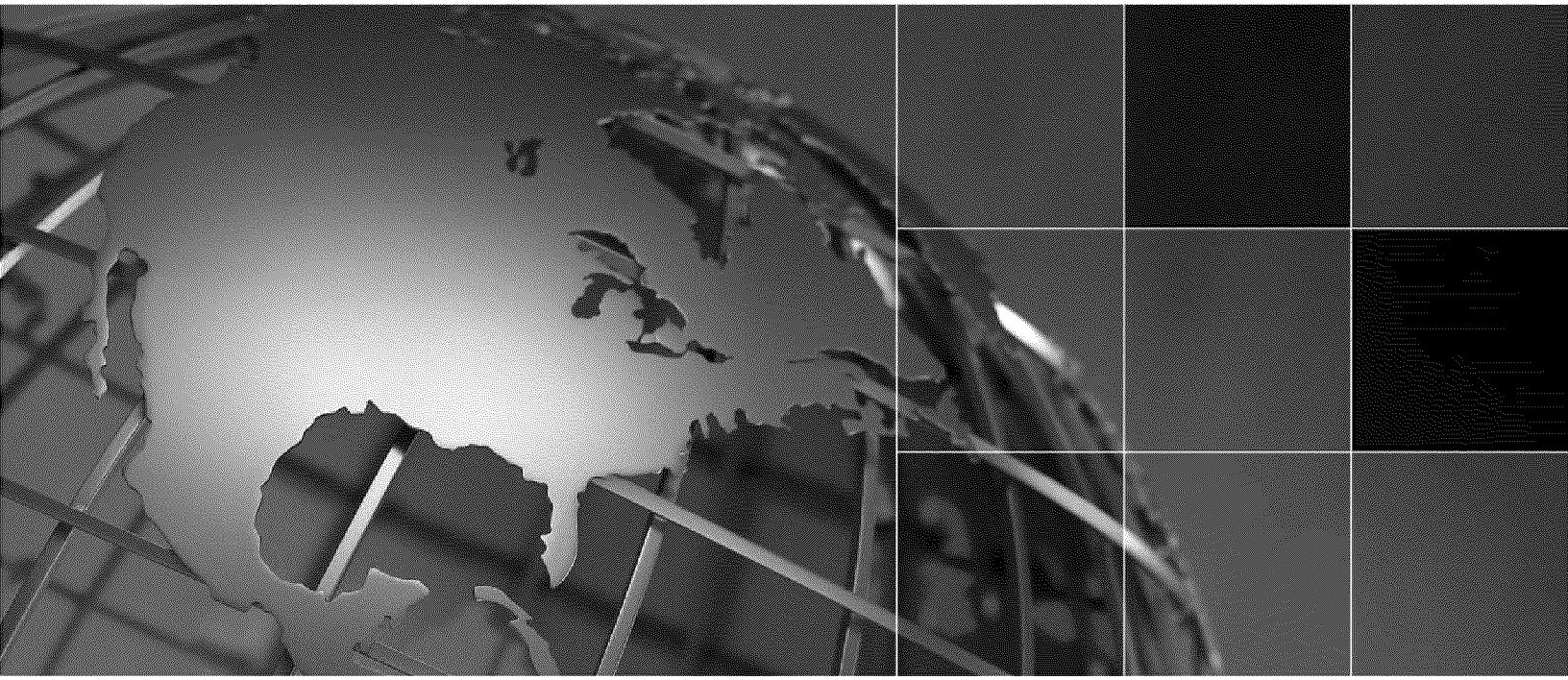

Crowe Horwath™

Town of Palm Beach

Internal Audit Report
Grant Compliance Monitoring
October 2010

Town of Palm Beach

Internal Audit Report
Grant Compliance Monitoring

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I. Executive Summary

OVERVIEW

Crowe Horwath LLP (Crowe) performed an internal audit of the Grant Compliance Monitoring function of the Town of Palm Beach (Town) as of August 30, 2010. The overall objective was to review the controls over Grant Compliance Monitoring. We reviewed grant management policies and procedures, discussed those policies and procedures with Town management, selected specific grant agreements to discuss compliance requirements, and performed limited testing on certain detail records related to reporting of those selected grants.

BACKGROUND

I. General Understanding of Grant Compliance and Monitoring

Federal Grant Regulations - In 1984, (amended 1996), the United States Congress passed the Single Audit Act to consolidate fragmented and inefficient approach to auditing of federal grants. The Federal Office of Management and Budget (OMB) issued Circular A-133, Audits of State, Local Governments, and Non-Profit Organizations, to implement the Single Audit Act. Currently, non federal entities that expend $500,000 or more in federal assistance in a fiscal year are required to undergo an annual comprehensive financial and compliance audit each year.

State Grant Regulations - In 1998, (amended 2000), the Florida Single Audit Act was enacted to establish state audit and accountability requirements for state financial assistance provided to non state entities. The Legislature found that while federal financial assistance passing through the state to non state entities was subject to mandatory federal audit requirements, significant amounts of state financial assistance was being provided to non state entities that was not subject to audit requirements that paralleled federal audit requirements. Accordingly, it was the intent of the Act that state audit and accountability requirements, to the extent possible, parallel the federal audit requirements.

II. Grant Compliance Monitoring

All the departments of the Town of Palm Beach have the ability to apply for federal and/or state grant funding. The grant compliance and monitoring functions are the responsibility of each individual department. The Town of Palm Beach currently has an established grant management policy, which is provided and assessable to all Town departments. A copy of all grant applications and final awards are required to be provided to the finance department. All grant applications that are greater than ten thousand dollars ($10,000) are required to be presented and approved by the Finance Director, Town Manager and Town Council. When the Town of Palm Beach has expended federal or state grant funds that exceed $500,000, the finance department is

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responsible for properly reporting those expenditures on the Schedule of Expenditures of Federal and State Awards. Although all expenditures are tracked in the Eden system, each department tracks grant expenditures differently, in most instances, outside the system in an excel file. The information in the excel file is then compiled for monthly, quarterly, or annual reporting requirements as outlined in the final grant award.

REPORTING METHODOLOGY

In this report, we provide a summary of our results and recommendations as well as management's responses. To assist you in analyzing our recommendations, we have provided our suggestions for corrective action based on the finding's exposure to loss or increased regulatory scrutiny, as follows:

High – Requires *immediate* remedy and, if left uncorrected, exposes the Town to significant or immediate risk of loss, asset misappropriation, data compromise or interruption, fines and penalties, or increased regulatory scrutiny.

Moderate – Requires *timely* remedy and, if left uncorrected, may expose the Town to risk of loss or misappropriation of company assets, compromise of data, fines and penalties, or increased regulatory scrutiny. These issues should be resolved in a timely manner, but after any high priority issues.

Low – Should be addressed as time and resources permit. While it is not considered to represent significant or immediate risk, repeated oversights without corrective action or compensating controls could lead to increased exposure or scrutiny.

Best Practice – Represents operational efficiencies or improvements for consideration by management based on industry best practices and Crowe's experiences.

SUMMARY OF RESULTS

The table below displays the number of recommendations identified through our procedures, categorized by priority.

Risk Rating	Total
High	0
Moderate	1
Low	1
Total	**2**

Best Practice	1

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Detailed observations and recommendations are provided in Section II – Results and Recommendations. These items offer opportunities for the Town to further strengthen controls and processes.

A summary of our observations is as follows:

Overall, we found the internal control environment and procedures related to grant compliance monitoring satisfactory. Our observations primarily related to enhancements of existing polices and procedures that could improve the overall control environment as outlined specifically in each grant compliance supplement and awarded grant agreement. Due to the fact that the Town of Palm Beach currently has not expended federal or state grant funding that would meet the criteria for a Federal and State grant compliance audit, we have determined all the observations would be documented as moderate and below.

Our observations can be summarized as follows:

Moderate:

1. A process should be implemented for specific tracking of expenses related to American Recovery and Reinvestment Act Funds within the general ledger.

Low:

2. Documentation of control procedures related to the compliance requirements of grant funding could be enhanced in the following areas: documentation of the risk assessment process related to grant controls and compliance, separate tracking of grant expenses in the general ledger, documentation of approval of all grant applications in accordance with Town policy, designating a grant compliance coordinator, and implementing additional grant specific internal controls related to approval of grant expenses by those knowledgeable of the grant requirements.

Best Practice:

3. The Town could provide periodic training to supervisors and managers, not in the accounting department, with grant compliance responsibilities.

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II. Results and Recommendations

Finding #1: *A process should be implemented for specific tracking of expenses related to American Recovery and Reinvestment Act Funds within the general ledger.*
Risk Rating: *Moderate*

The Town of Palm Beach currently has been awarded a grant with American Recovery and Reinvestment Act Funds. Organizations that receive grant funding with American Recovery and Reinvestment Act funds must adhere to additional special reporting provisions. The OMG A-133 Circular Appendix VII states:

> "The American Recovery and Reinvestment Act of 2009 (Pub. L. No. 111-5) (ARRA) and the related OMB Guidance (i.e., *Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009* (February 18, 2009); *Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009* (April 3, 2009); and *Updated Guidance on the American Recovery and Reinvestment Act* (March 22, 2010)) located at the OMB Management website http://www.whitehouse.gov/omb/management) have significant implications for audits performed under OMB Circular A-133. The ARRA imposes new transparency and accountability requirements on Federal awarding agencies and their recipients. The key factor in the achievement of accountability is: (1) the recipients and uses of all funds are transparent to the public, and the public benefits of these funds are reported clearly, accurately, and in a timely manner; and (2) funds are used for authorized purposes and instances of fraud, waste, error, and abuse are mitigated."

This transparency mentioned above is outlined in the form of "special provisions". The special provisions outlined on page 21 of the Town's grant award states that ARRA funds must be tracked separately and the organization must ensure funds are not commingled with funds from any other sources. Currently, the town had not received funds from the grant. The ARRA program has an additional website in which organizations have to report funds (expended or awarded and not yet expended), on a quarterly basis. Total distributions of ARRA funds for 2009 were estimated at $787 billion and costs to perform field investigations and inquiry on organizations awarded the funds for 2009 were estimated at 75% of distributed funds. ARRA funds recovery.gov website has a 'Where Is the Money Going' link, which lists all the agencies/organization that have received funding.

Recommendation

The Town should develop within the Eden general ledger system specific accounts for tracking of expenses of ARRA grant funding. These accounts should be separate from any other expenses within a project.

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Management's Action Plan:

The Town received $5,621 on October 26, 2011 for the purchase of a Segway. The revenue was posted to a separate account established for ARRA grant revenue related to the Segway and an expenditure account was established for the purchase of the Segway.

The Town has been awarded one other ARRA grant. The Florida Energy and Climate Commission Grant Agreement No. ARE046, in the amount of $250,000, is to be used to develop a strategy for Town energy efficiency and conservation initiatives, audit and retrofit facilities, purchase hybrid electric vehicles, and host and develop community workshops to engage interest community programs to improve energy efficiency. We will create separate accounts within the General Ledger for any expenditures and revenues relating to this grant. This grant requires monthly reporting to the Florida Energy and Climate Commission. The Deputy Town Manager has been tasked with completing the monthly reports.

The grant policy will be updated to include ARRA requirements.

Individual(s) Responsible: Jane Struder, Finance Director
and Cheryl Somers, Assistant Finance Director

Due Date: January 31, 2011

Finding #2: *Documentation of control procedures related to the compliance requirements of grant funding could be enhanced in several areas to improve the overall control environment.*

Risk Rating: *Low*

Office of Management and Budget (OMB) A-123, Management's Responsibility for Internal Control states:

> "Management is responsible for develop, establishing and maintaining internal control to achieve the objectives of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. Management shall consistently apply the internal control standards to meet each of the internal control objectives and to assess internal control effectiveness. Management must assess the effectiveness of internal control over financial reporting and compliance with financial-related laws and regulations, management must follow the assessment process contained in *Appendix A* of OMB A-123. Programs must operate and resources must be used consistent with agency missions, in compliance with laws and regulations, and with minimal potential for waste, fraud, and mismanagement."

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Office of Management and Budget (OMB), A-133, states:

> "The Senate and House Reports supporting the 1996 Amendments cited studies of the single audit process performed by the Government Accountability Office, the President's Council on Integrity and Efficiency, and the National State Auditors Association (NSAA). The NSAA study stated, "The Compliance Supplement provides an invaluable tool to both Federal agencies and auditors in setting forth the important provisions of Federal assistance programs. This tool allows Federal agencies to effectively communicate items that they believe are important to the successful management of the program and legislative intent. Such a valuable tool requires constant review and update."

We reviewed the Town's policies and procedures over grant compliance and internal control. During this review and inquiry with Town management, we noted five areas of enhancement that would align the current policy with the requirements in the OMB A-133 and Florida Single Audit supplement requirements.

- The grant supplements provided by the State and Federal government require that all organization receiving grant funding perform an internal control risk assessment on current policies in comparison to each of the respective attributes outlined in the grant award letters and compliance supplement, to ensure proper establishment, development and execution of those internal controls. This initially starts with the identification of the attribute requirements per the federal or state matrix. See Appendix C attached. We noted the Town currently does not document the performance of an internal control risk assessment when a grant is obtained or on an annual basis.

- Federal and state compliance supplements require that expenditures of federal and state grant funding should be specifically identified in the general ledger. We noted that the Town does have separate accounts identified for expenditures of the Federal Emergency Management Agency (FEMA) grant.

- The Town's policy outlines a specific dollar threshold of $10,000 for grant applications that are required to be presented before the Town Manager and Town Council for approval. Per our inquiry, this policy is not consistency applied.

- The Town's policy requires that each department that has applied for a grant is to provide the finance department with a copy of any grant application and the grant award to ensure that the finance department is aware of the award and reporting/compliance requirements. Per our inquiry, this policy in not consistently followed; and additional steps are often needed by the finance department to identify grants timely.

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- The control in place to determine if a grant expense is an allowable cost in accordance with the grant agreement and the compliance supplement is the current accounts payable/disbursements cycle process verification. This process may or may not involve an approval by an individual who is involved in the grant process and knowledgeable of the grant requirements.

Recipients of Federal or State grant funds, no matter how material or immaterial to the financial position of the organization, must comply with all applicable state and federal statues, regulations, and policies. Part of those regulations state that management must develop, establish, and maintain proper internal controls and oversight over funding received. If the Town does not develop, establish, and maintain proper internal controls and is found in non compliance could lead to the following:

- Special oversight/review status
- Administrative sanctions
    - Reduction in payments
    - Termination of Grant
- Suspension/debarment/exclusion
- Corrective action plans
- Mandatory compliance plans
- Criminal and Civil Penalties
    - False Statements
    - Criminal and Civil False Claims

Recommendation

- The Town could develop a risk assessment process in accordance with OMB A-123 Appendix A, that would enable the Town to document its performance a grant specific risk assessment at least on an annual basis. Upon receipt of a grant award letter, the Town could go to the respective State or Federal compliance website for the matrix of compliance requirements and the grant specific compliance supplement, to ensure all internal control and compliance attributes identified are clearly documented.

- The Town should develop within the Eden general ledger system specific accounts for tracking of expenses of federal and state funding. These accounts should be separate from any other expenses within a project.

- The Town should consistently apply the policy for approval of grant applications or modify the existing policy if the $10,000 threshold is no longer practical to conform to the current practices in place.

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- As grant funding may increase in the future, the Town could consider designating one individual as a central grants coordinator and consolidating the duties and responsibilities for monitoring compliance, tracking grant applications, following up on grant awards, etc.

- To insure compliance with the allowable cost requirement, grant expenditures should be approved by someone involved in the grant program that is knowledgeable to the program and applicable compliance requirements before the expense is processed for payment. This individual could perform comparisons made with budget and expectations of allowable costs, analytic reviews, and monitor flow of information from the regulatory agencies.

Management's Action Plan:

We will update our Grant policy to include the internal audit recommendations. In addition, as part of our external audit we will perform an internal control risk assessment.

During a storm event, we have accounts in most programs that have been established to track hurricane related expenditures. Most of the expenditures in these accounts are FEMA reimbursable. We will use our project accounting module to track hurricane expenditures for potential FEMA reimbursement.

The Town submits all grant applications to the Town Council for approval regardless of amount. The policy will be updated to reflect the current action. We have requested that each Department submit grant applications to Finance. The Finance Department reviews each Town Council agenda to determine if there are new grants from the Departments to ensure compliance.

A representative from the Department that requested the grant will provide Finance with the expenditures to be claimed for reimbursement under the grant agreement. The departments will perform reviews to ensure grant and budget compliance and a representative from Finance will also perform these reviews.

Amy Wood, Accounting Supervisor will be designated as the central grants coordinator.

Individual(s) Responsible: Jane Struder, Finance Director
and Cheryl Somers, Assistant Finance Director
Due Date: January 31, 2011

Finding #3: *The Town could provide periodic training to supervisors and managers, not in the accounting department, with grant compliance responsibilities.*
Risk Rating: *Best Practice*

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The finance department is proactive in attending grant specific compliance training; however, we noted that other department employees outside of the finance department have not attended training related to grant compliance. Without proper training, department employees charged with the responsibility of making the determination of eligible costs, compliance with reporting requirements, and monitoring of other grant internal control requirements, could potentially not identify a non compliance on a timely basis which could result in deficiencies in the internal control and compliance reports.

Recommendation

We recommend that department employees that have responsibilities for administering grant funds participate in periodic grant training. .

Management's Action Plan:

We will provide training regarding grant compliance responsibilities and procedures to individuals responsible for grant monitoring and compliance in departments other than Finance.

Individual(s) Responsible: Jane Struder, Finance Director and
Cheryl Somers, Assistant Finance Director
Due Date: Initial Training by May 31, 2011 and Ongoing Thereafter

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III. Summary of Scope

The specific procedures performed were based on the concepts of selective testing. Although our testing was performed in some areas without exception, we can provide no assurance that exceptions would not have been detected had procedures been changed or expanded.

It should also be recognized that internal controls are designed to provide reasonable, but not absolute, assurance that errors and irregularities will not occur, and that procedures are performed in accordance with management's intentions. There are inherent limitations that should be recognized in considering the potential effectiveness of any system of internal controls. In the performance of most control procedures, errors can result from misunderstanding of instructions, mistakes in judgment, carelessness, or other factors. Internal control procedures can be circumvented intentionally by management with respect to the execution and recording of transactions, or with respect to the estimates and judgments required in the processing of data. Controls may become ineffective due to newly identified business or technology exposures. Further, the projection of any evaluation of internal control to future periods is subject to the risk that the procedures may become inadequate because of changes in conditions, and that the degree of compliance with procedures may deteriorate.

Scope of Work
1. Determine that the organization has established internal controls to provide reasonable assurance that it complies with the laws and regulations and provisions of contracts and grant agreements. 2. If an award/grant agreement requires the organization to monitor the recipient's or sub-recipient's activities, obtain and review documentation of the organization's monitoring. 3. Determine whether all parties to the agreement have met the award/grant agreement requirements and that all requirements were met on a timely basis.

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Appendix A - Compliance Supplement Example

A. ACTIVITIES ALLOWED OR UNALLOWED

Compliance Requirements

The specific requirements for activities allowed or unallowed are unique to each Federal program and are found in the laws, regulations, and the provisions of contract or grant agreements pertaining to the program. For programs listed in this Supplement, the specific requirements of the governing statutes and regulations are included in Part 4 – Agency Program Requirements or Part 5 – Clusters of Programs, as applicable. This type of compliance requirement specifies the activities that can or cannot be funded under a specific program.

In addition, ARRA has established a cross-cutting unallowable activity for all ARRA-funded awards. Pursuant to Section 1604 of ARRA, none of the funds appropriated or otherwise made available in ARRA may be used by any State or local government, or any private entity, for any casino or other gambling establishment, aquarium, zoo, golf course, or swimming pool.

Source of Governing Requirements

The requirements for activities allowed or unallowed are contained in program legislation or, as applicable, ARRA, Federal awarding agency regulations, and the terms and conditions of the award.

Audit Objectives

1. Obtain an understanding of internal control, assess risk, and test internal control as required by OMB Circular A-133 §___.500(c).

2. Determine whether Federal awards were expended only for allowable activities.

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Appendix B- Internal Control Supplement Example

June 2010 Internal Control A-133 Compliance Supplement 6-1

PART 6 - INTERNAL CONTROL INTRODUCTION

The A-102 Common Rule and OMB Circular A-110 (2 CFR part 215) require that non-Federal entities receiving Federal awards (i.e., auditee management) establish and maintain internal control designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements. OMB Circular A-133 requires auditors to obtain an understanding of the non-Federal entity's internal control over Federal programs sufficient to plan the audit to support a low assessed level of control risk for major programs, plan the testing of internal control over major programs to support a low assessed level of control risk for the assertions relevant to the compliance requirements for each major program, and, unless internal control is likely to be ineffective, perform testing of internal control as planned.

This Part 6 is intended to assist non-Federal entities and their auditors in complying with these requirements by describing, for each type of compliance requirement, the objectives of internal control, and certain characteristics of internal control that, when present and operating effectively, may ensure compliance with program requirements. However, the categorizations reflected in this Part 6 may not necessarily reflect how an entity considers and implements internal control. Also, this part is not a checklist of required internal control characteristics. Non-Federal entities could have adequate internal control even though some or all of the characteristics included in Part 6 are not present. Further, non-Federal entities could have other appropriate internal controls operating effectively that have not been included in this Part 6. Non-Federal entities and their auditors will need to exercise judgment in determining the most appropriate and cost effective internal control in a given environment or circumstance to provide reasonable assurance for compliance with Federal program requirements.

The objectives of internal control pertaining to the compliance requirements for Federal programs (Internal Control Over Federal Programs), as found in §____.105 of OMB Circular A-133, are as follows:

(1) Transactions are properly recorded and accounted for to:
   (i) Permit the preparation of reliable financial statements and Federal reports;
   (ii) Maintain accountability over assets; and
   (iii) Demonstrate compliance with laws, regulations, and other compliance requirements;

(2) Transactions are executed in compliance with:
   (i) Laws, regulations, and the provisions of contracts or grant agreements that could have a direct and material effect on a Federal program; and
   (ii) Any other laws and regulations that are identified in the compliance supplements; and

(3) Funds, property, and other assets are safeguarded against loss from unauthorized use or disposition.

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Appendix C- Matrix Example

CFDA	Types of Compliance Requirements													
	A. Activities Allowed or Unallowed	B. Allowable Costs/Cost Principles	C. Cash Management	D. Davis-Bacon Act	E. Eligibility	F. Equipment and Real Property Management	G. Matching, Level of Effort, Earmarking	H. Period of Availability of Federal Funds	I. Procurement and Suspension and Debarment	J. Program Income	K. Real Property Acquisition/ Relocation Assistance	L. Reporting	M. Subrecipient Monitoring	N.** Special Tests And Provisions
10 – United States Department of Agriculture (USDA)														
10.001*	Y	Y	Y			Y		Y	Y	Y		Y		Y
10.500	Y	Y	Y			Y	Y	Y	Y	Y		Y	Y	
10.551 10.561	Y	Y	Y		See Part 4	Y	Y	Y	Y			Y	Y	Y
10.553 10.555 10.556 10.559	Y	Y	Y		Y	Y	Y	Y	Y	Y		Y	Y	Y
10.557	Y	Y	Y		Y	Y		Y	Y	Y		Y	Y	Y
10.558	Y	Y	Y		Y	Y	Y	Y	Y			Y	Y	Y
10.566	Y	Y	Y		Y	Y	Y	Y	Y			Y	Y	Y
10.568 **10.569**	Y	Y	Y	Y	Y	Y	Y	Y	Y			Y	Y	Y
10.582	Y	Y	Y		Y	Y	Y	Y	Y			Y	Y	
10.665 10.666	Y	Y	Y				Y		Y					
10.760	Y	Y	Y	Y		Y	Y	Y	Y			Y		Y
10.766	Y	Y	Y	Y		Y		Y	Y			Y		Y
11 – Department of Commerce (DOC)														

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CFDA	Types of Compliance Requirements													
	A. Activities Allowed or Unallowed	B. Allowable Costs/Cost Principles	C. Cash Management	D. Davis-Bacon Act	E. Eligibility	F. Equipment and Real Property Management	G. Matching, Level of Effort, Earmarking	H. Period of Availability of Federal Funds	I. Procurement and Suspension and Debarment	J. Program Income	K. Real Property Acquisition/ Relocation Assistance	L. Reporting	M. Subrecipient Monitoring	N.** Special Tests And Provisions
11.300 11.307	Y	Y	Y	Y		Y	Y	Y	Y	Y	Y	Y	Y	Y
11.555	Y	Y	Y			Y	Y	Y	Y			Y	Y	
11.557	**Y**	**Y**	**Y**	**Y**		**Y**	**Y**	**Y**	**Y**	**Y**		**Y**		**Y**
11.558	**Y**	**Y**	**Y**				**Y**	**Y**	**Y**			**Y**		**Y**

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