



U.S. ENVIRONMENTAL PROTECTION AGENCY
OFFICE OF INSPECTOR GENERAL

Catalyst for Improving the Environment

Quick Reaction Report

Costs Claimed under EPA Grant XP98011401 Awarded to the City of Rupert, Idaho

Report No. 09-2-0078

January 12, 2009



Report Contributors: Darren Schorer
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Abbreviations

| | |
|---------|--|
| CADD | Computer-Aided Design and Drafting |
| CFR | Code of Federal Regulations |
| EPA | U.S. Environmental Protection Agency |
| FSR | Financial Status Report |
| Grantee | City of Rupert |
| OIG | Office of Inspector General |
| OMB | Office of Management and Budget |
| Region | Environmental Protection Agency Region 10 |
| USDA-RD | U.S. Department of Agriculture-Rural Development |

Cover photo: City of Rupert's 1.1 million gallon water storage tank, known as "Big Blue."
(Picture taken by OIG staff in June 2008.)



At a Glance

Catalyst for Improving the Environment

Why We Did This Review

The U.S. Environmental Protection Agency (EPA) Office of Inspector General is reviewing Special Appropriation Act Project grants to identify issues warranting further analysis. We selected the City of Rupert (grantee) for one of these reviews.

Background

In 1998, the City of Rupert received an EPA Special Appropriation Act Project grant, XP98011401. The purpose of the grant was to provide Federal assistance of \$2 million to construct a water supply system. The City of Rupert was required to provide local matching funds equal to 45 percent of the EPA-awarded funds.

For further information, contact our Office of Congressional, Public Affairs and Management at (202) 566-2391.

To view the full report, click on the following link:
www.epa.gov/oig/reports/2009/20090112-09-2-0078.pdf

Costs Claimed under EPA Grant XP98011401 Awarded to the City of Rupert, Idaho

What We Found

The grantee did not meet the Title 40 Code of Federal Regulations Part 31 requirements for financial management. In particular, the grantee:

- Claimed unsupported costs,
- Claimed unallowable pre-award costs,
- Claimed unallowable interest costs,
- Claimed unallowable equipment costs, and
- Reported cumulative total project costs that were not supported by accounting records.

Because of the above issues, EPA needs to recover \$63,256 of the \$423,106 in costs questioned under the grant.

What We Recommend

We recommend that EPA Region 10's Regional Administrator disallow \$423,106 and recover \$63,256 in costs questioned under Grant XP98011401.

With the exception of pre-award costs, the grantee concurred with the findings and recommendations in the discussion draft.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

OFFICE OF
INSPECTOR GENERAL

January 12, 2009

MEMORANDUM

SUBJECT: Costs Claimed under EPA Grant XP98011401
Awarded to the City of Rupert, Idaho
Report No. 09-2-0078

FROM: Robert K. Adachi
Director of Forensic Audits

A handwritten signature in dark ink, appearing to read "Robert K. Adachi", is positioned above the printed name in the "FROM:" field.

TO: Elin Miller
Regional Administrator
EPA Region 10

This report contains a time-critical issue the Office of Inspector General (OIG) identified. This report represents the opinion of the OIG and does not necessarily represent the final position of the U.S. Environmental Protection Agency (EPA). EPA managers will make final determinations on matters in this report.

The estimated cost of this report – calculated by multiplying the project's staff days by the applicable daily full cost billing rates in effect at the time – is \$101,3397.

Action Required

In accordance with EPA Manual 2750, Chapter 3, Section 6(f), you are required to provide us your proposed management decision for resolution of the findings contained in this report before any formal resolution can be completed with the recipient. Your proposed decision is due in 120 days, or on May 12, 2009. To expedite the resolution process, please e-mail an electronic version of your proposed management decision to adachi.robert@epa.gov.

We have no objections to the further release of this report to the public. This report will be available at <http://www.epa.gov/oig>. If you have any questions, please contact me at (415) 947-4537 or at the e-mail address above.

Purpose

The Office of Inspector General is reviewing Special Appropriation Act Project grants to identify issues warranting further analysis. This includes reviewing the total project costs incurred by selected grant recipients. During our review of the Special Appropriation Act Project grant awarded to the City of Rupert, Idaho (grantee), we found that the grantee did not meet the Title 40 Code of Federal Regulations (CFR) Part 31 requirements for financial management.

Background

U.S. Environmental Protection Agency (EPA) Region 10 (Region) awarded grant number XP98011401 to the grantee on March 31, 1998. The purpose of the grant was to provide Federal assistance of \$2 million to construct a water supply system. The construction project activities under this grant included a storage facility, new well, distribution lines, and a water treatment process. EPA was responsible for 55 percent of the eligible project costs up to \$2 million and the grantee was responsible for the remaining 45 percent. Total project costs under the grant agreement were \$3.67 million. The grant was amended five times, resulting in a budget and project period that started August 1, 1998, and ended June 30, 2005.

Scope and Methodology

We conducted this performance audit in accordance with generally accepted government auditing standards, except we did not obtain an understanding of the information systems controls. Our results were based on accounting information system output data provided by the grantee and our verification of these data to the corroborating documents, such as cancelled checks and vendor invoices. The generally accepted government auditing 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 objectives.

We conducted our audit from June 2, 2008, to November 4, 2008. We made a site visit to the grantee and performed the following steps:

- Conducted a tour of the facilities.
- Obtained and reviewed grantee support for the cumulative amounts reported for the period ended June 30, 2005, including the grantee's electronic accounting records, invoices, cancelled checks, and contracts.
- Obtained and reviewed the grantee's supporting documentation for payment requests.
- Conducted interviews of grantee personnel.

Findings

The grantee did not meet the Title 40 CFR Part 31 requirements for financial management. In particular, the grantee:

- Claimed unsupported costs,
- Claimed unallowable pre-award costs,
- Claimed unallowable interest costs,
- Claimed unallowable equipment costs, and
- Reported cumulative total project costs that were not supported by accounting records.

Because of the above issues, EPA needs to recover \$63,256 of the \$423,106 in costs questioned under the grant. Table 1 below is a summary of the questioned costs.

Table 1: Summary of Questioned Costs

| Cost Category | Costs Questioned | Note |
|-------------------------------|-------------------------|-------------|
| Costs Claimed | \$3,944,459 | |
| Questioned Costs: | | |
| Unsupported Costs | (86,750) | 1 |
| Pre-award | (35,231) | 2 |
| Interest | (202,697) | 3 |
| Equipment | (98,428) | 4 |
| Total Costs Questioned | \$423,106 | |
| Total Allowable Claimed Costs | \$3,521,353 | |
| EPA Share (55%) | \$1,936,744 | |
| Payments Made | \$2,000,000 | |
| Amount Owed to EPA | \$63,256 | |

Sources: Claimed costs are from the *Financial Status Report*. Costs questioned were based on OIG's analyses of the supporting documentation provided by the grantee.

Note 1: See discussion under **Unsupported Project Costs**.

Note 2: See discussion under **Unallowable Pre-award Costs**.

Note 2: See discussion under **Unallowable Interest Costs**.

Note 3: See discussion under **Unallowable Equipment Costs**.

Unsupported Project Costs

The grantee did not have supporting documentation for \$86,750 of project costs claimed in the final payment request under the grant submitted to the Region during June 2005. Title 40 CFR 31.20 (b)(6) requires expenditures to be supported by source documentation such as invoices and cancelled checks. As a result, we questioned the \$86,750 claimed under the grant.

Unallowable Pre-award Costs

The grantee claimed \$35,231 in costs that under the grant that were unallowable because they were incurred prior to the grant's funding and project periods. Title 40 CFR 31.23(a) states that where a funding period is specified, the grantee may charge to the award only costs resulting from obligations of the funding period. The grantee's payment request submitted to the Region during 1999 included project costs incurred between May 20, 1998 and July 15, 1998. These

costs predated the grant budget and project period start date of August 1, 1998. Therefore, we questioned the \$35,231 of pre-award costs.

Unallowable Interest Costs

The grantee claimed \$202,697 in unallowable interest costs under the grant. The grantee incurred these costs in order to meet its 45 percent match funding requirement under the grant. The grantee's share of the funding was provided from a U.S. Department of Agriculture-Rural Development (USDA-RD) loan of \$1,750,000. However, USDA-RD, as a condition of providing the loan, required the grantee to obtain interim financing from commercial credit sources to fund its share of costs during construction of the project. The grantee obtained the required financing from a commercial lender and claimed \$233,091 in interest costs under the grant. However, the grantee did not offset these costs with the corresponding interest earnings from the proceeds of the interim financing. The grantee deposited the proceeds from the financing in a local government investment pool account. During the period that the interest costs claimed under grant were incurred, the grantee earned \$202,697 in interest from the funds deposited in the local government investment pool.

According to Office of Management and Budget (OMB) Circular A-87, Attachment B.23.b, financing costs (including interest) associated with the otherwise allowable costs of building acquisition, construction, or fabrication, reconstruction, or remodeling are allowable when four conditions are met. One of these four conditions is that the financing is by a bona fide third party external to the governmental unit. However, another of these conditions specifies that interest expense should be offset by interest earned on borrowed funds. As a result, we questioned \$202,697 of the interest costs claimed under the grant. These questioned costs represent the interest earned during the period that the interest costs were incurred.

Unallowable Equipment Costs

The grantee claimed unallowable equipment costs totaling \$98,428. OMB Circular A-87, Attachment A, Section C.1., specifies several factors that must be met in order for costs to be allowable under Federal grant awards. These factors include that costs must be (1) necessary and reasonable for proper and efficient performance and administration of Federal awards, and (2) allocable to Federal awards. The costs itemized in Table 2 were not allowable because they were not necessary for the performance and administration of the grant's scope of work or included in the budget for the grant award.

Table 2: Equipment Costs

| Description | Cost |
|--------------------|-----------------|
| Backhoe | \$66,861 |
| CADD Station | 8,498 |
| Billing Machine | 10,869 |
| Computers | 12,200 |
| Total | \$98,428 |

Source: EPA analysis of City of Rupert data

The grantee purchased a backhoe during the project period and claimed the cost under the grant. The grant award provided funding for construction of the water supply system, but did not provide funding for maintenance of the system. A July 2003 email from the Idaho Department of Environmental Quality to the grantee stated that the EPA project officer agreed that the backhoe could be purchased with grant funds. The email further said that the backhoe would be dedicated to the project during the construction phase and used for maintenance of the system once construction was completed. However, the grantee was unable to provide us with equipment records showing the extent of use for the backhoe during the construction phase. Since the claimed costs for the backhoe were not a necessary cost under the grant, we questioned the \$66,861 claimed under the grant for the cost of the backhoe.

The grantee claimed the cost of a computer-aided design and drafting (CADD) station under the grant. According to the grantee, the equipment was purchased during the project period to run water distribution modeling. However, the grantee could not explain how the CADD station was used for the modeling. The grantee also acknowledged that its engineering contractor generally performed the water distribution modeling during construction phase of the project. Because the grantee could not demonstrate that the CADD station was necessary and benefited the project, we questioned the \$8,498 cost of this equipment claimed under the grant.

The grantee claimed the cost of a billing machine and the maintenance contract for the machine under the grant. The grantee purchased this office equipment during the project period to fold water monthly billings and place them in envelopes for mailing to customers. However, this equipment and maintenance contract was not necessary for the proper and efficient performance and administration of the grant's scope of work. Therefore, we questioned the \$10,869 cost of the billing machine and maintenance contract claimed under the grant.

The grantee also purchased four desktop personal computers during the project period. According to the grantee, these computers were purchased for office administrative purposes, such as preparing monthly billings to water system customers. The grantee was unable to demonstrate that the computers were necessary costs for proper and efficient performance and administration of the construction of the water system. As a result, we questioned the \$12,200 claimed under the grant for the cost of the office computers.

Financial Status Report Was Not Supported by Accounting Records

The cumulative total costs claimed in the grantee's final Financial Status Report (FSR) for the grant were not supported by accounting records as required by 40 CFR 31.20. The grantee submitted the final FSR for the grant to Region 10 in January 2006. This FSR claimed total cumulative project costs of \$3,944,459 under the grant. However, expenditures recorded in the grantee's general ledger accounts as costs incurred under the grant totaled \$3,856,167. Therefore, the total cumulative costs in the FSR exceeded the grant expenditures recorded in the general ledger accounts by \$88,292. Under 40 CFR 31.20(b)(1), the grantee must make accurate, current, and complete disclosure of the financial results of financially assisted activities in accordance with the financial reporting requirements of the grant. Title 40 CFR 31.20(b)(2) requires that grantees also maintain records which adequately identify the source and application of funds provided for financially assisted activities. Therefore, the grantee needs to improve its

accounting system to ensure these Federal reporting and financial management requirements are met.

Potentially Eligible Project Costs

The grantee reportedly incurred additional potentially eligible project costs that EPA has not reviewed or considered for grant reimbursement. Since the grant is officially closed and these costs were never submitted to EPA, we cannot offset other costs questioned with unclaimed costs. We did not evaluate these additional costs to determine whether they were allowable under the grant because they were not included in the grantee's final FSR.

Recommendation

1. We recommend that EPA Region 10's Regional Administrator disallow \$423,106 and recover \$63,256 in costs questioned under Grant XP98011401.

Region 10's and Auditee's Comments

On November 13, 2008, an exit conference was held with representatives from Region 10 and the grantee to obtain their comments regarding the factual accuracy of our discussion draft. With the exception of pre-award costs, the grantee concurred with the findings and recommendations in the discussion draft. We questioned the pre-award costs because the grantee was unable to show during field work that EPA had provided written approval for these costs. However, on November 10, 2008, the grantee provided us with a July 1998 letter from the Region 10 project officer for the grant approving eligible construction costs incurred in advance of the project start date.

The Region did not provide a response to the discussion draft because it did not have sufficient time to work with the city on the findings and recommendations.

OIG Response

Our position remains unchanged on the \$423,106 of questioned costs discussed in the report. With regard to the questioned pre-award costs, the Region's July 1998 letter does not provide an acceptable deviation from the requirement of Title 40 CFR 31.23(a). Under Title 40 CFR 31.6(c), a deviation from the requirement must be obtained from the Director for the EPA Grants Administration Division. We made minor revisions to the report to more clearly explain the basis for questioning the pre-award costs claimed under the grant.

Status of Recommendations and Potential Monetary Benefits

| RECOMMENDATIONS | | | | | | POTENTIAL MONETARY BENEFITS (in \$000s) | |
|-----------------|-------------|---|---------------------|-------------------------------------|-------------------------------|--|---------------------|
| Rec. No. | Page No. | Subject | Status ¹ | Action Official | Planned Completion Date | Claimed Amount | Agreed To Amount |
| 1 | 5 | Disallow \$423,106 and recover \$63,256 in costs questioned under Grant XP98011401. | U | Region 10 Regional Administrator | TBD | \$63 | \$44 |

¹ O = recommendation is open with agreed-to corrective actions pending;
C = recommendation is closed with all agreed-to actions completed;
U = recommendation is undecided with resolution efforts in progress

Appendix A

Distribution

Regional Administrator, Region 10
Director, Office of Wastewater Management, Office of Water
Director, Office of Wastewater Management - Municipal Support Division, Office of Water
Director, Office of Grants and Debarment
Director, Grants and Interagency Agreements Management Division
Agency Follow-up Official (the CFO)
Agency Follow-up Coordinator
Associate Administrator for Congressional and Intergovernmental Relations
Associate Administrator for Public Affairs
Region 10 Audit Follow-up Coordinator
Region 10 Public Affairs Office
Region 10 Special Appropriation Act Project Coordinator
Mayor, City of Rupert, Idaho
Deputy Inspector General