



JUN 13 1996

## Memorandum

Date

*Michael Mangano*

From

for June Gibbs Brown  
Inspector General

Subject

Review of Facility Purchases by the Head Start Program during Fiscal Years  
1993 and 1994 (A-09-94-00085)

To

Mary Jo Bane  
Assistant Secretary for  
Children and Families

Attached is our final audit report titled, "Review of Facility Purchases by the Head Start Program during Fiscal Years 1993 and 1994." The objective of our review was to evaluate the Administration for Children and Families' (ACF) procedures for reviewing, approving, and accounting for purchases of facilities by Head Start grantees to identify possible areas requiring ACF action and to provide information that may be useful in administering the program. This review was initiated at the request of Region X ACF officials who noted problems in implementing this relatively new authority under the Head Start Program.

We identified the following two areas for which we are making recommendations to assist ACF in the further development of policies and procedures: (1) review and approval of purchase requests; and (2) accounting for facility purchases. In response to our draft report, ACF officials generally concurred with our recommendations.

If you have any questions, please call me or have your staff contact John A. Ferris, Assistant Inspector General for Administrations of Children, Family and Aging Audits, at (202) 619-1175. Please provide us with information on any additional actions taken on the recommendations within 60 days of the report issue date.

Attachment

**Department of Health and Human Services**

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF FACILITY PURCHASES  
BY THE HEAD START PROGRAM  
DURING FISCAL YEARS 1993 AND 1994**



**JUNE GIBBS BROWN  
Inspector General**

**JUNE 1996  
A-09-94-00085**

# EXECUTIVE SUMMARY

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## BACKGROUND

Region X personnel at Administration for Children and Families (ACF) requested this review of the implementation of section 644(f) of the Head Start Improvement Act of 1992. This legislation provided a new authority for Head Start grantees to request and obtain approval to purchase facilities for use in carrying out Head Start programs.

The ACF staff informed us that, during Fiscal Years 1993 and 1994, ACF nationwide had approved the purchase of 95 facilities valued at about \$24.1 million with costs for renovations estimated at an additional \$4.4 million. Some of these properties were purchased outright; others were mortgaged over several years with Head Start funds used for down payments, renovations and closing costs.

Our review included ACF regional offices in San Francisco, California and Seattle, Washington. We also met with ACF officials from the Head Start Bureau in Washington, D.C. In addition, we made on-site reviews at 10 selected Head Start grantees in California, Washington, Oregon, and Idaho.

## OBJECTIVE

The objective of our review was to evaluate ACF's procedures for reviewing, approving, and accounting for purchases of facilities by Head Start grantees to identify possible areas requiring ACF action and to provide information that may be useful in administering the program.

## SUMMARY OF RESULTS OF REVIEW

Our review was conducted early in the implementation phase of the new authority to purchase Head Start facilities in order to provide timely information for ACF in administering this program. Prior to starting our review, we held discussions with ACF officials, and they agreed that our review would be beneficial in the continuing effort to develop guidelines for this program.

At the time we began our review, ACF had issued program instructions to grantees and was in the process of developing regulations and program guidelines; this report will be helpful in specifying the information needed to complete this process. Also, in February 1995, the ACF produced a Head Start Facilities Manual to help grantees in the purchasing process by providing tools for assessing their facilities' needs.

In our review, we identified the following two areas for which we are making recommendations to assist ACF in the further development of policies and procedures:

- Review and approval of purchase requests.
- Accounting for facility purchases.

## **Review and Approval of Purchase Requests**

In our review of ACF procedures for reviewing and approving facility purchase requests from Head Start grantees, we identified a number of issues that ACF should address in the management of the program. To address those issues, we are recommending that ACF:

- ▶ continue efforts to develop expertise for providing technical assistance to grantees acquiring or planning to acquire facilities (see Page 4),
- ▶ require that property inspection reports submitted by grantees include the results of tests for environmental hazards (see Page 5),
- ▶ require grantees to disclose any restrictions on the use of the facilities imposed by organizations providing supplemental funding (see Page 5),
- ▶ ensure that all necessary documentation, such as property appraisals and inspection reports, be submitted prior to making grant awards (see Page 6),
- ▶ ensure that purchase requests submitted by grantees describe all renovations that need to be made to the property, and that grantees obtain professional help, if necessary, in determining the need and estimated costs of renovations (see Page 7),
- ▶ require grantees considering loans with balloon payments to disclose these plans, and explain how the balloon payment obligation will be met (see Page 7), and
- ▶ require grantees to consider coordinating the acquisition of Head Start facilities with the facility needs of programs funded by the Administration on Aging, such as senior citizen programs (see Page 8).

In response to the draft report, ACF officials generally concurred with the recommendations for improvements of the review and approval of purchase requests.

## Accounting for Facility Purchases

With regard to ACF's ability to account for facilities purchased with Head Start funds, we identified areas where improvements can be made and are recommending that ACF:

- ▶ continue efforts to develop and implement a system to account for Head Start funds utilized for each facility purchased (see Page 11), and
- ▶ provide guidelines to calculate the Federal interest in properties which are acquired with the assistance of funds provided from other programs and when a portion of the facility is used for other purposes (see Page 11).

In response to the draft report, ACF officials concurred with the recommendations for improvements in the accounting for facility purchases.

## OTHER MATTERS

During our review, we found the following "best practices" which are worthy of consideration for use on a regular basis by ACF:

- ▶ conditions included in grant award documents restricting the use of grant funds specifically to facility purchases (see Page 14), and
- ▶ grantee negotiation of innovative lease provisions that resulted in savings to the Head Start program when the facility was purchased at a later date (see Page 14).

In the Other Matters section, we also note that, if the requirement for accounting for modular buildings as real property remains when the final regulations are issued, ACF will need to develop procedures to account for modular buildings in the same way as other facility acquisitions.

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We have summarized ACF comments after each finding discussed in the report. The complete text of ACF comments is included as an APPENDIX to this report.

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# INTRODUCTION

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## PROGRAM INFORMATION

The Head Start Improvement Act of 1992 amended the Head Start Act by adding section 644(f) which allows grantees to request and obtain approval from the Administration for Children and Families (ACF) to purchase facilities for use in carrying out Head Start programs. Such a request must contain:

- ▶ a description of the site of the facility proposed to be purchased;
- ▶ the plans and specifications of such facility;
- ▶ information demonstrating that: (i) the proposed purchase will result in savings when compared to the costs that would be incurred to acquire the use of an alternative facility to carry out such program, or (ii) the lack of alternative facilities will prevent the operation of such program; and
- ▶ such other information and assurances as the Secretary may require.

The ACF staff informed us that, during Fiscal Years (FY) 1993 and 1994, ACF nationwide had approved the purchase of 95 facilities valued at about \$24.1 million, with costs for renovations estimated at an additional \$4.4 million. Some of these properties were purchased outright; others were mortgaged over several years with Head Start funds used for down payments, renovations, and closing costs.

## SCOPE

Our review was made in accordance with generally accepted government auditing standards. Accordingly, we performed such tests and other auditing procedures as necessary to meet the objective of the review. The objective was to evaluate ACF's procedures for reviewing, approving, and accounting for purchases of facilities by Head Start grantees to identify possible areas requiring ACF action and to provide information that may be useful in administering the program.

Our review was limited to facility purchases by Head Start grantees authorized by section 644(f) of the Head Start Act, as amended by the Head Start Improvement Act of 1992. The review period included Head Start funds awarded in FYs 1993 and 1994 for facility purchases. We did not review grant awards for construction of Head Start facilities which were later authorized under section 644(g) of the Head Start Act, as amended by the Human Services Amendments of 1994.

Our review included ACF regional offices in San Francisco, California and Seattle, Washington. We also met with ACF representatives from the Head Start Bureau in Washington, D.C.

In addition, we made on-site reviews at 10 selected Head Start grantees in California, Washington, Oregon, and Idaho. Grantees selected included those located within the two selected regions which had purchased, or were in the process of purchasing Head Start facilities. We also based our selection on information disclosed by our review of grant files, property values, and specific site locations.

The ACF had been authorizing Head Start grantees to purchase modular buildings prior to enactment of section 644(f) of the Head Start Improvement Act and categorizing the modular buildings as equipment. Because modular buildings were purchased as equipment, we excluded them from our review except in situations where such purchases were being made in connection with a land or building purchase.

The review was conducted from October 1, 1994 through June 30, 1995.

# FINDINGS AND RECOMMENDATIONS

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Our review was conducted early in the implementation phase of the new authority to purchase Head Start facilities in order to provide timely information for Administration for Children and Families (ACF) in administering this program. The ACF had developed program instructions during Fiscal Years (FY) 1993 and 1994, and was in the process of developing regulations and program guidelines.

In our review, we identified the following two areas for which we are making recommendations to assist ACF in the further development of policies and procedures:

- Review and approval of purchase requests.
- Accounting for facility purchases.

## REVIEW AND APPROVAL OF PURCHASE REQUESTS

With regard to the review and approval of purchase requests, we identified the following issues that ACF should address in the management of the program:

- ▶ expertise for providing technical assistance to Head Start grantees,
- ▶ inspections for environmental hazards,
- ▶ restrictions imposed on the use of the facilities by organizations providing funding to supplement the Head Start funds,
- ▶ documentation of property appraisals and inspections,
- ▶ facility purchase request disclosures regarding renovations and financing, and
- ▶ coordination with programs funded by the Administration on Aging (AoA).

## Background

The ACF required that grantees which wanted to acquire facilities for Head Start purposes submit written facility purchase requests to their respective regional offices. The grantees were required to include, as an integral part of the request, certain documentation to justify the facility purchases. The documentation included descriptions of the facilities, relevant data on the selling prices of the facilities and renovation costs, cost versus lease comparisons, appraisal reports, structural inspection reports, and the methods of financing.

The regional ACF staff reviewed and approved or disapproved the facility purchase requests. If a purchase request was approved, the regional ACF staff would issue a grant award to the grantee to be used to acquire the property. Ten days after the property was purchased, the grantee was required to submit to ACF copies of the deed, loan instrument, mortgage, and any other legal documents.

Although the new legislation allowed grantees to purchase facilities, ACF was not given additional funds specifically earmarked for facility purchases. The funds for such purchases had to be obtained from existing Head Start funding. In addition, ACF encouraged grantees to seek supplemental funds, such as grants from city governments and private foundations, to be used with the funds received from the Head Start program.

The Head Start Act includes a nonfederal share requirement for Head Start grantees. Federal regulations require that each grantee include in its purchase request a statement of the effect that the purchase of the facility would have on the grantee's ability to meet the nonfederal share requirement, including whether the grantee is seeking a waiver of its nonfederal share obligation.

## **Technical Assistance**

The ACF needs to develop expertise for providing advice and technical assistance to grantees in areas such as property appraisals, inspections, financing arrangements and other technical issues regarding facility purchases. Since our review was made early in the implementation of the program, ACF was still in the process of developing policies and procedures for administering the program. For example, ACF issued proposed final regulations addressing facility purchases in December 1994, and produced a Head Start Facilities Manual in February 1995.

During our site visits to grantees, they expressed concern that they were not able to obtain sufficient technical advice and guidance from ACF regional staff in such areas as financing, renovations and compliance with the Davis-Bacon and Americans with Disabilities Acts. Also, ACF staff voiced concerns that they had little or no experience in the area of facility acquisitions and did not always feel prepared to provide grantees with technical assistance.

In some cases, grantee personnel had been referred by regional personnel to other grantees for technical assistance. This could result in actions which may not be consistent with Head Start goals and objectives.

To better serve grantees and the Head Start program, the ACF needs to continue efforts to develop expertise for providing technical assistance, such as arranging for specialized training for ACF staff, contracting with private consulting firms, or arranging for assistance from other agencies, such as the Public Health Service, Office of Engineering Services.

## **Inspections for Environmental Hazards**

The ACF required grantees to include structural inspection reports as part of their facility purchase requests, but did not require grantees to include reports showing the results of tests for environmental hazards. Although the structural stability of the buildings to be purchased is very important, there may also be significant environmental hazards associated with the land and building. The presence of environmental hazards can result in facilities that are unusable because the facilities cannot be licensed as safe for children. Also, cleanup of the hazards may be too costly and cause extensive delays in using the Head Start facility. The ACF should be in a position to take any environmental hazards into consideration when deciding whether or not to approve the purchase requests.

During our visits to grantees, we learned that many grantees were purchasing older buildings which are more likely to have certain environmental problems, such as leaking storage tanks, asbestos, lead-based paint, contaminated water supplies, or insect infestations. Also, some grantees were purchasing buildings that had previously been used in commercial enterprises which may be likely to have contamination problems.

To illustrate, one grantee intended to purchase a warehouse for conversion to a Head Start facility. The warehouse had underground tanks that leaked oil into the soil. The grantee's executive director told us that the seller offered to reduce the selling price of the warehouse by \$25,000 if the grantee would assume responsibility for the cleanup. Fortunately, the executive director was experienced in real estate transactions and insisted that the seller clean up the environmental hazard and obtain the proper certification before the sale could be completed. The executive director stated, at the time of our site visit, that the seller had expended over \$50,000 for cleanup and had not yet completed the work. The ACF program staff informed us they were not aware of the environmental hazard at the time the grant was awarded.

The ACF should require that inspection reports submitted by grantees as part of facility purchase requests be expanded in scope, as necessary, to include the results of tests for environmental hazards, such as those described above. Criteria could be established by ACF as to when additional testing is necessary. The grantees should include environmental reports as part of their purchase requests, or justify in the requests why environmental testing was not necessary. If environmental problems are identified and ACF plans to approve the request, ACF should require the seller to eliminate the hazard prior to completion of the purchase.

## **Restrictions Imposed by Supplemental Funding**

The ACF encouraged Head Start grantees to obtain supplemental funds that could be used together with Head Start funds in facility purchases. Grantees may obtain these additional funds from Federal, State, city, and county governments as well as foundations and private businesses.

Although ACF encouraged grantees to obtain supplemental funds, the supplemental funding sources may place restrictions on the funds which are not always consistent with Head Start goals and objectives. The ACF was not always informed of the conditions imposed by the organizations providing the supplemental funds because the restrictions were not disclosed in the purchase requests.

In our review, we found 1 example where a grantee received a loan from a city redevelopment agency that provided 50 percent of the down payment on a building to be purchased. The terms of the loan required the grantee to reserve a specific portion of the purchased facility for rental to for-profit businesses which must give priority to hiring residents of the local neighborhood. The terms of the loan preclude any further expansion by the Head Start program at the purchased site.

The ACF regional personnel who approved the purchase were not informed of the special conditions of the loan. Although they may have approved the purchase even with these restrictions, such restrictions imposed by organizations providing supplemental funds need to be disclosed by grantees in their purchase requests and carefully considered by ACF in the review process to ensure that the purchase is consistent with the Head Start program's goals and objectives.

## **Documentation of Appraisals and Inspections**

The ACF has sometimes approved facility purchase requests from Head Start grantees without having received appraisal and/or inspection reports. This resulted, in part, from the desire to issue grant awards by the end of the FY deadlines. Head Start program instructions required that such documents be submitted as part of the purchase requests. Without the receipt and review of the required appraisal and inspection reports, the Head Start funds could be at risk.

Appraisal and inspection reports are important documents and should be included in the grantees' purchase application packages. The appraisal offers an independent assessment of the value of the facilities. The inspection report provides an assessment of the structural soundness of the facilities.

During our review at one ACF regional office, we determined that, of 10 facility requests approved, the staff did not receive 3 appraisal reports and 6 building inspection reports. Without a review of the appraisal report, ACF staff did not know whether the grantees were paying too much for the buildings. Without a review of the building inspection reports, they did not know if the buildings were structurally sound. Because the staff were relying solely on desk reviews of the purchase requests provided by the grantees when deciding to approve or deny the purchases, the information provided needs to be complete and accurate.

## Facility Purchase Request Disclosures

The ACF has sometimes approved facility purchase requests from Head Start grantees without receiving accurate information on renovation costs or methods of financing the facilities. Grantees did not always disclose renovation costs, and sometimes understated them. Also, some grantees did not fully disclose the financing methods planned for purchasing facilities. Such omissions may result in additional, unanticipated Head Start outlays in subsequent years.

**Renovations.** As part of the facility purchase requests, grantees were required to include detailed estimates of the costs, if any, of remodeling, renovating, or altering facilities in order to make the facilities suitable for the Head Start program.

Grantees did not always disclose renovation costs. Sometimes the disclosure was not made because the grantees planned to obtain supplemental funding to cover the renovations. Supplemental funding is not always assured, and Head Start funds could ultimately be required to pay for these costs. At other times, the renovation costs may not have been anticipated. Specifically, we found that 1 grantee was required by the city to put in a sidewalk, and another grantee needed a \$60,000 elevator.

In our review, we noted that when grantees significantly underestimated the renovation costs, there were indications of a need for professional assistance in estimating the costs. We identified an instance where one grantee did not get professional estimates, but used rough, rule-of-thumb estimates. His estimates were understated by over \$20,000.

The ACF should encourage grantees to include in their facility purchase requests all possible renovation costs necessary to make the facility suitable for the Head Start program. Also, when appropriate, grantees should be encouraged to use the services of professional architects and contractors to determine what renovations are needed and provide reliable estimates of renovation costs.

**Financing.** In addition to disclosures about renovation costs, grantees were required to describe the methods being proposed to purchase the facilities. Some facilities were being purchased outright. However, many facilities were being purchased with down payments and subsequent mortgage payments.

Grantees did not always fully disclose the financing methods planned for purchasing the facilities. Some grantees arranged short-term financing with balloon payments without informing ACF of this fact or without providing information on how they would meet the large obligations when they became due. A loan with a balloon payment is one which allows small regular payments during the term of the loan with all or most of the principal falling due in a large final payment.

We found a situation where 1 grantee purchased a building in FY 1994 with a balloon payment due in 7 years but did not disclose the balloon payment requirement. A second

grantee disclosed that it had a 2-year loan with a balloon payment, but did not provide information on how the payment would be made. During our site visits, the grantees stated that they hoped to either refinance the loans, pay off the mortgages through year-end operating surpluses, or request additional funds from the Head Start program.

If grantees could not refinance or pay down the mortgages with existing Head Start monies, such short-term financing could result in additional, unanticipated requests by grantees for Head Start funds. Or alternatively, if Head Start could not provide the grantees with additional funds because of budgetary constraints, the grantees could face the loss of the facilities. To address these potential problems, ACF should require grantees considering loans with balloon payments to disclose the plans and explain how the balloon payment obligation will be met.

## **Coordination with AoA Programs**

Currently, ACF requires grantees to include statements in their facility purchase requests related to coordination with other service providers in such areas as child care and health. However, at the present time ACF procedures do not specifically include plans for coordination with AoA programs.

In January 1995, we issued a report titled, "Co-located Intergenerational Activities in Department of Health and Human Services' Programs," CIN: A-05-94-00009, which recommended coordination of Head Start programs and facilities with those of AoA on a voluntary basis. The ACF concurred with the recommendation. Accordingly, we are recommending that ACF require grantees to consider coordinating the acquisition of Head Start facilities with the facility needs of AoA programs, and to include in their purchase requests information on their plans, if any.

## **Recommendations**

We recommend that ACF develop guidelines to address the issues identified in our review. Specifically, we recommend that ACF:

1. Continue efforts to develop expertise for providing technical assistance, such as arranging for specialized training for ACF staff, contracting with private consulting firms, or arranging for assistance from other agencies, such as the Public Health Service, Office of Engineering Services.
2. Require that inspection reports submitted by grantees as part of facility purchase requests be expanded in scope, as necessary, to include the results of tests for environmental hazards. If environmental problems are identified and ACF plans to approve the request, ACF should require the seller to eliminate the hazard prior to completion of the purchase.

3. Require grantees to disclose: (i) any restrictions on the use of the facilities imposed by organizations providing supplemental funding, and (ii) the effect, if any, the restrictions could have on the Head Start program.
4. Ensure that all necessary documentation, including appraisal and inspection reports, is submitted prior to making grant awards.
5. Ensure that grantees include in their requests for funds all renovations needed, and, if necessary, that they obtain professional assistance in determining the need and estimated costs of renovations.
6. Require grantees considering loans with balloon payments to disclose the plans and explain how the balloon payment obligation will be met.
7. Require grantees to consider coordinating the acquisition of Head Start facilities with the facility needs of AoA programs and to include in their purchase requests information on these plans, if any.

## ACF Comments

The ACF officials generally concurred with our recommendations. The actions taken or planned by ACF are summarized below and the complete text of ACF comments is included as an APPENDIX to this report.

**Technical Assistance.** The ACF officials stated that the following actions were taken or planned.

- ▶ A Head Start Facilities Manual was published and distributed to grantees, technical assistance providers, and regional offices.
- ▶ A training conference was held which provided a training model for the technical assistance contractor, consultant, and regional office participants to use when providing facility training and workshops.
- ▶ A toll free number was established to allow grantees to access a database of Davis-Bacon prevailing wage information.
- ▶ A database of resources relating to early childhood facilities will be available to grantees.
- ▶ The Head Start Bulletin will devote an entire issue to facility acquisition topics.

**Inspections for Environmental Hazards.** The ACF officials agreed with our conclusion and stated that they would consider requiring that inspection reports, which grantees must submit as part of their facility applications, include the results of tests for environmental hazards, or a justification as to why environmental testing was not necessary.

**Restrictions Imposed by Supplemental Funding.** The ACF officials stated that they would consider requiring grantees to disclose any restrictions on the use of the facilities imposed by organizations providing supplemental funding.

**Documentation of Appraisals and Inspections.** The ACF officials stated that they would emphasize to regional offices the importance of receiving all necessary documentation.

**Facility Purchase Request Disclosures.** The ACF officials stated that they would issue directions to regional offices to carefully scrutinize grantee applications for renovation costs and obtain independent analyses of the costs of proposed purchases, if necessary.

They also stated that they would consider the inclusion of language in the final regulations specifying that information on balloon payments and other unconventional terms be included in the application.

**Coordination with AoA Programs.** The ACF officials stated that they would list AoA programs in the final regulations as an example of social service and health providers which grantees should consider for collaboration.

## **ACCOUNTING FOR FACILITY PURCHASES**

The ACF needs to develop and implement a system to account for facilities purchased with Head Start funds. Without an adequate system to account for the facilities purchased, the Federal interest in the properties is not sufficiently protected.

In addition, ACF needs to clarify the procedures for determining the Federal reversionary interest in the facilities, which would be needed in the event the properties are subsequently sold or otherwise disposed of. Recent regulations for determining Federal reversionary interest do not adequately address situations where Head Start funds are used in conjunction with supplemental funding provided by other sources for acquiring facilities.

### **Requirements of Federal Regulations**

Federal regulations included in 45 CFR Part 1309, dated December 1994, provide that the Federal Government has a reversionary interest in facilities purchased with Head Start funds. The methodology to calculate the Federal reversionary interest is set forth in the revised version of the grants administration regulations, 45 CFR Part 74.2, as follows:

Federal share of real property, equipment, or supplies means that percentage of the property's or supplies' acquisition costs and any improvement expenditures paid with Federal funds. This will be the same percentage as the Federal share of the total costs under the award for the funding period in which the property was acquired (excluding the value of third party in-kind contributions). For property acquired on an amortized basis over more than one funding period, the Federal share will be the percentage of the amount of paid-in equity at the time of disposition.

In order to determine the Federal reversionary interest, ACF needs to maintain information on the total costs expended under the grant awards, Federal costs expended under the grant awards, and the time periods over which the purchases were made. In addition, ACF must maintain information on any improvements made to the facilities.

### **System to Account for Facility Purchases**

Our review determined that ACF regional offices in San Francisco and Seattle did not maintain sufficient information in their Head Start property files. Manual files had been compiled with grantee purchase requests, grant awards, and other real property information. However, the files being maintained were not always complete and did not afford ACF the capability to adequately account for the real property purchased.

Although the regions reviewed were maintaining a permanent file on each facility purchased, the files did not contain documentation on Federal expenditures or information on subsequent renovations. The regional offices were maintaining records for the property on a fragmented basis. That is, information on Head Start funds used for a facility over the life of the facility would need to be obtained from numerous manually-maintained grant files. This would be time consuming, and every file would need to be reviewed to determine the expenditures made for the facility.

The ACF needs to develop and implement a system to account for Head Start funds utilized for each facility purchased and for determining the Federal reversionary interest in the facility. The information needs to be updated on a continuing basis to account for subsequent Head Start payments related to the facility such as mortgage payments and renovations. The ACF officials have advised us that they were contracting for the development of a centralized system to account for the facilities purchased.

### **Federal Reversionary Interest**

Procedures for determining the Federal reversionary interest in facilities acquired with Head Start funds do not address all situations in which supplemental funds from other sources are also used in the purchase. The current procedures involve a calculation of the Federal

reversionary interest based on the percentage of Federal expenditures under the Head Start program to the total expenditures for the program.

The procedures do not account for situations in which: (i) supplemental funds used to purchase the facilities were provided by programs not related to the Head Start program, and (ii) these programs will also be using a portion of the facilities. Using the current procedures to calculate the Federal reversionary interest will result in an overstatement of the Federal share of the property.

One grantee included in our review acquired a facility for \$800,000 with a \$500,000 down payment and a \$300,000 mortgage. Of the down payment, \$250,000 was provided by the Head Start program and \$250,000 was provided by the city's redevelopment agency. The funds provided by the city were not for financing the Head Start program. In providing the funds, the city required that a specific portion of the facility be used to house for-profit businesses employing local residents. Because the city's portion of the down payment was not related to the Head Start program, the funds were accounted for by the grantee separately from Head Start program funds. Therefore, the total down payment for this facility recorded under the Head Start program would be the \$250,000 supplied by the Federal Government.

In a simplified illustration using the current Federal calculation methodology, the Federal percentage of ownership at the time of purchase for the example above would be 100 percent based on Federal Head Start expenditures of \$250,000 to total Head Start expenditures of \$250,000. The methodology does not take into account the portion of the down payment provided by the city nor the portion of future mortgage payments and renovations paid with funds provided from outside the Head Start program.

The ACF needs to provide guidelines to calculate the Federal reversionary interest in properties which are acquired with the assistance of funds provided from other programs and when a portion of the facility is used for other purposes.

## **Recommendations**

We recommend that ACF:

1. Continue efforts to develop and implement a system to account for Head Start funds utilized for each facility purchased and for determining the Federal reversionary interest in the facility.
2. Provide guidelines to calculate the Federal reversionary interest in properties which are acquired with the assistance of funds provided from other programs and when a portion of the facility is used for other purposes.

## ACF Comments

The ACF officials concurred with our recommendations. The actions taken or planned by ACF are summarized below.

**System to Account for Facility Purchases.** The ACF officials stated that work on a system to account for facility purchases has been completed and information on all facility purchases made with Head Start grant funds is being entered into the system.

**Federal Reversionary Interest.** The ACF officials stated that they will issue guidance regarding the calculation of the Federal interest in a facility acquired with several sources of funding or when part of the facility is used for other than Head Start purposes.

## OTHER MATTERS

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### BEST PRACTICES

During our review, we found practices which appear worthy of consideration for use by ACF on a regular basis. These "best practices" are summarized below.

- ▶ One ACF regional office placed restrictive language in grant award documents that limited the use of funds provided specifically to facility acquisitions. If circumstances did not enable the grantees to spend the funds on the facility purchases, they had to return the funds or obtain written approval from the ACF regional office to use the funds for other purposes. This should help ensure that funds designated for facility purchases are used for the intended purposes.
  
- ▶ One grantee leased a facility to which it planned to make extensive renovations. In anticipation of a possible future purchase of the facility, the grantee negotiated with the seller to establish the future selling price of the facility without reflecting the value of the renovations. The grantee subsequently bought the building, and this advance arrangement resulted in Head Start program savings.

### MODULAR BUILDINGS

At the time of our audit field work, modular buildings were accounted for as equipment rather than real property. The ACF required grantees to be responsible for maintaining equipment records, and did not keep its own record of equipment purchased with Head Start funds.

The regulations at 45 CFR 1309.30, which were proposed in December 1994 and pending finalization at the time of our review, made the purchase of modular buildings subject to the requirements of facility purchases, with a few exceptions. If the requirement for accounting for modular buildings as real property remains when the final regulations are issued, ACF will need to develop procedures to account for modular buildings in the same way as other facility acquisitions.

# APPENDIX



DEPARTMENT OF HEALTH & HUMAN SERVICES

ADMINISTRATION FOR CHILDREN AND FAMILIES  
Office of the Assistant Secretary, Suite 600  
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Washington, D.C. 20447

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May 17, 1996

TO: June Gibbs Brown  
Inspector General

FROM: Mary Jo Bane  
Assistant Secretary *MJ Bane*  
for Children and Families

RECEIVED  
MAY 21 1996 3:15  
OFFICE OF THE ASSISTANT SECRETARY  
GENERAL

SUBJECT: OIG Draft Report on "Review of Facility Purchases by the Head Start Program during Fiscal Years 1993 and 1994." (A-09-94-00085)

Thank you for the opportunity to respond to your draft report of findings concerning facility purchases by Head Start programs during fiscal years 1993 and 1994. The report is a thoughtful analysis of the early implementation of the authority given Head Start grantees in 1992 to use grant funds to purchase facilities. It contains information and ideas which will be helpful to us as we finalize our policies in this area. Our comments follow the organization of your report.

Review and Approval of Purchase Requests

1. Technical Assistance

The draft report states that ACF needs to continue efforts to develop expertise for providing technical assistance to grantees seeking help with facilities concerns. We are continuing such efforts and to date the following facilities technical assistance activities have occurred or are planned:

- a. The Head Start Facilities Manual was published and distributed to grantees, technical assistance providers and regional offices last year. The Manual has been a significant source of guidance for grantees seeking help with a variety of facilities issues.
- b. A train-the-trainer conference, held in September 1995, provided a training model for over 40 technical assistance contractors, consultants and Regional Office participants. Facility training and workshops based on the sessions and materials presented at this meeting have been held or are scheduled in many regions.

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- c. Access to a database of Davis-Bacon prevailing wages was set up for grantees, with a recently established toll free number which grantees can use to easily obtain prevailing wage information.
- d. A database of resources on early childhood facilities is almost completed. Beginning in April, grantees will be able to contact our contractor, describe an information need, and be sent an abstract of information and ordering information on the specified topic from such sources as books, articles, or videotapes.
- e. An issue of the Head Start Bulletin devoted entirely to facilities issues will be published later this year. The issue will include contributions from technical assistance contractor facility specialists, consultants and grantees.

## 2. Inspections for Environmental Hazards

We agree with the report's conclusion that "ACF should be in a position to take any environmental hazards into consideration when deciding whether or not to approve" facility purchase requests. The report emphasizes that ACF must know of any environmental hazards of a proposed facility and site which may affect the usefulness and salability of the facility. The Notice of Proposed Rulemaking (NPRM) on facility purchases published on December 1, 1994, specifies that an application for grant funds to purchase a facility must include an assessment of the impact of the proposed acquisition on the human environment if the purchase involves significant renovation or a significant change in land use, but the NPRM does not require a report from the grantee on other environmental hazards of the kind mentioned in the OIG draft report. This is an important point and we will consider following the draft report's recommendation to require that the inspection reports, which grantees must submit as part of their facility applications, include the results of tests for environmental hazards, or a justification as to why environmental testing was not necessary.

## 3. Restrictions Imposed by Supplemental Funding

We agree with the draft report's recommendation and we will consider requiring grantees to disclose any restrictions on the use of the facilities imposed by organizations providing supplemental funding.

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#### 4. Documentation of Appraisals and Inspections

As the draft report states, we require that applications for the purchase of a facility with grant funds include an appraisal and an inspection report of the property. The draft report states that in some cases facility purchases were funded without this documentation having been first obtained. We believe that this finding reflects the fact that the period of the review was confined to the early stages of implementation of this funding authority. The need to assure compliance with this important part of the oversight process will be emphasized to our Regional Offices.

#### 5. Facility Purchase Request Disclosures

**Renovations:** The draft report finds that grantees did not always disclose renovation costs necessary to make a facility suitable for use as a Head Start facility as part of their applications, as required by the NPRM. We will issue directions to our Regional Offices to carefully scrutinize this part of the application and to obtain an independent analysis of the costs of proposed purchases, as allowed by the NPRM, if necessary.

**Financing:** The NPRM requires that grantees include in their application information on the terms of any loans related to the purchase of the facility, and the repayment plans. Despite this, the OIG review found that grantees did not always disclose the financing methods planned for purchasing facilities. In particular, it states that some grantees arranged short-term financing with balloon payments without informing ACF of this fact or without providing information on how they would meet large obligations when they became due. When we issue the Final Rule on facility purchases, we will consider specifying that information on balloon payments or other unconventional terms must be included in the application.

#### 6. Coordination with AoA Programs

The draft report recommends that we require grantees to consider coordinating the acquisition of Head Start facilities with the facility needs of AoA programs. When we issue the Final Rule on purchasing facilities, we will list AoA programs as an example of social service and health providers which grantees should consider for collaboration.

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Accounting for Facility Purchases

1. System to Account for Facility Purchases

The draft report recommends that ACF continue efforts to develop and implement a system to account for Head Start funds utilized for each facility purchased and for determining the federal reversionary interest in the facility. Work on such a system has recently been completed and information on all facility purchases made with Head Start grant funds is now being entered in the system.

2. The draft report recommends that ACF provide guidelines to calculate the federal reversionary interest in properties which are acquired with the assistance of funds provided from other programs and when a portion of the facility is used for other purposes. Calculation of the federal interest in a facility is made with reference to the definitions or formulas found in 45 CFR Part 74 or Part 92, as applicable. We agree that these formulas may be difficult to apply when a grantee purchases a facility with several sources of funding or when part of the facility is used for other than Head Start purposes, and we will issue guidance in this area.

I want to thank you again for the opportunity to comment on this useful and well written report. Please feel free to contact me if we can be of further assistance in this matter.