grant (PR-50134-11) for the period August 2011 through July 2013. The project proposes to study, document, and model the use of data preparation and distributed digital preservation frameworks to collaboratively preserve digitized and born-digital newspaper collections. As documented by the approved budget, the bulk of the grant award represents personnel/fringe costs (\$████████) and subrecipient costs (\$████████). At this juncture, the Institute has submitted one request for reimbursement (SF-270) totaling \$████████.

The Institute, formally the MetaArchive Cooperative, was founded in 2004 as a community-based network of libraries, archives, and other cultural heritage organizations that cooperatively preserve their digital content utilizing distributed digital preservation practices. The organization represents a non-profit and is recognized by the Internal Revenue Service as a Section 501(c)(3) tax exempt organization. Upon review of the organizational survey (represents the Society's first NEH award), the Office of Grants Management discovered that the Institute has never undergone a formal audit and the organization lacks an accountant. As a result, the matter was referred to the Office of Inspector General (OIG) in September 2012.

Scope

Our efforts were limited to completing the pre-award survey document¹ and reviewing the underlying documentation supporting the first SF-270 payment request submitted to NEH. To

¹ The pre-award survey represents a standardized checklist of forty-seven questions that is used by the NEH-OIG to assess a grantee's accounting system and related financial management controls.

accomplish these goals, the OIG a) exchanged emails and held a conference call with the Institute's Executive Director; b) reviewed accounting and procurement manuals, Excel spreadsheet used to track accounting transactions, draft chart of accounts, subrecipient agreements executed with both the University of North Texas and Virginia Tech, and other documentation used to validate key controls asserted in policy manuals; and c) detail tested the January through June 2012 timesheets and payroll records associated with the SF-270 submission.

Conclusion

Based upon the work performed, the NEH-OIG concludes that the Institute's accounting system, management controls, and formalized policies/procedures do **not** currently meet the minimum requirements articulated by the NEH *General Terms and Conditions for Awards, Section 17-Financial Management Standards*, and OMB Circular A-110. Specifically, the Institute has not a) implemented either a working chart of accounts or an accounting software package²; b) retained a qualified bookkeeper/accountant with the requisite accounting skill set; or c) established a formalized system to track grant expenditures.

We understand that the grantee has encountered setbacks engaging a consultant to take the lead on developing a multi-segment chart of accounts and establishing an accounting file in QuickBooks³. Now that the Institute is managing Federal awards, this process must be completed with utmost urgency and, at the same time, a qualified bookkeeper needs to be retained to perform the ongoing day-to-day accounting duties. In accordance with OMB Circular A-110, Section 14 (see below), the NEH-OIG recommends that the Institute be classified as a high-risk entity and remain in this status until the above issues are resolved. Effective immediately, the Institute should only be paid on a cost-reimbursement basis (i.e. not eligible for advances) and will need to include supporting documentation with future payment requests.

.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. Any special conditions shall be promptly removed once the conditions that prompted them have been corrected.

² Currently, the Institute's Executive Director tracks the accounting transactions in a simplistic Excel spreadsheet (no g/l accounts used). This file does not allow the user to sort transactions by functional area or project/funder level.

³ As noted above, the Institute is now administering Federal grants. During the accounting survey process, the NEH-OIG worked with the Executive Director and stressed the need to adopt a multi-segment chart of accounts. This will allow the organization to easily absorb new departments and/or grants (with multiple funders) since it provides for one common set of natural accounts that can then be linked to unique departments, projects, and even funding sources within a project (i.e. "class" codes). By incorporating "class" codes, the Institute will have the ability to produce both organization-wide and detailed financial statements drilling all the way down to the individual department, project, and/or funding source level. We further advised that the organization establish unique general ledger accounts to capture and segregate unallowable costs that cannot be charged to the Federal grants.

Furthermore, the Institute needs to promptly address several other Federal compliance related issues identified during this review:

- I. The Institute's salaries and wages reporting infrastructure does not meet Federal compliance standards as stipulated by OMB Circular A-122, Section 8m. Moving forward, the organization must adopt the use of a true level-of-effort reporting system for all staff working on Federal grants (see item #2 below).

Although the Institute uses timesheets, tracks time by functional area, and both the employee and supervisor sign the timesheets, it became apparent that the time allocation reported on the timesheets is based on the approved budget rather than an actual "after the fact" determination. For all three employees (six months of timesheets reviewed for each individual), the time allocation percentages remained static for all pay periods tested and the timesheets lacked any detailed tracking of hours (i.e. simply provided a percentage breakdown by week). Furthermore, the time allocation percentages reported on the timesheets agreed to the approved budget.

- II. Over half of the budgeted grant work, based on dollar amount, will be performed by two subrecipients (digital librarian specialists at Virginia Tech and University of North Texas). We determined that the Institute's existing *Accounting and Procurement Manual* is silent concerning subrecipient compliance monitoring and one of the two subawards, which exceeds the small purchase threshold, lacks many of the required award terms and conditions, as required by OMB Circular A-110.⁴ To ensure compliance with key subrecipient monitoring requirements, written policies and procedures that encompass the items discussed below (item #4) must be developed.
- III. The acceptance of Federal grant funds imposes additional travel rules on a recipient organization. The existing accounting manual devotes a brief section to business travel; however, this policy does not discuss many of the unique Federal travel requirements. Specifically, there is no discussion of the Fly America Act, GSA approved per-diem rates, use of coach class plane tickets, prior written approval for foreign travel required from NEH (if not already pre-approved in grant award), etc. Accordingly, the existing travel policy needs to be updated.
- IV. We noted errors with the first reimbursement request (SF-270) submitted to NEH. In particular, a) non Federal expenses (i.e. cost-share) were omitted; b) reported program outlays were based on the grant budget (vs. actual payroll costs); and c) the grantee asserted that accounting records are maintained on an accrual basis which is not the case (clearly cash-basis). The Executive Director stated that the SF-270 would be amended and resubmitted.
- V. The Institute needs to develop a document retention policy that conforms to baseline Federal requirements as defined by OMB Circular A-110 (see item #7 below).

⁴ After discussing the matter with the Executive Director, we understand that the Institute has drafted an amendment to the University of North Texas (UNT) subaward that incorporates the missing terms. Management hopes to obtain UNT's sign-off in the near term.

Institute management has been advised of several core compliance requirements that directly impact this NEH award 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, if applicable. 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 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. In accordance with Federal guidelines, written procurement policies should provide for, at a minimum, the following procedural requirements:
 - a. The organization 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 NEH 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 organization, 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.
- e. Contracts in excess of the simplified acquisition threshold (currently \$100,000) must provide for:
 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 Institute, 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 Institute, the NEH, 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. As discussed in the OMB Circular A-133 Compliance Supplement and the NEH *Requirements for Grant Recipients that Serve as Sponsors of Projects*, subrecipient monitoring policies/procedures should address the following:
 - a. The grantee must provide to the subrecipient identifying information on the Federal award, such as the award name and number, NEH's name, and the relevant CFDA number (found at the bottom of the "Official Notice of Action").
 - b. The grantee must advise the subrecipient of the requirements of the NEH award, such as the applicable Federal laws and regulations, as well as the terms and conditions of the NEH grant agreement.
 - c. The grantee must collect the certifications that flow down to subrecipients, as outlined in the application guidelines for the particular NEH grant program.
 - d. The grantee must maintain an organizational prior approval system to manage the subrecipient's activities.
 - e. The grantee shall review financial and performance reports submitted by the subrecipient.

- f. The grantee shall conduct site visits to review financial and programmatic records and observe operations.
 - g. The grantee shall ensure that the scope of the project, as approved by NEH, is not changed without prior approval from NEH.
 - h. In addition to the grantee's own audit, it must ensure that the subrecipient has a single audit, if one is required by the standards outlined in OMB Circular A-133 (see #6 below). The subrecipient must be required to provide both the grantee, auditors, and the funding Agency access to its records and financial statements as necessary.
 - i. The grantee is responsible for issuing management decisions on subrecipient audit findings; and must ensure that the subrecipient takes timely and appropriate corrective action in response to the audit.
 - j. The grantee must monitor the activities of and maintain contact with the subrecipient as necessary to ensure compliance with the requirements mentioned above, and to ensure achievement of performance goals.
5. 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.
6. Since the Institute has not been subject to an annual audit and currently receives Federal grant funds, the organization was notified that OMB Circular A-133 "*Audits of States, Local Governments, and Non-Profit Organizations*" requires non-Federal entities that expend \$500,000 or more in a fiscal year in Federal awards to undergo a single or program-specific audit.

7. Financial records, supporting documentation, statistical records, and all other records pertinent to the NEH award must be retained by the Institute for three years from the date of submission of the final *Federal Financial Report*.

Management Representations

We have also received written assurance from [REDACTED] (Executive Director and Project Director), [REDACTED] (Board Chair), and [REDACTED] (Treasurer) that the Institute will:

1. Maintain supporting documentation in accordance with NEH and OMB regulations;
2. Comply with all of the specific terms and conditions of the NEH award;
3. Comply with the Uniform Administrative Requirements of OMB Circular A-110;
4. Comply with the Cost Principles for Nonprofit Organizations (OMB Circular A-122);
5. Comply with NEH General Terms and Conditions for Awards to Organizations; and
6. Comply with the audit requirements of OMB Circular A-133.

Please note that the Office of Inspector General may perform a subsequent review to assess the organization's a) compliance with the terms and conditions of the NEH award and b) progress made addressing the items discussed in the *Conclusion* section of this memorandum.