



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Office of Audit Services, Region VI
1100 Commerce Street, Room 632
Dallas, TX 75242

October 21, 2011

Report Number: A-06-11-00035

Ms. Jacquelyn Douglas
Executive Director
Galveston County Community Action Council, Inc.
P.O. Box 3206
Galveston, Texas 77552

Dear Ms. Douglas:

Enclosed is the U.S. Department of Health & Human Services (HHS), Office of Inspector General (OIG), final report entitled *Recipient Capability Audit of Galveston County Community Action Council, Inc.* 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 at (214) 767-8414 or contact Ms. Sylvie Witten, Audit Manager, at (512) 339-3071 or through email at Sylvie.Witten@oig.hhs.gov. Please refer to report number A-06-11-00035 in all correspondence.

Sincerely,

/Patricia Wheeler/
Regional Inspector General
for Audit Services

Enclosure

Direct Reply to HHS Action Official:

Mr. Leon R. McCowan
Regional Administrator, Region VI
Administration for Children and Families
U.S. Department of Health and Human Services
1301 Young Street, Suite 914
Dallas, TX 75202-5433

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**RECIPIENT CAPABILITY AUDIT OF
GALVESTON COUNTY COMMUNITY
ACTION COUNCIL, INC.**



Daniel R. Levinson
Inspector General

October 2011
A-06-11-00035

Office of Inspector General

<http://oig.hhs.gov>

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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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

Title VI of the Omnibus Budget Reconciliation Act of 1981 established Head Start as a Federal discretionary grant program. The major objectives of the Head Start program are to promote school readiness and to enhance the social and cognitive development of low-income children by providing educational, health, nutritional, and social services.

Within the U.S. Department of Health and Human Services, the Administration for Children and Families, Office of Head Start (OHS), administers the Head Start program. In fiscal year (FY) 2010, Congress appropriated \$7.2 billion to fund Head Start's regular operations.

The American Recovery and Reinvestment Act of 2009 (Recovery Act), P.L. No. 111-5, provided an additional \$2.1 billion for the Head Start program during FYs 2009 and 2010. These funds were intended for activities such as expanding enrollment, funding cost-of-living wage increases for employees of Head Start grantees, upgrading centers and classrooms, and bolstering training and technical assistance.

Galveston County Community Action Council, Inc. (the Council), a nonprofit agency, operates a Head Start program that serves approximately 400 3- to 5-year-old children and their families at various locations in Galveston County, Texas. Federal Government grants are the Council's primary funding source. For program year December 1, 2009, through November 30, 2010, OHS awarded approximately \$3.1 million in Federal Head Start funds to the Council. On June 30, 2009, the Council received \$201,022 in Recovery Act funding. The Council also received funds from the U.S. Department of Agriculture, the Community Services Block Grant program, and the Comprehensive Energy Assistance Program.

OBJECTIVE

Our objective was to assess the Council's financial viability and capacity to manage and account for Federal funds and to operate a Head Start program in accordance with Federal requirements.

SUMMARY OF FINDINGS

The Council generally is financially viable and has the capacity to manage and account for Federal funds and to operate a Head Start program in accordance with Federal requirements. However, we identified the following noncompliance issues:

- Fixed-fee contracts for consultants were inadequate.
- Property records had inaccurate information.
- The Council did not adequately segregate duties related to physical inventories.
- Procurement procedures were not complete or not followed.

- Employees did not follow written procedures related to vendor payments.
- Matching contributions were overvalued, unreasonable, not properly documented, and not properly recognized in accounting records.
- The Council did not adequately protect Head Start enrollees' personal information.

These issues occurred because the Council did not have adequate controls over its property and financial management systems. As a result, the Council claimed \$34,700 in unallowable costs for payments to consultants and \$67,100 in unallowable in-kind contributions.

RECOMMENDATIONS

We recommend that the Council:

- refund \$34,700 of unallowable costs for payments made to consultants;
- ensure that all contracts for services require invoices that specify the quantity and type of work provided;
- improve procedures used to maintain property records;
- ensure that individuals who maintain property records are not the same individuals who complete physical inventories;
- add written procedures for purchases in the \$25,000 to \$99,999 price range and ensure that employees follow written procurement procedures;
- ensure that employees follow written procedures for vendor payments;
- strengthen and implement procedures to ensure that (1) donated space and professional services are properly valued, (2) in-kind activities and the amount of time claimed are reasonable, and (3) only reasonable volunteer services are claimed and that services are documented;
- recognize the value of donated space and professional services in its accounting records; and
- use appropriate encryption standards to protect Head Start enrollees' personal information.

THE COUNCIL'S COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

In written comments on our draft report, the Council concurred with several of our findings and described actions it had taken to address them. However, the Council did not agree with our findings related to fixed-fee contracts for consultants and in-kind valuation, reporting, and recognition. The Council's comments are included in their entirety as the Appendix. Nothing in the Council's comments caused us to change our findings or recommendations.

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INTRODUCTION

BACKGROUND

Head Start Program

Title VI of the Omnibus Budget Reconciliation Act of 1981 established Head Start as a Federal discretionary grant program. The major objectives of the Head Start program are to promote school readiness and to enhance the social and cognitive development of low-income children by providing educational, health, nutritional, and social services.

Within the U.S. Department of Health and Human Services, the Administration for Children and Families, Office of Head Start (OHS), administers the Head Start program. In fiscal year (FY) 2010, Congress appropriated \$7.2 billion to fund Head Start's regular operations.

The American Recovery and Reinvestment Act of 2009 (Recovery Act), P.L. No. 111-5, provided an additional \$2.1 billion for the Head Start program during FYs 2009 and 2010. These funds were intended for activities such as expanding enrollment, funding cost-of-living wage increases for employees of Head Start grantees, upgrading centers and classrooms, and bolstering training and technical assistance.

Galveston County Community Action Council, Inc.

Galveston County Community Action Council, Inc. (the Council), a nonprofit agency, operates a Head Start program that serves approximately 400 3- to 5-year-old children and their families at various locations in Galveston County, Texas. The Council is funded primarily through Federal Government grants. For program year December 1, 2009, through November 30, 2010, OHS awarded approximately \$3.1 million in Federal Head Start funds to the Council. On June 30, 2009, the Council received \$201,022 in Recovery Act funding. The Council also received funds from the U.S. Department of Agriculture, the Community Services Block Grant program, and the Comprehensive Energy Assistance Program.

Federal Requirements

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

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

Our objective was to assess the Council's financial viability and capacity to manage and account for Federal funds and to operate a Head Start program in accordance with Federal requirements.

Scope

We performed this review based on a request from OHS. We did not perform an overall assessment of the Council's internal control structure. We reviewed only those internal controls directly related to our audit objective. Our review period was the Council's FY 2010.

We performed our fieldwork at the Council's administrative office in Galveston, Texas, during March and April 2011.

Methodology

To accomplish our objective, we:

- reviewed relevant Federal laws, regulations, and guidance;
- reviewed the Council's accounting, procurement, and financial reporting procedures and interviewed Council officials to gain an understanding of those procedures;
- reviewed Federal Government grant award documentation to determine the Council's Head Start and Recovery Act funding;
- reviewed the Council's audited financial statements for FYs 2006, 2008, and 2009, as well as unaudited financial statements for FY 2010;
- performed ratio analysis from the audited financial statements for FYs 2006, 2008, and 2009 to assess the Council's financial position;
- reviewed the Council's general ledger, timesheets, invoices, bank reconciliations, and other supporting documentation;
- reviewed the Council's property records and performed a physical inventory of selected items at two facilities;
- reviewed monthly reports and supporting documentation for non-Federal share amounts; and
- reviewed the Council's board of directors composition and board meeting minutes.

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

The Council generally is financially viable and has the capacity to manage and account for Federal funds and to operate a Head Start program in accordance with Federal requirements. However, we identified the following noncompliance issues:

- Fixed-fee contracts for consultants were inadequate.
- Property records had inaccurate information.
- The Council did not adequately segregate duties related to physical inventories.
- Procurement procedures were not complete or not followed.
- Employees did not follow written procedures related to vendor payments.
- Matching contributions were overvalued, unreasonable, not properly documented, and not properly recognized in accounting records.
- The Council did not adequately protect Head Start enrollees' personal information.

These issues occurred because the Council did not have adequate controls over its property and financial management systems. As a result, the Council claimed \$34,700 in unallowable costs for payments to consultants and \$67,100 in unallowable in-kind contributions.

FIXED-FEE CONTRACTS FOR CONSULTANTS

Pursuant to 2 CFR part 230, Appendix B, paragraph 37, the reasonableness and allowability of costs for consultant services are determined by multiple factors, including: (1) the nature and scope of the service rendered in relation to the service required; (2) the necessity of contracting for the service, considering the nonprofit organization's capability in the particular area; (3) whether the service can be performed more economically by employees rather than contractors; and (4) the adequacy of the contractual agreement (e.g., description of the service, estimate of the time required, rate of compensation, and termination provisions).

Pursuant to 45 CFR § 74.47, grantees must maintain a system for contract administration to ensure contractor conformance with the terms, conditions, and specifications of the contract and to ensure adequate and timely followup of all purchases. Recipients shall evaluate contractor performance and document, as appropriate, whether contractors have met the terms, conditions, and specifications of the contract.

Pursuant to 2 CFR part 230, Appendix A (A)(2)(g), to be allowable, a cost charged to a grant must be adequately documented.

The Council claimed \$34,700 in consultant costs that were not supported by adequate contractual agreements and did not always have adequate documentation, such as invoices, to support the services provided. Specifically:

- The Council contracted with another Head Start agency to obtain technical training and assistance in 12 areas, including program governance, planning, communication, ongoing monitoring, self assessment, human resources, and fiscal management. The Council paid \$20,000 to the other agency for these services. However, the contract did not require an invoice or other documentation to support the fees, and the Council did not provide any. Rather, the Council provided only training sign-in sheets that did not outline the types of services performed.
- The Council contracted for assistance in preparing an application for a facilities acquisition. The consultant for this contract was the executive director of the agency that provided the technical training and assistance. The scope of work stated that the consultant would provide “technical assistance in the following areas on an as needed basis: a. Facilities Application (Renovation and/or Construction) All technical assistance will be toward preparation of an acceptable facilities application that complies with 45 CFR 1309.” The Council paid the consultant \$7,500. However, the contract did not require documentation to support the fees, and the Council did not provide any.
- The Council contracted for information technology support. The consultant calculated monthly costs based on his estimate of the monthly support required for the Council’s equipment. According to the contract, the consultant was to donate \$28,008 (52 percent) of the total annual contract cost of \$54,228 as an in-kind contribution for the non-Federal share of the cost.¹ The Council allocated \$7,200 of this contract to the Head Start program. Although the consultant provided the Council with an invoice, the invoice did not provide a detailed monthly listing of the services rendered. In addition, the Council did not sign the contract, which incorrectly stated that it was for “a period of 1 year, beginning April 1, 2009 and ending April 30, 2011.”

As a result, the Council claimed \$34,700 for consultant services that were not allowable.

PROPERTY RECORDS

Pursuant to 45 CFR § 74.34(f)(3), grantees are required to maintain accurate records for equipment acquired with Federal funds. The records should include identifying information, including an identification number, such as the model or serial number, and the acquisition date and cost.

The Council’s property records had inaccurate identification numbers, acquisition dates, and cost data. Specifically, during a physical inventory of subjectively selected items at two locations, we found that property records:

- had inaccurate model numbers (five items), serial numbers (nine items), and a Council tag number (one item);
- did not include model numbers (five items) and serial numbers (two items);

¹ We will not consider the in-kind contribution for this contract unallowable because we did not verify the amount actually claimed as in-kind and allocated to the Head Start program.

- did not include the Council tag numbers (two items); and
- had inaccurate acquisition dates and costs for a refrigerator and a computer.

INVENTORY PROCEDURES

Pursuant to 45 CFR § 74.34(f), grantees are required to take a physical inventory of equipment every 2 years and reconcile the results with the equipment records. Pursuant to 45 CFR § 1304.50(g)(2): “Grantee and delegate agencies must ensure that appropriate internal controls are established and implemented to safeguard Federal funds in accordance with 45 CFR § 1301.13.”

The Council did not adequately segregate duties related to physical inventories. Site managers maintained facility inventory logs, performed physical inventories, and provided the results to the Head Start program director. For the most recent inventory in January 2011, the Head Start program director signed a memorandum stating that she had spot checked inventory logs and updated the master inventory log. However, inventories should be completed by individuals who are not also responsible for maintaining the inventory log.

PROCUREMENT PROCEDURES

Pursuant to 45 CFR § 74.44, grantees are required to establish written procurement procedures to avoid purchasing unnecessary items. Furthermore, 45 CFR § 74.45 requires the grantee to document the cost or price analysis in the procurement file for each procurement action.

The Council’s written procedures omitted guidelines related to purchases priced in the \$25,000 to \$99,999 range. According to financial staff, the Council used the procurement procedures for the \$5,000 to \$24,999 price range for all purchases up to \$99,999.

Also, the Council did not always follow its written procedures. For example, the procurement file for a purchase of seven computers included quotes from two vendors rather than three as required by the Council’s procedures. In addition, the Council did not complete a cost or price analysis to document the selection of its vendor.

VENDOR PAYMENTS

Pursuant to 45 CFR § 74.21(b)(7), the grantee’s accounting records should be supported by source documentation. The Council’s written procedures for its accounting system required the accounting department to compare vendor invoices with purchase orders and receiving documents. However, accounting employees stated that they did not always compare receiving reports with invoices prior to payment. For example, the Council paid a \$5,523 invoice for seven computers without obtaining a receiving report that verified receipt.

IN-KIND VALUATION, REPORTING, AND RECOGNITION

Pursuant to 45 CFR § 1301.20, grantees are to provide 20 percent of the total cost of the program through non-Federal share. Pursuant to 45 CFR § 74.23(a), matching contributions, to be acceptable, must be necessary and reasonable for proper and efficient accomplishment of

program objectives and be verifiable from the recipient's records. Pursuant to 45 CFR § 74.23(e), when an employer other than the recipient furnishes the services of an employee, these services shall be valued at the employee's regular rate of pay (plus an amount of fringe benefits that are reasonable, allowable, and allocable, but exclusive of overhead costs), provided these services are in the same skill for which the employee is normally paid. Financial Accounting Standard No. 116 (FAS 116) states that contributions received should be recognized as revenues or gains in the period received and as assets, a decrease in liabilities, or expenses, depending on the form of benefits received. FAS 116 also requires that contributions be measured at their fair value. Eligible contributions include the use of facilities and services that require specialized skills, such as accountants, architects, carpenters, doctors, electricians, lawyers, nurses, plumbers, teachers, and other professionals and craftsmen.

The Council was required to provide \$696,392 in non-Federal share; however, it provided support for \$835,615. The Council included \$67,100 in unallowable in-kind contributions because it overvalued donated space and volunteer professional services. However, we are not recommending repayment because the Council had in-kind contributions in excess of its required match. In addition, the Council did not recognize the value of the non-Federal share for donated space and professional services in its accounting records.

Donated Space

The Council included \$58,300 in unallowable in-kind contributions because it overvalued donated space. The Council overvalued donated space for one center by \$34,200 during FY 2010 because it used a monthly rental rate of \$9,850 rather than \$7,000. The appraised monthly rate of \$9,850 was applicable when the lessor paid all utilities. However, because the Council paid the utilities for the facility, the applicable rate was \$7,000 per month. The Council overstated its match at two other centers because it continued to report non-Federal matching contributions after discontinuing use of the facilities.

Donated Professional Services

The Council included an additional \$8,800 in unallowable in-kind contributions because it overvalued 81 hours of volunteer time for a prekindergarten coordinator. The Council valued the coordinator's time at \$150 per hour even though her hourly pay from the school district was \$41.36. Accordingly, the Council should have used an hourly rate of \$41.36, a difference in FY 2010 of \$8,800.

Volunteer Parent Services

The Council included \$348,825 (42 percent) in in-kind contributions for parent services provided outside of the classroom. The Council prepared Parent-Child Activities Time Sheets (time sheets), which provided an average of 5 hours per week of daily activities to be completed for each child. A significant number of hours recorded for these activities appeared unreasonable because of the types of activities and the age of the children. Examples of activities for which 1 hour per day was reported were, "Make sure you're doing your homework," "Hop, Skip, and Twist 10 times each," and "What are you going to do this summer?" According to a Council official, the Head Start centers did not have enough volunteers, and the non-Federal share

recorded on the time sheets at the beginning of the year was not sufficient. Therefore, the Council decided to enter on the time sheet the amount of time expected for the parent and child to spend on the activity.

Additionally, the Council did not adequately document volunteer services. Forms used to support volunteer services had:

- staff signatures that predated the date parents returned the form, which indicated that staff did not review the forms to ensure that activities had been completed;
- parent signatures dated before activities were completed;
- hours for which there were no documented activities;
- missing parent signatures; and
- activities that did not appear to be allowable program costs or reasonable for the amount of time reported, such as eating breakfast with children for Mother's Day and ensuring that a child's homework was complete.

Recognition of Revenue

The Council did not recognize the value of the non-Federal share for donated space and professional services in its accounting records. The Council received donated space worth \$197,153 and contractor services worth \$28,535 that it should have recognized as revenue in its accounting records.

INFORMATION SECURITY

The Council did not adequately secure its wireless network as required by 45 CFR § 1304.51(g) and the National Institute of Standards and Technology Special Publication 800-48, sections 3 and 4. Council employees used wireless networks to access a Web-based program that maintains information on Head Start enrollees, including physicals, dental information, moves, phone numbers for contacts and referrals, and eligibility information. The wireless routers we tested at two facilities used wired equivalent privacy encryption, which is the weakest encryption available for most routers. Because this type of encryption could have been broken using free software obtained from the Internet, the Council's sensitive data was not secure. Encryption provides additional protection for data that may be stolen or lost.

RECOMMENDATIONS

We recommend that the Council:

- refund \$34,700 of unallowable costs for payments made to consultants;
- ensure that all contracts for services require invoices that specify the quantity and type of work provided;

- improve procedures used to maintain property records;
- ensure that individuals who maintain property records are not the same individuals who complete physical inventories;
- add written procedures for purchases in the \$25,000 to \$99,999 price range and ensure that employees follow written procurement procedures;
- ensure that employees follow written procedures for vendor payments;
- strengthen and implement procedures to ensure that (1) donated space and professional services are properly valued, (2) in-kind activities and the amount of time claimed are reasonable, and (3) only reasonable volunteer services are claimed and that services are documented;
- recognize the value of donated space and professional services in its accounting records; and
- use appropriate encryption standards to protect Head Start enrollees’ personal information.

THE COUNCIL’S COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE

In written comments on our draft report, the Council concurred with several of our findings and described actions it had taken to address them. However, the Council did not agree with our findings related to fixed-fee contracts for consultants and in-kind valuation, reporting, and recognition of revenue. The Council’s comments are included in their entirety as the Appendix. Nothing in the Council’s comments caused us to change our findings or recommendations.

Fixed-Fee Contracts for Consultants

The Council’s Comments

The Council did not concur with our findings and recommendations related to three fixed-fee contracts for consultants. Regarding the contract for training and technical assistance, the Council stated that regulations do not require that an invoice be received before payment is made. In addition, the Council stated that the payment was proper because the consultant “only had to show up and provide specified training for which they did,” that the Council had paid in accordance with a legally binding contract, and that sign-in sheets support the consultant agency’s appearance. Regarding the contract for support of a facilities application, the Council stated that the Regional Office had recommended that the Council obtain assistance to complete the application and that the application and contract were support for the payment. Regarding the contract for an information technology consultant, the Council stated that its policies require consultants’ “invoices to be specific as to ‘services provided,’” and that its policies do not require ““a detailed monthly listing of the services rendered.””

Office of Inspector General Response

For each of the three contracts, documentation was not adequate to verify that payment was reasonable for the services provided. We did not maintain that regulations require an invoice; however, 2 CFR part 230, Appendix A(A)(2)(g), requires that to be allowable, a cost charged to a grant must be adequately documented. In addition, pursuant to 2 CFR part 230, Appendix B, paragraph 37, the reasonableness and allowability of costs for consultant services are determined by multiple factors, including the nature and scope of the service rendered in relation to the service required and the adequacy of the contractual agreement (e.g., description of the service, estimate of the time required, rate of compensation, and termination provisions). To determine the reasonableness of costs for contracts without detailed descriptions of services or time requirements, additional documentation, e.g., an invoice, is needed to compare services provided with the amount paid.

The contract for training and technical assistance did not specify the type or quantity of training required of the consultant agency. The scope-of-work section of the contract required the contractor to provide “Technical training and assistance in the following areas in an ongoing, as needed basis” and provided examples of those areas. Because the contract did not have specific requirements and the Council did not have supporting documentation with sufficient detail to show the amount and type of training that was provided by the contractor, we cannot determine whether the cost was reasonable.

Regarding the facilities application contract, the Council had a contract and submitted a facilities application but did not have any documentation to show the type or amount of work provided by the consultant. The Regional Office recommendation that the Council obtain assistance to complete the application is not a factor in the determination of cost reasonableness.

To determine the reasonableness of costs for the information technology contract, the consultant needs to provide a record of services provided. Because this is a fixed-fee contract, the Council is obligated to pay the consultant the same amount each month, regardless of the number of hours worked by the consultant. Without documentation to show the services rendered, we cannot determine the reasonableness of costs.

In-Kind Valuation, Reporting, and Recognition

The Council’s Comments

The Council did not concur with our findings and recommendations related to in-kind valuation, reporting, and recognition. Regarding in-kind valuation and reporting, the Council said that the findings should not be part of the report because the Council exceeded the amount of non-Federal funding required by the grant award. However, the Council stated that it has strengthened its procedures to ensure that the in-kind contributions it claims are reasonable. Regarding recognition of the value of the non-Federal share for donated space and professional service, the Council stated that recognition is at “the discretion of the non-federal auditor and standards promulgated by the AICPA.”

Office of Inspector General Response

We reported that the Council met its requirement for non-Federal funding. We included these issues in the report because the Council did not value and report non-Federal funding in accordance with Federal requirements.

Financial Accounting Standard No. 116 (FAS 116) requires the recognition of contributions of donated space and professional service. The Financial Accounting Standards Board issued this standard in 1993, and it was to become effective for financial statements issued after 1995. FAS 116 established standards for accounting for contributions; the standards made unacceptable those provisions in the American Institute of Certified Public Accountants' guides that were inconsistent with FAS 116.

APPENDIX

APPENDIX: THE COUNCIL'S COMMENTS

Galveston County Community Action Council

Maj. Ray Tuttoilmondo
President

Jacquelyn R. Douglas
Interim Executive Director

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2627 Avenue M * P.O. Box 3206
Galveston, Texas 77552

September 13, 2011

Ms. Patricia Wheeler
Regional Inspector General for Audit Services
Department of Health & Human Services
Office of Inspector General
Office of Audit Services, Region VI
1100 Commerce Street, Room 632
Dallas, Texas 75242

Re: Report Number: A-06-11-00035

Enclosed are our comments and exceptions to the Office of Inspector General's Findings and Recommendations dated September 2, 2011 in report entitled "Recipient Capability Audit of Galveston County Community Action Council, Inc."

If you have questions, please contact Jacquelyn Douglas at (409) 765-7878.

Cordially,

Jacquelyn R. Douglas

Jacquelyn R. Douglas
Interim Executive Director

combating poverty through communication, consultation, cooperation, coordination

FINDINGS AND RECOMMENDATIONS

The Council generally is financially viable and has the capacity to manage and account for Federal funds and to operate a Head Start program in accordance with Federal requirements. However, we identified the following weaknesses:

- Fixed-fee contracts for consultants were inadequate.
- Property records had inaccurate information.
- The Council did not adequately segregate duties related to physical inventories.
- Procurement procedures were not complete or not followed.
- Employees did not follow written procedures related to vendor payments.
- Matching contributions were overvalued, unreasonable, not properly documented, and not properly recognized in accounting records.
- The Council did not adequately protect Head Start enrollees' personal information.

These weaknesses occurred because the Council did not have adequate controls over its property and financial management systems. As a result, the Council claimed \$34,700 in unallowable costs for payments to consultants and \$67,100 in unallowable in-kind contributions.

FIXED-FEE CONTRACT FOR CONSULTANTS

The Council claimed \$34,700 in consultant Costs that were not supported by adequate contractual agreements and did not always have adequate documentation, such as invoices, to support the services provided. As a result, the Council claimed \$34,700 for consultant services that were not allowable.

RESPONSE TO FINDINGS AND RECOMMENDATIONS

We do not concur.

Training and technical assistance contract for \$20,000.

We do not concur.

There is not a statute or regulation that stipulates that all agreements must be accompanied by an invoice before payments are made. This statement is subjective. GCCAC's policies state that consultants services may also be obtained based on a retainer fee. To be allowable, however, evidence of bona fide services available or rendered must be supported. It was inferred that the

contract was inadequate because the Council provided only sign-in sheets that did not outline the types of services performed. It is documented that services were performed and the payment did not exceed the contractual arrangement. This contract was a fixed fee contract and based on the contract, there were no deliverables. The Head Start Agency only had to show up and provide specified training for which they did. GCCAC paid according to the contract that is a legally binding document. The sign in sheets support the fact that the Head Start Agency appeared. Numerous staff, board and policy council members and community representatives were present at these trainings as evidenced by the sign in sheets.

Facilities Application (Renovation and/or Construction) contract for \$7,500.

We do not concur.

GCCAC's policies state that the need to obtain the services of a consultant may be directed by the Regional Office. Regional Office recommended that GCCAC obtain assistance in preparation of their facilities application to comply with 45 CFR 1309. Again, this was a fixed fee contract. In this instance there was a deliverable i.e., the actual facilities application that was submitted to the Regional Office for approval. Therefore, the support for the fees was the Contract itself and the grant application SF 424. There is not a statute or regulation that stipulates that all agreements must be accompanied by an invoice before payments are made.

Information Technology contract for \$7,200 (Head Start allocation).

We do not concur.

GCCAC's policies require consultants invoices to be specific as to "services provided". Nowhere in the policies does it state that there must be "a detailed monthly listing of the services rendered". The IT consultant's invoice specifies that he provided IT maintenance. This is a personal preference of the OIG reviewer.

All future contracts will be executed by appropriate GCCAC representative as well as consultant. As the OIG representative was told, the period stated in the contract was a typographical error.

In anticipation of this going further we will appeal.

PROPERTY RECORDS

The Council's property records had inaccurate identification numbers, acquisition dates, and cost data.

RESPONSE TO FINDINGS AND RECOMMENDATIONS

We concur.

A physical inventory will be conducted and reconciled to the property records.

INVENTORY PROCEDURES

The Council did not adequately segregate duties related to physical inventories.

RESPONSE TO FINDINGS AND RECOMMENDATIONS

We concur.

Individuals who maintain property records will not be the ones that conduct physical inventory.

PROCUREMENT PROCEDURES

The Council's written procedures omitted guidelines related to purchases priced in the \$25,000 to \$99,999 range. According to financial staff, the Council used the procurement procedures for \$5,000 to \$24,999 price range for all purchases up to \$99,999.

RESPONSE TO FINDINGS AND RECOMMENDATIONS

We concur.

Fiscal procedures are being updated to include written procedures for purchases between \$25,000 to \$99,999 and employees will follow the written procedures.

VENDOR PAYMENTS

The Council's written procedures for its accounting system required the accounting department to compare vendor invoices with purchase orders and receiving documents. However, accounting employees stated that they did not always compare receiving reports with invoices prior to payment.

RESPONSE TO FINDINGS AND RECOMMENDATIONS

We concur.

The fiscal department now obtains receiving reports for deliverables and compares them to invoices prior to payment.

IN-KIND VALUATION, REPORTING, AND RECOGNITION

The Council was required to provide \$696,392 in non-Federal share; however, it provided support for \$835,615. The Council included \$67,100 in unallowable in-kind contributions because it overvalued donated space and volunteer professional services. However, we are not recommending repayment because the Council had in-kind contributions in excess of its required match. In addition, the Council did not recognize the value of the non-Federal share for donated space and professional services in its accounting records.

Donated Space

The Council included \$58,300 in unallowable in-kind contributions because it overvalued donated space. The Council overvalued donated space for one center by \$34,200 during FY 2010 because it used a monthly rental rate of \$9,850 rather than \$7,000. The appraised monthly rate of \$9,850 was applicable when the lessor paid all utilities. However, because the Council paid the utilities for the facility, the applicable rate was \$7,000 per month. The Council overstated its match at two other centers because it continued to report non-Federal matching contributions after discontinuing use of the facilities.

RESPONSE TO FINDINGS AND RECOMMENDATIONS (Donated Space)

EXCEPTION:

We take exception and do not concur with this being made a part of the OIG's report due to the fact that the Council exceeded its match as required by contractual obligation.

Donated Professional Services

The Council included an additional \$8,800 in unallowable matching contributions because it overvalued 81 hours of volunteer time for a prekindergarten coordinator. The Council valued the coordinator's time at \$150 per hour even though her hourly pay from the school district was \$41.36. Accordingly, the Council should have used an hourly rate of \$41.36, a difference in FY 2010 of \$8,800.

RESPONSE TO FINDINGS AND RECOMMENDATIONS (Donated Professional Services)

EXCEPTION:

We take exception and do not concur with this being made a part of the OIG's report due to the fact that the Council exceeded its match as required by contractual obligation.

Alternative Action

GCCAC is currently using the school district's hourly rate.

Volunteer Parent Services

The Council included \$348,825 (42 percent) in non-Federal share for parent services provided outside of the classroom. The Council prepared Parent-Child Activities Time Sheets (time sheets), which provided an average of 5 hours per week of daily activities to be completed for each child. A significant number of hours recorded for these activities appeared unreasonable because of the types of activities and the age of the children.

RESPONSE TO FINDINGS AND RECOMMENDATIONS (Volunteer Parent Services)

EXCEPTION:

We take exception and do not concur with this being made a part of the OIG's report due to the fact that the Council exceeded its match as required by contractual obligation.

Alternative Action

Procedures have been strengthened to ensure that in-kind claimed is reasonable.

Recognition of Revenue

The Council did not recognize the value of the non-Federal share for donated space and professional services in its accounting records. The Council received donated space worth \$197,153 and contractor services worth \$28,535 that it should have recognized as revenue in its accounting records.

RESPONSE TO FINDINGS AND RECOMMENDATIONS

To include this on the financial statements is the discretion of the non-federal auditor and standards promulgated by the AICPA. Therefore, the OIG should remove this recommendation mainly because these are non federal revenues and Government Accounting Standards do not require inclusion in the Statement of Activities.

INFORMATION SECURITY

The Council did not adequately secure its wireless network as required by 45 CFR § 1304.51(g) and the National Institute of Standards and Technology Special Publication 800-48, sections 3 and 4. Council employees used wireless networks to access a Web-based program that maintains information on Head Start enrollees, including physicals, dental information, moves, phone numbers for contacts and referrals, and eligibility information. The wireless routers we tested at two facilities used wired equivalent privacy encryption, which is the weakest encryption available for most routers. Because this type of encryption could have been broken using free software obtained from the Internet, the Council's sensitive data was vulnerable to interception. Encryption provides additional protection for data that may be stolen or lost.

RESPONSE TO FINDINGS AND RECOMMENDATIONS

We concur.

Encryption upgrades are being implemented.