



DEPARTMENT OF HEALTH AND HUMAN SERVICES

## OFFICE OF INSPECTOR GENERAL



OFFICE OF AUDIT SERVICES, REGION IX  
90 - 7<sup>TH</sup> STREET, SUITE 3-650  
SAN FRANCISCO, CA 94103

July 30, 2012

Report Number: A-09-11-01014

Ms. Mila Kaahanui  
Executive Director, Office of Community Services  
Department of Labor and Industrial Relations  
830 Punchbowl Street, Room 420  
Honolulu, HI 96813

Dear Ms. Kaahanui:

Enclosed is the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), final report entitled *Hawaii Claimed Unallowable Community Services Block Grant Costs for Hawaii County Economic Opportunity Council's Expenditures Under the Recovery Act*. We will forward a copy of this report to the HHS action official noted on the following page for review and any action deemed necessary.

The HHS action official will make final determination as to actions taken on all matters reported. We request that you respond to this official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://oig.hhs.gov>.

If you have any questions or comments about this report, please do not hesitate to call me, or contact Doug Preussler, Audit Manager, at (415) 437-8309 or through email at [Doug.Preussler@oig.hhs.gov](mailto:Doug.Preussler@oig.hhs.gov). Please refer to report number A-09-11-01014 in all correspondence.

Sincerely,

/Lori A. Ahlstrand/  
Regional Inspector General  
for Audit Services

Enclosure

**Direct Reply to HHS Action Official:**

Ms. Janice L. Samuel  
Director, Division of Financial Integrity  
Office of Financial Services  
Administration for Children and Families  
U.S. Department of Health and Human Services  
370 L'Enfant Promenade, SW  
Washington, DC 20447

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**HAWAII CLAIMED UNALLOWABLE  
COMMUNITY SERVICES  
BLOCK GRANT COSTS FOR  
HAWAII COUNTY ECONOMIC  
OPPORTUNITY COUNCIL'S  
EXPENDITURES UNDER THE  
RECOVERY ACT**



Daniel R. Levinson  
Inspector General

July 2012  
A-09-11-01014

# *Office of Inspector General*

<http://oig.hhs.gov>

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The mission of the Office of Inspector General (OIG), as mandated by Public Law 95-452, as amended, is to protect the integrity of the Department of Health and Human Services (HHS) programs, as well as the health and welfare of beneficiaries served by those programs. This statutory mission is carried out through a nationwide network of audits, investigations, and inspections conducted by the following operating components:

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The Office of Evaluation and Inspections (OEI) conducts national evaluations to provide HHS, Congress, and the public with timely, useful, and reliable information on significant issues. These evaluations focus on preventing fraud, waste, or abuse and promoting economy, efficiency, and effectiveness of departmental programs. To promote impact, OEI reports also present practical recommendations for improving program operations.

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The Office of Counsel to the Inspector General (OCIG) provides general legal services to OIG, rendering advice and opinions on HHS programs and operations and providing all legal support for OIG's internal operations. OCIG represents OIG in all civil and administrative fraud and abuse cases involving HHS programs, including False Claims Act, program exclusion, and civil monetary penalty cases. In connection with these cases, OCIG also negotiates and monitors corporate integrity agreements. OCIG renders advisory opinions, issues compliance program guidance, publishes fraud alerts, and provides other guidance to the health care industry concerning the anti-kickback statute and other OIG enforcement authorities.

# *Notices*

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Section 8L of the Inspector General Act, 5 U.S.C. App., requires that OIG post its publicly available reports on the OIG Web site.

## **OFFICE OF AUDIT SERVICES FINDINGS AND OPINIONS**

The designation of financial or management practices as questionable, a recommendation for the disallowance of costs incurred or claimed, and any other conclusions and recommendations in this report represent the findings and opinions of OAS. Authorized officials of the HHS operating divisions will make final determination on these matters.

## EXECUTIVE SUMMARY

### BACKGROUND

The American Recovery and Reinvestment Act of 2009 (Recovery Act), P.L. No. 111-5, provided \$1 billion to the Community Services Block Grant (CSBG) program for fiscal years (FY) 2009 and 2010. As with annually appropriated CSBG funds, Recovery Act funds were to be used to reduce poverty, revitalize low-income communities, and help low-income Americans. In addition, CSBG services funded by the Recovery Act were to be provided on or before September 30, 2010.

Within the U.S. Department of Health and Human Services, the Administration for Children and Families (ACF), Office of Community Services, administers the CSBG program. The CSBG program funds a State-administered network of more than 1,100 local community action agencies (CAA) that deliver programs and services to low-income Americans. The CAAs provide services addressing employment, education, better use of available income, housing, nutrition, and health to combat the causes of poverty.

In the State of Hawaii, the Department of Labor and Industrial Relations, Office of Community Services (State agency), was responsible for approving CAAs' applications for CSBG Recovery Act funds and monitoring CAAs' compliance with Federal requirements. Under the Recovery Act, the State agency was awarded \$5 million in CSBG funds for FYs 2009 and 2010.

Hawaii County Economic Opportunity Council (Council) is a nonprofit CAA that has served low-income individuals in the county of Hawaii since 1965. The mission of the Council is to alleviate, eliminate, and prevent poverty in Hawaii through various programs. For the period November 5, 2009, through September 30, 2010, the State agency awarded the Council \$1,016,063 in CSBG Recovery Act funds (the award). The Council expended \$975,368 of the award. The remaining \$40,695 was not expended and was returned to the State agency.

By accepting grant awards, States agree to comply with Federal regulations governing the administration of the grants, including compliance with various cost principles. Federal law requires that States receiving CSBG funds ensure that cost and accounting standards of the Office of Management and Budget apply to a recipient of the funds. Nonprofit CAAs are subject to 45 CFR part 74. These regulations state that the allowability of costs will be determined in accordance with 2 CFR part 230, *Cost Principles for Non-Profit Organizations*. To be allowable under an award, costs must be reasonable for the performance of the award and allocable to the award under these principles. Costs are allocable if they are distributed in reasonable proportion to the benefits received.

### OBJECTIVE

Our objective was to determine whether the CSBG costs that the State agency claimed for the Council's program expenditures were allowable in accordance with applicable Federal requirements.

## **SUMMARY OF FINDINGS**

Of the \$975,368 of CSBG costs that the State agency claimed for the Council's program expenditures, \$830,766 was allowable in accordance with applicable Federal requirements. The remaining \$144,602 consisted of \$22,602 of fringe benefit costs that we determined was unallowable and \$122,000 that we set aside for ACF resolution. Specifically, we set aside:

- \$28,796 of salaries and wages for the Council's administrative and program employees because the costs were based on budget estimates,
- \$21,789 of fringe benefits applicable to the set-aside salaries and wages, and
- \$71,415 of shared costs because the costs were not allocated to the Council's programs in reasonable proportion to the benefits received.

The State agency claimed these costs because it did not have adequate monitoring procedures to ensure that the CSBG costs claimed for the Council's program expenditures were allowable in accordance with applicable Federal requirements.

## **RECOMMENDATIONS**

We recommend that the State agency:

- refund to the Federal Government \$22,602 for unallowable fringe benefit costs,
- work with ACF to determine the allowability of \$122,000 that we set aside and refund to the Federal Government any amount determined to be unallowable,
- work with the Council to ensure that it allocates shared costs to programs in reasonable proportion to the benefits received, and
- strengthen monitoring procedures to ensure that costs claimed are allowable in accordance with applicable Federal requirements.

## **HAWAII COUNTY ECONOMIC OPPORTUNITY COUNCIL COMMENTS**

In its written comments on our draft report, the Council agreed with our finding on unallowable fringe benefit costs. In addition, based on the available documentation, the Council concurred with our findings related to the set-aside amount. However, the Council stated that it would continue to search for documentation that may lower the set-aside amount and would work with the State agency to address and resolve our findings. The Council's comments are included in their entirety as Appendix B.

## **STATE AGENCY COMMENTS**

In its written comments on our draft report, the State agency generally concurred with our findings and provided information on corrective actions that it had taken or planned to take to address our recommendations. The State agency's comments are included in their entirety as Appendix C.



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## **INTRODUCTION**

### **BACKGROUND**

#### **American Recovery and Reinvestment Act**

The American Recovery and Reinvestment Act of 2009 (Recovery Act), P.L. No. 111-5, authorized supplemental appropriations for job preservation and creation, infrastructure investment, energy efficiency and science, assistance to the unemployed, and State and local fiscal stabilization. The Recovery Act provided \$1 billion to the Community Services Block Grant (CSBG) program for fiscal years (FY) 2009 and 2010. As with annually appropriated CSBG funds, Recovery Act funds were to be used to reduce poverty, revitalize low-income communities, and help low-income Americans. In addition, CSBG services funded by the Recovery Act were to be provided on or before September 30, 2010.

#### **Community Services Block Grant Program**

The CSBG program was reauthorized by the Community Opportunities, Accountability, and Training and Educational Services Act of 1998 (CSBG Act), P. L. No. 105-285, to provide funds to alleviate the causes and conditions of poverty in communities. Within the U.S. Department of Health and Human Services (HHS), the Administration for Children and Families (ACF), Office of Community Services, administers the CSBG program.

The CSBG program funds a State-administered network of more than 1,100 local community action agencies (CAA) that deliver programs and services to low-income Americans. The CAAs provide services addressing employment, education, better use of available income, housing, nutrition, and health to combat the causes of poverty. Recovery Act grant funds were intended to cover additional costs for the same types of services.

#### **Hawaii Department of Labor and Industrial Relations, Office of Community Services**

In the State of Hawaii, the Department of Labor and Industrial Relations, Office of Community Services (State agency), was responsible for approving CAAs' applications for CSBG Recovery Act funds and monitoring CAAs' compliance with Federal requirements. Under the Recovery Act, the State agency was awarded \$5 million in CSBG funds for FYs 2009 and 2010.

#### **Hawaii County Economic Opportunity Council**

Hawaii County Economic Opportunity Council (Council) is a nonprofit CAA that has served low-income individuals in the county of Hawaii since 1965. The mission of the Council is to alleviate, eliminate, and prevent poverty in Hawaii. The Council offers programs in transportation, housing, education, youth services, diversified agriculture, energy, and economic development activities to assist individuals and families to improve the quality of their lives.

For the period November 5, 2009, through September 30, 2010, the State agency awarded the Council \$1,016,063 in CSBG Recovery Act funds (the award). The Council expended \$975,368 of the award. The remaining \$40,695 was not expended and was returned to the State agency.<sup>1</sup>

## **Federal Requirements for Grantees**

By accepting grant awards, States agree to comply with Federal regulations governing the administration of the grants, including compliance with various cost principles. Section 678D(a)(1)(B) of the CSBG Act requires that States receiving CSBG funds ensure that cost and accounting standards of the Office of Management and Budget (OMB) apply to a recipient of the funds. Nonprofit CAAs are subject to 45 CFR part 74. The regulations at 45 CFR § 74.27(a) state that the allowability of costs will be determined in accordance with 2 CFR part 230 (formerly OMB Circular A-122), *Cost Principles for Non-Profit Organizations*. In addition, regulations at 45 CFR part 74, *Standards for Financial and Program Management Systems*, require nonprofit CAAs to maintain financial management systems.

## **OBJECTIVE, SCOPE, AND METHODOLOGY**

### **Objective**

Our objective was to determine whether the CSBG costs that the State agency claimed for the Council's program expenditures were allowable in accordance with applicable Federal requirements.

### **Scope**

We reviewed the State agency's claim of \$975,368 for the Council's program expenditures funded by the Recovery Act award for the period November 5, 2009, through September 30, 2010. We did not review the overall internal control structure of the State agency or the Council. We limited our review of internal controls to those that were significant to the objective of our audit.

We conducted our audit from June to December 2011 and performed fieldwork at the State agency's office in Honolulu, Hawaii, and the Council's office in Hilo, Hawaii.

### **Methodology**

To accomplish our objective, we:

- reviewed applicable Federal laws, regulations, and guidance;
- reviewed contractual and supplemental agreements between the State agency and the Council for the period November 5, 2009, through September 30, 2010;

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<sup>1</sup> We reviewed the award funds returned to the State agency in a separate report entitled *Hawaii Claimed Unallowable Community Services Block Grant Costs for Administrative Expenditures Under the Recovery Act* (A-09-12-01000), issued June 20, 2012.

- reviewed the Council’s board of directors’ meeting minutes;
- reviewed the Council’s accounting policies and procedures;
- reviewed the Council’s cost allocation methodologies for shared costs;
- interviewed State agency officials to gain an understanding of their fiscal and program monitoring procedures;
- interviewed Council officials to gain an understanding of the costs charged under the award;
- reviewed the State agency’s fiscal and program monitoring reports;
- reviewed correspondence between the State agency and Council officials;
- reviewed the Council’s audited financial statements for the periods October 1, 2007, through September 30, 2008; October 1, 2008, through September 30, 2009; and October 1, 2009, through September 30, 2010;
- reconciled the costs that the State agency claimed under the award with the Council’s general ledger;
- analyzed the Council’s general ledger to identify large, unusual, and/or recurring transactions and examined, on a test basis, evidence supporting selected transactions for claimed costs to determine their allowability;<sup>2</sup> and
- discussed our findings with State agency and Council officials.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

## **FINDINGS AND RECOMMENDATIONS**

Of the \$975,368 of CSBG costs that the State agency claimed for the Council’s program expenditures, \$830,766 was allowable in accordance with applicable Federal requirements. The remaining \$144,602 consisted of \$22,602 of fringe benefit costs that we determined was

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<sup>2</sup> We determined that the number, dollar amounts, and types of transactions selected were sufficient for determining allowability of costs based on the adequacy of supporting documentation.

unallowable and \$122,000 that we set aside for ACF resolution. Specifically, we set aside:

- \$28,796 of salaries and wages for the Council's administrative and program employees because the costs were based on budget estimates,
- \$21,789 of fringe benefits applicable to the set-aside salaries and wages, and
- \$71,415 of shared costs because the costs were not allocated to the Council's programs in reasonable proportion to the benefits received.

The State agency claimed these costs because it did not have adequate monitoring procedures to ensure that the CSBG costs claimed for the Council's program expenditures were allowable in accordance with applicable Federal requirements.

See Appendix A for a schedule of the costs that the State agency claimed for the Council's expenditures and the results of our audit (i.e., allowable, unallowable, and set-aside costs).

## **SALARIES AND WAGES**

Federal cost principles (2 CFR part 230, Appendix B, section 8.m.) state that charges to awards for salaries and wages must be supported by personnel activity reports that reflect an after-the-fact determination of the actual activity of each employee. Budget estimates (i.e., estimates determined before the services are performed) do not qualify as support for charges to awards. In addition, 2 CFR part 230, Appendix A, section A.2., states that to be allowable under an award, costs must be reasonable for the performance of the award and adequately documented.

Of the \$332,760 claimed for salaries and wages, \$303,964 claimed for the Council's direct employees was allowable in accordance with applicable Federal requirements.<sup>3</sup> We set aside the remaining \$28,796 for ACF resolution because the Council charged salaries and wages for its administrative and program employees based on budget estimates instead of charging the costs based on the actual activity of each employee.<sup>4</sup>

Although the Council maintained timesheets for each employee, Council officials indicated that the timesheet clerk adjusted the administrative and program employees' timesheets to match the Council's budget. In addition, the employees' timesheets did not clearly identify which activities were related to CSBG program activities funded under the Recovery Act. Therefore, we could not determine the correct amount of time that should have been charged to the award.

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<sup>3</sup> The \$303,964 of allowable salaries and wages for the Council's direct employees was supported with timesheets that reflected an after-the-fact determination of the actual time of each employee. Direct employees charged 100 percent of their time to the CSBG Recovery Act grant.

<sup>4</sup> Administrative and program employees' salaries and wages were paid indirectly with CSBG and other grant funds.

## **FRINGE BENEFITS**

Federal cost principles (2 CFR part 230, Appendix A, section A.2.) state that to be allowable under an award, costs must be reasonable for the performance of the award and adequately documented. In addition, 2 CFR part 230, Appendix B, section 8.g., states that fringe benefits in the form of regular compensation paid to employees for authorized leave are allowable, provided such costs are absorbed by all organization activities in proportion to the relative amount of time or effort actually devoted to each. Fringe benefits in the form of employer contributions or expenses, whether treated as indirect or direct costs, must be distributed to particular awards and other activities in a manner consistent with the pattern of benefits accruing to individuals or groups of employees whose salaries and wages are chargeable to such awards and other activities.

Of the \$123,770 claimed for fringe benefits, \$79,379 was allowable in accordance with applicable Federal requirements.<sup>5</sup> The remaining \$44,391 consisted of \$22,602 that we determined was unallowable and \$21,789 that we set aside for ACF resolution:

- The \$22,602 was unallowable because the Council did not have supporting documentation to justify fringe benefit charges made on September 30, 2010, the end of the award period. Of this amount, \$14,329 related to the Council's Dropout Prevention program and \$8,273 related to the Council's Language Arts Multicultural program. Council officials stated that they did not know how these fringe benefits were calculated and whether they should have been charged to the award. Council officials believed that the previous fiscal officer (who was no longer employed at the Council) charged fringe benefits based on the approved budget to claim the remaining funds available under the award.
- The \$21,789 of fringe benefits that we set aside was applicable to the set-aside salaries and wages discussed in the previous section.

## **SHARED COSTS**

Federal cost principles (2 CFR part 230, Appendix A, section A.4.) state that a cost is allocable to an award if it benefits both the award and other work and can be distributed in reasonable proportion to the benefits received. Any cost allocable to a particular award or other cost objective under these principles may not be shifted to other Federal awards to overcome funding deficiencies or to avoid restrictions imposed by law or by the terms of the award.

Federal regulations (45 CFR § 74.21(b)) state that grantees must maintain financial management systems that contain written procedures for determining the reasonableness, allocability, and allowability of costs. Grantees must also maintain accounting records that are supported by source documentation and maintain financial systems that provide for accurate and complete reporting of grant-related financial data.

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<sup>5</sup> The \$79,379 of allowable fringe benefits was related to the allowable salaries and wages for the Council's direct employees (discussed in the previous section).

Of the \$77,998 claimed for shared costs,<sup>6</sup> \$6,583 was allowable in accordance with applicable Federal requirements.<sup>7</sup> We set aside the remaining \$71,415 for ACF resolution because the Council did not allocate the costs to its programs in reasonable proportion to the benefits received. Specifically, the Council did not have adequate documentation to support how it allocated \$71,415 of shared costs to the award.

The Council's senior accountant believed that the previous fiscal officer allocated shared costs to the award based on the approved budget to claim the remaining funds available under the award. Because of the lack of adequate supporting documentation, we could not determine the correct amount of costs that should have been charged to the award.

## **LACK OF ADEQUATE MONITORING PROCEDURES**

The State agency did not have adequate monitoring procedures to ensure that the CSBG costs claimed for the Council's program expenditures for salaries and wages, fringe benefits, and shared costs were allowable in accordance with applicable Federal requirements. In a fiscal monitoring report covering the Council's use of CSBG Recovery Act funds, the State agency reported weaknesses related to the Council's personnel and shared costs; however, the State agency concluded that there was no evidence of any misuse or excessive use of CSBG Recovery Act funds and that all reported expenditures were supported with proper documentation.

We found, on the contrary, that the Council charged salaries and wages based on budget estimates. In addition, the Council claimed fringe benefits based on the availability of funds without supporting documentation. Finally, the Council's shared costs were not allocated among its programs in reasonable proportion to the benefits received.

## **RECOMMENDATIONS**

We recommend that the State agency:

- refund to the Federal Government \$22,602 for unallowable fringe benefit costs,
- work with ACF to determine the allowability of \$122,000 that we set aside and refund to the Federal Government any amount determined to be unallowable,
- work with the Council to ensure that it allocates shared costs to programs in reasonable proportion to the benefits received, and
- strengthen monitoring procedures to ensure that costs claimed are allowable in accordance with applicable Federal requirements.

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<sup>6</sup> Shared costs included costs for vehicle gas and oil, telecommunications, utilities, insurance, audit service, data processing, postage, freight and delivery, publication, printing, and copying expenses.

<sup>7</sup> Allowable shared costs of \$6,583 included other vehicle gas and oil, data processing, postage, freight, and delivery expenses that had adequate supporting documentation and were allocated in an equitable manner.

## **HAWAII COUNTY ECONOMIC OPPORTUNITY COUNCIL COMMENTS**

In its written comments on our draft report, the Council agreed with our finding on unallowable fringe benefit costs. In addition, based on the available documentation, the Council concurred with our findings related to the set-aside amount. However, the Council stated that it would continue to search for documentation that may lower the set-aside amount and would work with the State agency to address and resolve our findings. The Council's comments are included in their entirety as Appendix B.

## **STATE AGENCY COMMENTS**

In its written comments on our draft report, the State agency generally concurred with our findings and provided information on corrective actions that it had taken or planned to take to address our recommendations. The State agency's comments are included in their entirety as Appendix C.



# **APPENDIXES**

**APPENDIX A: COSTS CLAIMED AND RESULTS OF AUDIT FOR THE PERIOD  
NOVEMBER 5, 2009, THROUGH SEPTEMBER 30, 2010**

<b>Element of Cost</b>	<b>Claimed</b>	<b>Allowable</b>	<b>Unallowable</b>	<b>Set Aside</b>
Salaries and Wages	\$332,760	\$303,964	\$0	\$28,796
Equipment	177,184	177,184	0	0
Fringe Benefits	123,770	79,379	22,602	21,789
Consultant and Professional Costs	103,272	103,272	0	0
Other Costs <sup>1</sup>	90,752	90,752	0	0
Shared Costs <sup>2</sup>	77,998	6,583	0	71,415
Supplies	37,365	37,365	0	0
Vehicle Costs	21,758	21,758	0	0
Travel and Mileage	7,804	7,804	0	0
Facilities	2,292	2,292	0	0
Physical Exam/Drug Testing	413	413	0	0
<b>Total</b>	<b>\$975,368</b>	<b>\$830,766</b>	<b>\$22,602</b>	<b>\$122,000</b>

<sup>1</sup> Other costs included costs for office and yard maintenance, workshop training and Results Oriented Management and Accountability, program activities, summer school tuition, community garden preparation, and benefits and enrollment coordination funds.

<sup>2</sup> Shared costs included costs for vehicle gas and oil, telecommunications, utilities, insurance, audit service, data processing, postage, freight and delivery, publication, printing, and copying expenses.

## APPENDIX B: HAWAII COUNTY ECONOMIC OPPORTUNITY COUNCIL COMMENTS



H. C. E. O. C.  
Hawaii County Economic Opportunity Council  
47 Rainbow Drive Hilo, Hawaii 96720  
(808) 961-2681



May 17, 2012

Report Number: A-09-11-01014

Lori A. Ahlstrand  
Regional Inspector General for Audit Services,  
Department of Health and Human Services  
Office of Inspector General, Office of Audit Services, Region IX  
90 - 7<sup>th</sup> Street, Suite 3-650  
San Francisco, CA 94103

Dear Inspector Ahlstrand:

We at the Hawaii County Economic Opportunity Council (HCEOC) have read your April 20, 2012 letter citing unallowable and set aside funds for our FYE 2010 ARRA CSBG Grant.

We agree with the \$22,602 unallowable citation regarding fringe benefit charges.

We also concur that based upon the source documents that we are currently able to supply, the \$122,000 set aside findings are valid.

However, for those staff like myself who were heavily involved in achieving the rigorous milestones and benchmarks of the ARRA CSBG program, we still feel that there may be documents yet uncovered which may reduce the set aside amount currently assessed to us.

In the upcoming weeks, we shall continue our search for invoices, receipts, data entries, and reports that could lower the \$122,000 set aside funds.

We shall work with our State Office of Community Services to address and resolve the concerns expressed in your report.

We would like to thank the OIG team who visited us for their exceptionally professional, respectful and helpful conduct.

Sincerely,

Lester Seto  
Interim Executive Director  
HCEOC

**APPENDIX C: STATE AGENCY COMMENTS**

NEIL ABERCROMBIE  
GOVERNOR



DWIGHT TAKAMINE  
DIRECTOR

AUDREY HIDANO  
DEPUTY DIRECTOR

MILA KA'AHANUI  
EXECUTIVE DIRECTOR

**STATE OF HAWAII**  
**OFFICE OF COMMUNITY SERVICES**  
DEPARTMENT OF LABOR AND INDUSTRIAL RELATIONS  
830 PUNCHBOWL STREET, ROOM 420  
HONOLULU, HAWAII 96813

July 12, 2012

Ms. Lori A. Ahlstrand  
Regional Inspector General for Audit Services  
Office of Audit Services, Region IX  
90-7<sup>th</sup> Street, Suite 3650  
San Francisco, California 94103

Re: Audit Findings for Hawaii County Economic Opportunity Council  
from Preliminary Draft Report # A-09-11-01014, dated June 15, 2012

Dear Ms. Ahlstrand:

This letter constitutes the response of the Hawaii State Office of Community Services (HOCS) to the Draft Report #A-09-11-01014 of your office, regarding the Inspector General's monitoring of the Hawaii County Economic Opportunity Council ("HCEOC", or the "Council"). Generally, HOCS concurs with the findings, and will offer some clarification and comments on the report sections referenced below. Please find the relevant text of the draft report emboldened in this document with the State's response in italicized font.

*From Draft Report #A-09-11-01014*

[1] **"FINDINGS AND RECOMMENDATIONS**

**"Of the \$975,368 of CSBG costs that the State agency claimed for the Council's program expenditures, \$830,766 was allowable in accordance with applicable Federal requirements. The remaining \$144,602 consisted of \$22,602 of fringe benefit costs that we determined was unallowable and \$122,000 that we set aside for ACF resolution. Specifically, we set aside:**

- **\$28,796 of salaries and wages for the Council's administrative and program employees because the costs were based on budget estimates,**
- **\$21,789 of fringe benefits applicable to the set-aside salaries and wages, and \$71,415 of shared costs because the costs were not allocated to the Council's programs in reasonable proportion to the benefits received.**

**"The State agency claimed these costs because it did not have adequate monitoring procedures to ensure that the CSBG costs claimed for the Council's program expenditures were allowable in accordance with applicable Federal requirements."**

Ms. Lori A. Ahlstrand  
 July 12, 2012  
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**State Response:** *Generally, the State concurs with this finding. During the ARRA period, the State of Hawaii experienced economic downturn, and the Governor at the time attempted to restrict administrative costs by instituting a hiring and travel freeze. Due to Hawaii's island geography, monitoring could not be performed without extensive air travel and overnight stays. The Governor at the time did approve of ARRA funded additional staff and travel, however no administrative funds were provided by the ARRA grant for salaries or travel costs. Thus, although formula CSBG funds were available for administration, HOCS implemented the \$5 million CSBG ARRA grant and the \$3.7 million CSBG formula grant with one half-time staff.*

**Corrective Action:** *Since the ARRA period, HOCS has been allowed a limited restoration of staff. In 2010 a new Executive Director was appointed and a new CSBG Administrator was assigned shortly thereafter in June 2011. The new CSBG Administrator has developed and implemented new monitoring tools, and the most recent State Plan, due in September, will be updated to include HOCS' monitoring dates. With the entrance of the new Governor State, Departmental, Division, and General fiscal policies and procedures are in the process of being updated. In addition, the new Executive Director has refocused HOCS with an increased emphasis on transparency and compliance through more structured monitoring.*

[2] "SALARIES AND WAGES

**"Federal cost principles (2 CFR part 230, Appendix B, section 8.m.) state that charges to awards for salaries and wages must be supported by personnel activity reports that reflect an after-the- fact determination of the actual activity of each employee. Budget estimates (i.e., estimates determined before the services are performed) do not qualify as support for charges to awards. In addition, 2 CFR part 230, Appendix A, section A.2., states that that to be allowable under an award, costs must be reasonable for the performance of the award and adequately documented. Of the \$332,760 claimed for salaries and wages, \$303,964 claimed for the Council's direct employees was allowable in accordance with applicable Federal requirements. We set aside the remaining \$28,796 for ACF reselution because the Council charged salaries and wages for its administrative and program employees based on budget estimates instead of charging the costs based on the actual activity of each employee.**

**"Although the Council maintained timesheets for each employee, Council officials indicated that the timesheet clerk adjusted the administrative and program employees' timesheets to match the Council's budget. In addition, the employees' timesheets did not clearly identify which activities were related to CSBG program activities funded under the Recovery Act. Therefore, we could not determine the correct amount of time that should have been charged to the award.**

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#### **“FRINGE BENEFITS**

**“Federal cost principles (2 CFR part 230, Appendix A, section A.2.) state that that to be allowable under an award, costs must be reasonable for the performance of the award and adequately documented. In addition, 2 CFR part 230, Appendix B, section 8.g., states that fringe benefits in the form of regular compensation paid to employees for authorized leave are allowable, provided such costs are absorbed by all organization activities in proportion to the relative amount of time or effort actually devoted to each. Fringe benefits in the form of employer contributions or expenses, whether treated as indirect or direct costs, must be distributed to particular awards and other activities in a manner consistent with the pattern of benefits accruing to individuals or groups of employees whose salaries and wages are chargeable to such awards and other activities. Of the \$123,770 claimed for fringe benefits, \$79,379 was allowable in accordance with applicable Federal requirements. The remaining \$44,391 consisted of \$22,602 that we determined was unallowable and \$21,789 that we set aside for ACF resolution:**

- **The \$22,602 was unallowable because the Council did not have supporting documentation to justify fringe benefit charges made on September 30, 2010, the end of the award period. Of this amount, \$14,329 related to the Council’s Dropout Prevention program and \$8,273 related to the Council’s Language Arts Multicultural program. Council officials stated that they did not know how these fringe benefits were calculated and whether they should have been charged to the award. Council officials believed that the previous fiscal officer (who was no longer employed at the Council) charged fringe benefits based on the approved budget to claim the remaining funds available under the award.**
- **The \$21,789 of fringe benefits that we set aside was applicable to the set-aside salaries and wages discussed in the previous section.**

#### **“SHARED COSTS**

**“Federal cost principles (2 CFR part 230, Appendix A, section A.4.) state that a cost is allocable to an award if it benefits both the award and other work and can be distributed in reasonable proportion to the benefits received. Any cost allocable to a particular award or other cost objective under these principles may not be shifted to other Federal awards to overcome funding deficiencies or to avoid restrictions imposed by law or by the terms of the award.**

**“Federal regulations (45 CFR § 74.21(b)) state that grantees must maintain financial management systems that contain written procedures for determining the reasonableness, allocability, and allowability of costs. Grantees must also maintain accounting records that are supported by source documentation and maintain financial systems that provide for accurate and complete reporting of grant-related financial data.**

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**“Of the \$77,998 claimed for shared costs, \$6,583 was allowable in accordance with applicable Federal requirements. We set aside the remaining \$71,415 for ACF resolution because the Council did not allocate the costs to its programs in reasonable proportion to the benefits received. Specifically, the Council did not have adequate documentation to support how it allocated \$71,415 of shared costs to the award.**

**“The Council’s senior accountant believed that the previous fiscal officer allocated shared costs to the award based on the approved budget to claim the remaining funds available under the award. Because of the lack of adequate supporting documentation, we could not determine the correct amount of costs that should have been charged to the award.”**

***State Response:** Although these paragraphs involve three cost categories, Salaries and Wages, Fringe Benefits, and Shared Costs, the common finding in all three categories is the inability of HCEOC to correctly allocate funds in proper or reasonable amounts. In general, the State agrees with this finding. We believe the issues above are primarily shortcomings of the accounting system used by HCEOC at the time. Because HCEOC was not accounting for funds on a grant-by-grant basis and relied on paper ledger sheets where duplicate entries in multiple programs could be entered, it was impossible for HOCS to ascertain any duplication of costs or to compare total cost allocation across programs. In such a ledger, unless the coding is consistent from program to program and the code identifies the funding source, it would be difficult for an auditor to ascertain whether or not an expense is being charged in two different programs. As a side note, the flexibility of CSBG formula funds to be used without guidelines or limits on administrative expenditures creates the impression among many Community Action Agencies that it is allowable to attempt to completely expend an award without proper allocation. Finally, there is no clear authority from the Federal Government for State agencies to examine the entire CAA’s budget within the scope of CSBG audit, nor a clear definition of the scope of CSBG audit. This creates a situation where agencies are resistant to opening each program ledger. Without a proper comparison between the affected program and others, it is impossible to determine relative proportions and determine reasonableness.*

***Corrective Action:** Through continued monitoring and through the recommendations of an outside contractor, Meliora Partners, HOCS has assisted HCEOC in reconstituting the Board of Directors, reorganizing or eliminating non-performing programs, liquidating unnecessary or irrelevant assets, partially funding and approving use of HCEOC funds to purchase MIP-SAGE accounting software, as well as provided training funds for the agency. Through continued monitoring and dialogue since the ARRA period, HCEOC has, this past year, achieved an audit with no material misstatements; however the agency continues to have findings relating to timeliness of reporting. We believe the adoption of this new software will modernize and streamline the reporting process and provide more opportunities for checks and balances.*

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### [3] "LACK OF ADEQUATE MONITORING PROCEDURES

**"The State agency did not have adequate monitoring procedures to ensure that the CSBG costs claimed for the Council's program expenditures for salaries and wages, fringe benefits, and shared costs were allowable in accordance with applicable Federal requirements. In a fiscal monitoring report covering the Council's use of CSBG Recovery Act funds, the State agency reported weaknesses related to the Council's personnel and shared costs; however, the State agency concluded that there was no evidence of any misuse or excessive use of CSBG Recovery Act funds and that all reported expenditures were supported with proper documentation. We found, on the contrary, that the Council charged salaries and wages based on budget estimates. In addition, the Council claimed fringe benefits based on the availability of funds without supporting documentation. Finally, the Council's shared costs were not allocated among its programs in reasonable proportion to the benefits received."**

*State Response: The State concurs with this finding, with a few comments. The CSBG funding source is intended to be a flexible, "infrastructure" grant to allow Community Action Agencies to absorb shortcomings in other grants in order to support a wider array of programming. Although the model allows flexibility and is successful in responsible agencies, it can be very detrimental when viewed as agency "duct tape" to repair mismanaged programs. The CSBG Act does not contain sufficient clarity on the State's authority to expand the scope of monitoring to include entire agency budgets, nor does it clearly outline terms such as "reasonable proportion" of allocable costs. In this case, an auditor, the State, and the CAA may have three different interpretations of "reasonableness." Currently, the existing norm for appropriate administrative proportion is 15%, however this is a "best practice" and unenforceable. In lean years, CAA administrative proportions have exceeded this figure and expanded to as much as 50% in some agencies. If a number or percentage were clearly defined at the Federal level, the State would be able to assist the CAA's in achieving this goal.*

*Corrective Action: The State plans to clarify authority in the State contracting negotiation process by inserting provisions in our contracts with the agencies that clarify HOCS' authority to review and monitor the CAAs' agency-wide budgets. However, this is likely to be viewed by Community Action Agencies as an attempt by the State to overstep its authority. Clarity and guidance on acceptable administrative levels and reasonable proportions from the Federal Government would be preferable. Because monitoring is based on sampling, it is already a provision in all contracts that costs found unallowable after the fact will be reimbursed by the contractor.*



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**[4] "RECOMMENDATIONS**

**"We recommend that the State agency:**

- **refund to the Federal Government \$22,602 for unallowable fringe benefit costs,**
- **work with ACF to determine the allowability of \$122,000 that we set aside and refund to the Federal Government any amount determined to be unallowable,**
- **work with the Council to ensure that it allocates shared costs to programs in reasonable proportion to the benefits received, and**
- **strengthen monitoring procedures to ensure that costs claimed are allowable in accordance with applicable Federal requirements."**

***Corrective Actions based on Recommendations:***

- *Once the OIG draft is finalized and approved by ACF-OCS, and a bill for collection is submitted to the State, OCS will submit to HCEOC an invoice for \$22,602 for unallowable costs. HCEOC has agreed the agency was at fault and will reimburse the State.*
- *HOCS will need to have further contact with ACF, once the OIG report is finalized, in order to determine what documents will be sufficient to establish allowability or reasonableness from the Federal perspective. HOCS files monthly reports on outstanding CAA and CSBG issues to the Federal Program Administrator for Region IX, Dr. James Gray, and will continue to report on the HCEOC situation. HCEOC has, along with one other agency, been identified as borderline high-risk. Both of these agencies will receive increased monitoring over the next State Plan cycle. Unlike previous State Plans from Hawaii, the State's monitoring plan will be more clearly defined.*
- *HOCS has already provided funding to train accounting staff and Board members on reasonableness, allowability, and proper allocation, as well as partial funding for MIP Sage software.*
- *As stated above, HOCS has implemented new monitoring tools, assigned a more experienced and capable Program Administrator, and sent the new PA to various trainings to assure understanding of program requirements.*

We believe this document adequately addresses the OIG's findings and are willing to provide any follow up information your office may require. Please contact myself or the CSBG Administrator, En Young, at (808) 586-8675 if you have any additional concerns.

Sincerely,

  
MILA KAAHANUI, MSW  
Executive Director