

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL

AUDIT OF ECONOMIC DEVELOPMENT GRANTS
AND A COOPERATIVE AGREEMENT WITH
EAST TENNESSEE NOT-FOR-PROFIT ORGANIZATIONS

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TABLE OF CONTENTS

	Page
SUMMARY.....	1
PART I - APPROACH AND OVERVIEW.....	3
Introduction.....	3
Scope and Methodology.....	3
Background.....	4
PART II - FINDINGS AND RECOMMENDATIONS	7
1. Payments to the East Tennessee Economic Council.....	7
2. Cash Advance to the East Tennessee Economic Council	11
PART III - MANAGEMENT AND AUDITOR COMMENTS	13

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SUMMARY

The downsizing of Department of Energy (Department) facilities as a result of the end of the Cold War may have a negative impact on many communities that were heavily dependent on Departmental operations for economic stability. To lessen the negative effects on these communities, the Department has encouraged the formation of local community reuse organizations. These organizations determine and sponsor economic development initiatives to offset the local consequences of the Department's downsizing. The Department provided financial assistance to these organizations through grants and cooperative agreements. We initiated this audit to determine whether economic development grants and a cooperative agreement with East Tennessee not-for-profit organizations were achieving the Department's intended purposes.

Overall, we found that a large majority of funds awarded to East Tennessee not-for-profit organizations were being used for their intended purposes. However, significant amounts awarded to the East Tennessee Economic Council (ETEC) were not. For example, ETEC used about \$161,000 to purchase furniture, equipment, and services which were outside the grants' approved scopes of work. Also, ETEC used about \$29,000 to purchase equipment that was not held by ETEC and was not used specifically for grant purposes. These conditions occurred because the Department considered certain types of costs to be allowable even though they were outside the grants' approved scopes of work, and because reviews of ETEC's invoices did not reveal all items that should not have been billed or were billed in error. As a result, the Department reimbursed ETEC about \$220,000 in questionable costs.

Also, Federal regulations require that cash advances be limited to the minimum amount needed to meet grant recipients' immediate cash requirements and that interest earned on cash advances be deposited in the U.S. Treasury. However, the Department advanced ETEC about \$1.4 million more than ETEC needed to establish a revolving loan fund and then allowed ETEC to hold about \$148,000 in interest earned on the advanced funds. This occurred because the Oak Ridge Operations Office officials responsible for awarding and administering these grants were not

familiar with Federal rules on cash advances and interest earned on cash advances.

Management agreed with the findings and recommendations and will take appropriate action to correct the conditions disclosed in the report.

Office of Inspector

General

.PART I

APPROACH AND OVERVIEW

INTRODUCTION

As a result of the end of the Cold War, the Department of Energy (Department) has downsized many of its facilities. This may have a negative impact on many communities that were heavily dependent on Departmental operations for economic stability. To lessen the negative effects on these communities, the Department has encouraged the formation of community reuse organizations that are responsible for acting on behalf of the community to determine and sponsor initiatives to offset the consequences of the Department's downsizing. One such initiative has been the award of economic development grants and cooperative agreements. The objective of the audit was to determine whether economic development grants and a cooperative agreement with East Tennessee not-for-profit organizations were achieving the Department's intended purposes.

SCOPE AND METHODOLOGY

The audit was performed at the Oak Ridge Operations Office from April 10 to July 18, 1996. To accomplish the audit objective, we:

- * Evaluated Departmental guidance for economic development activities;
- * Reviewed Federal regulations governing grants awarded to not-for-profit organizations;
- * Examined grant files, invoices and supporting documentation;
- * Conducted walk-throughs of grantee facilities; and
- * Held discussions with Departmental and grantee personnel.

The audit was conducted in accordance with

generally accepted Government auditing standards for performance audits, and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the objective of the audit. Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. We did not conduct a reliability assessment of computer-processed data because only a very limited amount of computer-processed data was used during the audit.

We held an exit conference with the Program Development Manager, Office of Partnerships and Program Development, Oak Ridge Operations Office, on September 19, 1996.

BACKGROUND

The Oak Ridge Operations Office has awarded economic development grants and a cooperative agreement to several local not-for-profit organizations located in East Tennessee. In an attempt to mitigate the impact on displaced workers and local communities, the Department has awarded six grants and a cooperative agreement to local not-for-profit organizations. Our review covered 5 of the grants and a cooperative agreement worth \$4.5 million. The sixth grant was covered in our prior audit report entitled "Audit of Work Force Restructuring at the Oak Ridge Operations Office," ER-B-95-06. The following table shows the five grants and one cooperative agreement that were included in this review.

GRANT OR COOPERATIVE AGREEMENT	RECIPIENT	AMOUNT
New business development initiative	ETEC	\$2,000,000
Technology 2020 initiative	ETEC	1,500,000
Technical reuse of Departmental facilities	ETEC	100,000
Feasibility studies	ETEC	100,000
21st century jobs initiative	TRV	750,000
Environmental technology transfer	ORWMA	85,000
TOTAL		\$4,535,000

As the table shows, the Department awarded grants to local not-for-profit organizations for new business initiatives, equipment, feasibility studies and various other programs and activities. Four of the five grants were awarded to the East Tennessee Economic Council (ETEC). The fifth grant was awarded to Tennessee's Resource Valley (TRV). Each of these grants was approved by the Director of the Office of Worker and Community Transition. In addition to the five grants, the Department has entered into a cooperative agreement with the Oak Ridge Waste Management Association (ORWMA) in an effort to enhance environmental technology transfer efforts. Each of these organizations and the grants or cooperative agreement they have received from the Department are discussed below.

East Tennessee Economic Council

ETEC was the community reuse organization established to represent the East Tennessee region. Departmental Guidance For Support of Local Economic Development Activities encourages the establishment of community reuse organizations to determine and sponsor the actions the community may take to offset the local consequences of the Department's downsizing. ETEC, a division of the Oak Ridge Chamber of Commerce, is a not-for-profit organization of about 75 businesses and individuals. ETEC was replaced as the community reuse organization by the Community Reuse Organization of East Tennessee in 1995. However, according to ETEC's Director of Small Business Development, as of June 1996, no Departmental grants had been awarded to the new organization.

ETEC has received a total of \$3.7 million from the Department for 4 of the economic development grants included in our review. Each of the four grants is discussed below.

The Department awarded ETEC a \$2 million grant for the New Business Development Initiative. The period of performance for the grant is from September 1, 1994, through August 31, 1999. The grant seeks to foster small business development efforts, incubation efforts, and technology transfer from the Department to small and medium-sized businesses. The majority of the funds were used to establish a \$1.7 million revolving loan fund to provide needed expansion debt capital for small businesses in East Tennessee. The grant also covers salaries, wages, and other direct and indirect costs for the administration of the grant.

The Department awarded a \$1.5 million grant to ETEC for the Technology 2020 initiative. The grant provided for technological equipment to be used on the project, such as video teleconferencing equipment, multi-media presentation and training equipment, and internet equipment. The grant was awarded in February 1994 and initially covered the period February 4, 1994, to February 3, 1995. The grant was modified twice, extending the period through June 30, 1996. As of July 1996, about \$900,000 of the \$1.5 million was expended by the recipient.

The Department awarded a \$100,000 grant to ETEC to provide technical assistance in the reuse of Departmental facilities. The purpose of the grant was to provide funding for ETEC to hire several consultants to conduct land surveys and study tax issues for Oak Ridge Reservation facilities that are not being used by the Department.

The Department awarded a \$100,000 grant to ETEC to study the feasibility of a technology, trade, and exhibition center and a regional industrial center in East Tennessee. ETEC hired consultants to perform each of the respective feasibility studies.

Tennessee's Resource Valley

TRV seeks to organize and focus both public and private energy and resources on the strength of the East Tennessee region to maximize economic benefit. Further, they seek to establish an ongoing process of institutional evolution among the region's government laboratories and public and private organizations in the wake of Federal government downsizing.

The Department awarded TRV a \$750,000 grant for the 21st Century Jobs Initiative Project. The overall purpose of the grant was to mobilize economic leaders and stakeholders to develop an economic strategy for East Tennessee that would reduce dependence on Federal funding and enable the region to be self-supporting in future years.

Oak Ridge Waste Management Association

ORWMA is a not-for-profit organization that represents the interests of 107 environmental concerns in Oak Ridge, Tennessee. ORWMA was organized primarily to develop a heightened level of awareness, both within Tennessee and in the nation, of waste management technical capabilities that exist in the Oak Ridge area. ORWMA acts as a legislative liaison to Washington, D.C., and Nashville on behalf of the ORWMA membership.

The Department has entered into an \$85,000 cooperative agreement with ORWMA to act as the principal point of contact between the Department and ORWMA members in technology transfer efforts. ORWMA recently changed its name to the East Tennessee Environmental Business Association.

In our opinion, the matters discussed in this report identified material internal control weaknesses within the Department that should be considered when preparing the yearend assurance memorandum on internal controls. Detailed management comments are contained in Part III of this report.

PART II

FINDINGS AND RECOMMENDATIONS

1. Payments to the East Tennessee Economic Council

FINDING

Federal regulations stipulate that costs are allowable under grants with not-for-profit organizations provided the costs are ordinary and necessary for performance of the grants' approved statement of work. However, the Oak Ridge Operations Office (Operations Office) reimbursed the East Tennessee Economic Council (ETEC) for costs that were not ordinary and necessary for performance of the grants' approved statements of work. For example, the Operations Office reimbursed ETEC for computers that were used by the Oak Ridge Chamber of Commerce (Chamber) for Chamber operations and for facsimile machines that were used by

Tennessee's Resource Valley (TRV) for TRV operations. Questionable costs were reimbursed to ETEC because the Operations Office considered certain types of costs to be reasonable and allowable even though they were outside the approved statements of work, and because invoice reviews did not reveal billing errors made by ETEC. As a result, the Department reimbursed ETEC \$219,785 in questionable costs.

RECOMMENDATIONS

We recommend that the Manager, Oak Ridge Operations Office:

Closely scrutinize all ETEC invoices to ensure that only costs required for performance of approved statements of work are reimbursed under current and future grants;

Recover \$161,310 used by ETEC to purchase furniture, equipment, and consulting services outside the scope of the Technology 2020 and New Business Development Initiative grants, or appropriately modify the statements of work to include these types of cost;

Recover \$29,384 reimbursed to ETEC and used to purchase equipment for the Chamber and TRV for their operations, or ensure the purchased equipment is returned to Technology 2020;

Recover \$22,891 from ETEC for costs billed in excess of written contractual agreements under the feasibility studies and Technical Assistance in Reuse of Departmental Facilities grants, or require ETEC to modify the subagreements to cover the costs; and

Recover \$6,200 from ETEC for costs reimbursed twice under the Technology 2020 grant.

MANAGEMENT REACTION

Management concurred with the findings and recommendations and agreed to take corrective action. Part III of the report provides detailed management and auditor comments.

DETAILS OF FINDING

GRANT REGULATIONS

Federal regulations stipulate that costs are allowable under grants with not-for-profit organizations provided the costs are ordinary and necessary for the operation of the organization (indirect cost allocations) or for the performance of the grants' approved statements of work (direct costs). Office of Management and Budget Circular A-122, Cost Principles for Nonprofit Organizations, defines the types of costs that are allowable under grants to not-for-profit organizations. The circular states that to be allowable, costs must be reasonable for the

performance of the award. The circular states that to be reasonable, costs should be of a type generally recognized as ordinary and necessary for the operation of the organization or the performance of the award. Costs of the organization's operations may be allocated to a Federal grant provided the costs benefit both the grant and other work and can be distributed in proportion to the benefits received. In order to be necessary for the performance of the award, costs must be consistent with the approved statement of work for the award.

PAYMENTS TO ETEC

We found that the Operations Office reimbursed ETEC \$219,785 in questionable costs. These included \$161,310 for furniture, equipment, and services outside the grants' scopes of work; \$29,384 for equipment not used by ETEC and not used specifically for performance of the grant; \$22,891 for vendor costs in excess of written agreements, and \$6,200 paid for duplicate billings. Each of these conditions is discussed below.

Items Outside the Scope of Work

ETEC used \$141,130 in Departmental funds to purchase office furniture, equipment, and consulting services outside the scope of the Technology 2020 grant. The approved statement of work for the grant stated that ETEC would use Departmental funds to purchase technological equipment needed to initially establish the Technology 2020 project. At the time the grant was awarded, other organizations had agreed to furnish ETEC with funds needed to construct the facility and to manage its daily operations. Notwithstanding the Department's agreement with ETEC, the Operations Office reimbursed ETEC \$119,430 for funds used to purchase lobby furnishings, office furniture, kitchen appliances, and a mailing machine. Also, ETEC was reimbursed \$21,700 used to purchase a multimedia marketing presentation prepared for TRV. None of these items were covered under the grants approved statement of work.

ETEC also used \$20,180 in Departmental funds to purchase furniture and office equipment under its New Business Development Initiative grant. The approved statement of work for this grant provided funding to be used primarily to establish and operate a revolving loan fund to help create new businesses. The statement of work did not specifically provide for Departmental funds to be used to purchase office furniture and equipment.

Equipment Not Used For Grant Purposes

ETEC used Departmental funds provided under its Technology 2020 grant to purchase \$29,384 in equipment that was neither used by ETEC nor used specifically for the Technology 2020 project. Five computers and two computer modems acquired with grant funds were located at the Oak Ridge Chamber of Commerce and were being used for Chamber operations. Additionally, a portable computer, a computer upgrade, a plain paper facsimile machine, and a facsimile-on-demand system (located at and used for TRV

operations) were acquired with ETEC grant funds. Finally, another computer was on loan to the Small Business Resource Center operated by Roane State and Pellissippi State Colleges. None of this equipment was being used for the Technology 2020 program.

Costs in Excess of Written Agreements

ETEC also used \$22,891 in funds awarded for the feasibility studies and technical assistance grants to pay costs billed in excess of written contractual agreements. ETEC paid the firm hired to study the feasibility of the technology, trade, and exhibition center \$2,000 more than the maximum amount agreed to in the fixed-price agreement. This \$2,000 was then billed to and paid by the Department. Additionally, ETEC had a fixed-price agreement for \$8,500 with a consulting firm to conduct studies of land use, infrastructure needs, and utilities under the technical assistance grant. However, ETEC paid the firm \$20,891 in excess of the agreed upon amount for an environmental assessment and various other services not included in the original agreement. Representatives of both ETEC and the consulting firm stated that the additional work was agreed to in meetings but never formalized in a written agreement.

Duplicate Reimbursements

ETEC overbilled \$6,200 in expenditures under the Technology 2020 grant. Equipment acquired for \$1,669 was invoiced individually and in aggregate, resulting in double billing. We also found that a projection screen acquired for \$197 and equipment installation charges of \$282 were paid twice. Finally, ETEC billed the Department \$4,052 for a damaged computer that was also paid for by TRV's insurance company.

OPERATIONS OFFICE REVIEW

Questionable costs were reimbursed under ETEC's grants because the Operations Office considered certain types of costs to be reasonable and allowable even though they were outside the approved statements of work, and because invoice reviews did not reveal errors made by ETEC. When ETEC invoiced the Department for lobby furnishings, office furniture, and kitchen appliances purchased with grant funds, the Operations Office determined that the items were outside the grants' approved statements of work, but they also determined that the costs were reasonable. Therefore, the Operations Office allowed the invoices to be paid even though some of the items were outside the grants' scopes of work. Further, the Operations Office's review of ETEC's invoices did not identify the items mentioned in this report that either should not have been billed or were billed in error. The billing errors were not obvious and were not easily detectable.

QUESTIONABLE EXPENDITURES

As a result of these conditions, the Department reimbursed ETEC \$219,785 in questionable costs. Questionable costs included

\$161,310 for furniture, equipment, and services outside the approved statements of work; \$29,384 for equipment not used by ETEC and not used specifically for grant performance; \$22,891 for costs billed in excess of cost ceilings; and \$6,200 for items that were reimbursed more than once.

2. Cash Advance to the East Tennessee Economic Council

FINDING

Federal regulations require that cash advances be limited to the minimum amount needed to meet grant recipients' immediate cash requirements and that interest earned on cash advances be deposited in the U.S. Treasury. However, the Department advanced ETEC more than the minimum funds needed to meet immediate cash requirements and allowed ETEC to keep interest on the funds advanced. This occurred because the Operations Office officials responsible for awarding and administering this grant were not familiar with Federal rules regarding cash advances. As a result, ETEC received \$1.4 million more than it needed and retained about \$148,000 in interest due the U.S. Treasury.

RECOMMENDATIONS

We recommend that the Manager, Oak Ridge Operations Office:

1.Ensure that any cash advances made under economic development grants are needed for immediate disbursement, and that any interest earned on advance funds is returned to the Department for remittance to the U.S. Treasury; and

2.Recover all interest earned on funds advanced to ETEC to establish the revolving loan fund under the New Business Development Initiative grant and remit the recovered interest to the U.S. Treasury.

MANAGEMENT REACTION

Management concurred with the findings and recommendations and agreed to take corrective action. Part III of the report provides detailed management and auditor comments.

DETAILS OF FINDING

REQUIREMENT FOR CASH ADVANCES AND INTEREST EARNED

Section 600.122, Title 10, of the Code of Federal Regulations (Title 10) establishes rules to be followed by the Department in providing cash advances to grantees and in recovering interest earned on cash advances. Title 10 requires

that cash advances be limited to the minimum amount needed by the receiving organization in carrying out the purpose of the program or project. The timing and amount of cash advances are to be as close as is administratively feasible to the actual disbursements by the recipient organization for program or project purposes. Further, Title 10 requires that recipients maintain advances of Federal funds in interest bearing accounts, and that interest earned on the advances be promptly remitted to the U.S. Treasury.

CASH ADVANCED AND INTEREST EARNED

The Department gave ETEC a \$1.7 million cash advance without requiring ETEC to justify that the entire amount was needed immediately for program outlays. Additionally, the Department did not require ETEC to remit interest earned on the account to the U.S. Treasury.

ETEC requested and received \$1.7 million from the Department, the majority of which was to be used to establish a revolving loan fund to provide expansion debt capital for small businesses in East Tennessee. However, ETEC did not justify the advance of \$1.7 million and did not propose specifically how or when the funds would be disbursed. The Department did not require ETEC to show that the funds were needed for immediate disbursement before giving the funds to ETEC. Although ETEC received the entire amount in a lump sum payment in December 1994, only \$310,000 had been disbursed for loan commitments by December 1995.

In addition, the Department did not require ETEC to return interest accumulated on the revolving loan fund for remittance to the U.S. Treasury. Instead, the terms and conditions of the grant allowed ETEC to add interest earned on the advance to the general loan fund balance available to be loaned out to small businesses.

UNFAMILIARITY WITH REQUIREMENTS

This condition occurred because the Operations Office was not familiar with Federal rules governing cash advances and interest earned on cash advances. Management stated that this was the first grant the Operations Office had awarded to establish a revolving loan fund and the requirements were unclear. Therefore, the Operations Office was not sure how to handle the fund. The cost and price analysis of the grant proposal raised several questions regarding how the revolving loan fund should be handled. However, the questions were never resolved.

FUNDS DUE THE U.S. TREASURY

As a result, ETEC was advanced \$1.4 million more than it needed to establish a revolving loan fund, and retained more than \$148,000 in interest due the U.S. Treasury. ETEC received \$1.7

million in December 1994, and as of December 1995, had only disbursed \$310,000 from the fund. Also, through the end of May 1996, ETEC had accumulated \$148,465 in interest on the \$1.7 million advanced for the revolving loan fund.

PART III

MANAGEMENT AND AUDITOR COMMENTS

Oak Ridge Operations Office concurred with the findings and recommendations and agreed to take corrective actions. Management also agreed with the estimated monetary impact of the report. We consider management's comments to be responsive to our recommendations. Management's specific comments follow.

Finding 1. - Payments to the East Tennessee Economic Council

Recommendation 1. Closely scrutinize all ETEC invoices to ensure that only costs required for performance of approved statements of work are reimbursed under current and future grants.

Management Comments. Management concurred and stated they have an ongoing process to ensure invoices will be scrutinized to determine that costs incurred and payable are explicitly described in the statements of work.

Recommendation 2. Recover \$161,310 used by ETEC to purchase furniture, equipment, and consulting services outside the scope of the Technology 2020 and New Business Development Initiative grants, or appropriately modify the statements of work to include these types of cost.

Management Comments. Management concurred. The Department plans to modify the statements of work by November 1, 1996, to include this type of cost.

Recommendation 3. Recover \$29,384 reimbursed to ETEC and used to purchase equipment for the Chamber and TRV for their operations, or ensure the purchased equipment is returned to Technology 2020.

Management Comments. Management concurred. Oak Ridge Operations Office will direct that ETEC have the equipment returned to Technology 2020 by December 1, 1996.

Recommendation 4. Recover \$22,891 from ETEC for costs billed in excess of written contractual agreements under the feasibility studies and Technical Assistance in Reuse of Departmental Facilities grants, or require ETEC to modify the subagreements to cover the costs.

Management Comments. Management concurred. The Department will direct ETEC to modify their subagreements to reflect actual costs by November 15, 1996.

Recommendation 5. Recover \$6,200 from ETEC for costs reimbursed twice under the Technology 2020 grant.

Management Comments. Management concurred. The Department will direct an adjustment for \$2,148 in double billing and \$4,052 for damaged computer reimbursement after the indirect rate audit and final settlement. The adjustments will be completed by November 30, 1996.

Finding 2 - Cash Advance to the East Tennessee Economic Council

Recommendation 1. Ensure that any cash advances made under economic development grants are needed for immediate disbursement, and that any interest earned on advance funds is returned to the Department for remittance to the U.S. Treasury.

Management Comments. Management concurred and stated that written direction will be provided to clarify requirements for immediate disbursements and need for remittance of interest earned on advance funds and revolving fund loans by November 1, 1996.

Recommendation 2. Recover all interest earned on funds advanced to ETEC to establish the revolving loan fund under the New Business Development Initiative grant and remit the recovered interest to the U.S. Treasury.

Management Comments. Management concurred. The Department will seek reimbursement from ETEC for the exact amount of interest earned from the \$1.7 million advance revolving loan by November 30, 1996.

IG Report No. ER-B-97-01

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