



DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Memorandum

Date SEP 2 1997

From June Gibbs Brown
Inspector General *June G Brown*

Subject Audit of Training Contract Costs Claimed for Federal Reimbursement
by the Washington State Department of Social and Health Services
(A-10-96-00004)

To Olivia A. Golden
Principal Deputy Assistant Secretary
for Children and Families

Bruce C. Vladeck
Administrator
Health Care Financing Administration

This memorandum is to alert you to the issuance on September 4, 1997 of our final audit report. A copy is attached.

The objective of our audit was to determine if training contract costs claimed by the Washington State Department of Social and Health Services (DSHS) for Federal reimbursement were allowable under Federal regulations and policies.

We found that DSHS claimed Federal reimbursement of \$5.6 million for unallowable costs relating to staff training contracts for the period July 1, 1989 through June 30, 1995. The unallowable costs related to six contracts with Western Washington University, which was the largest external source utilized for staff training during our audit period. We found that the State (i) used unallowable third-party contributions to meet the matching requirements under certain Federal programs, (ii) claimed costs for university employees in excess of actual costs incurred, (iii) claimed unallowable costs for facilities, equipment, and other miscellaneous items, and (iv) did not always properly allocate training costs between federally participating and nonparticipating programs.

We are recommending that DSHS implement various procedural changes and improvements to ensure that unallowable costs are not claimed for Federal reimbursement under staff training contracts, and that the State refund \$5.6 million to the Federal Government. We are also recommending that the State determine the amount of third-party contributions inappropriately claimed subsequent to our audit period and make a financial adjustment to refund the additional amounts overclaimed.

In response to the draft report, DSHS officials agreed to refund \$1,287,158, and disagreed with recommendations for refunding the balance of \$4,340,233. The agreed-on amounts included \$53,818 of

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unallowable third-party in-kind contributions; \$1,002,109 of overclaimed employee costs; \$189,983 of overclaimed or duplicated costs for space, equipment and administration; and, \$41,248 of improperly allocated costs. The disagreed-on amount represents recommended refunds for unallowable third-party in-kind contributions.

The State officials disagreed with the procedural recommendations in the report involving third-party in-kind contributions except as the recommendations applied to the Refugee Resettlement program. The State officials also did not agree with our recommendation for identifying and refunding third-party contributions inappropriately claimed subsequent to our audit period. The basis for disagreement was generally the interpretation of the provisions of Federal regulations and other criteria for the various Federal programs included in the audit.

Any questions or comments on any aspect of this memorandum are welcomed. Please call me or have your staff contact:

Lawrence Frelot
Regional Inspector General
for Audit Services, Region IX
50 United Nations Plaza, Room 171
San Francisco, CA 94102
(415) 437-8360

Attachment

Department of Health and Human Services

**OFFICE OF
INSPECTOR GENERAL**

**AUDIT OF TRAINING CONTRACT COSTS
CLAIMED FOR FEDERAL
REIMBURSEMENT BY THE
WASHINGTON STATE DEPARTMENT OF
SOCIAL AND HEALTH SERVICES**



JUNE GIBBS BROWN
Inspector General

AUGUST 1997
CIN: A-10-96-00004



Region IX
Office of Audit Services
50 United Nations Plaza
Room 171
San Francisco, CA 94102

CIN: A-10-96-00004

Lyle Quasim, Secretary
Department of Social and Health Services
State of Washington
P.O. Box 45010
Olympia, WA 98504-45010

Dear Mr. Quasim:

Enclosed are two copies of the U.S. Department of Health and Human Services (HHS), Office of Inspector General (OIG), Office of Audit Services' (OAS) report entitled, "AUDIT OF TRAINING CONTRACT COSTS CLAIMED FOR FEDERAL REIMBURSEMENT BY THE WASHINGTON STATE DEPARTMENT OF SOCIAL AND HEALTH SERVICES."

Final determination as to actions taken on all matters reported will be made by the HHS action official named below. We request that you respond to the HHS action official within 30 days from the date of this letter. Your response should present any comments or additional information that you believe may have a bearing on the final determination.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG, OAS reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act which the Department chooses to exercise.
(See 45 CFR Part 5.)

To facilitate identification, please refer to Common Identification Number (CIN) A-10-96-00004 in all correspondence related to this report. Thank you for the courtesy extended our auditors during the audit.

Sincerely yours,

Lawrence Frelot
Regional Inspector General
for Audit Services

Enclosure

Direct Reply to HHS Action Official:

Director, Division of Audit Resolution
Office of Grant and Acquisition Management
Assistant Secretary of Management and Budget
U.S. Department of Health and Human Services
Wilbur J. Cohen Building, Room 1067
330 Independence Avenue, S.W.
Washington, D.C. 20201

EXECUTIVE SUMMARY

BACKGROUND

This final report presents the results of our audit of training contract costs claimed for Federal reimbursement by the Washington State Department of Social and Health Services. The training was provided to State employees with responsibilities in the social and health service areas to provide the staff with the necessary skills to accomplish the objectives of the various programs administered by the Department. Although many training needs were met through internal resources, a substantial amount of training was obtained through contracts with outside organizations such as educational institutions and independent contractors.

OBJECTIVE

Our objective was to determine if training contract costs claimed by the Department of Social and Health Services for Federal reimbursement were allowable under Federal regulations and policies. Specifically, we wanted to determine if the State:

- ▶ claimed third-party contributions as the State's required matching share of training contract costs only as allowed by Federal regulations,
- ▶ adequately documented and supported the matching share of training contract costs claimed for Federal reimbursement, and
- ▶ appropriately allocated training contract costs between federally participating and nonparticipating programs.

SUMMARY OF FINDINGS AND RECOMMENDATIONS

The Department of Social and Health Services claimed Federal reimbursement of \$5.6 million for unallowable costs relating to staff training contracts with performance periods during the period July 1, 1989 through June 30, 1995. The unallowable costs related to six contracts with Western Washington University, which was the largest external resource utilized for the staff training during our audit period. We found that the State (i) used unallowable third-party contributions to meet the matching requirements under certain Federal programs, (ii) claimed costs for WWU employees in excess of actual costs incurred, (iii) claimed unallowable costs for facilities, equipment, and other miscellaneous items, and (iv) did not always properly allocate training costs between federally participating and nonparticipating programs.

We are recommending that the Department of Social and Health Services implement various procedural changes and improvements to ensure that unallowable costs are not claimed for Federal reimbursement under staff training contracts, and that the State refund \$5,627,391 to the Federal Government. We are also recommending that the State determine the amount of third-party contributions inappropriately claimed subsequent to our audit period and make a financial adjustment to refund the additional amounts overclaimed.

In response to the draft report, Department of Social and Health Services officials agreed to refund \$1,287,158, and disagreed with recommendations for refunding the balance of \$4,340,233. The agreed-on amounts included \$53,818 of unallowable third-party in-kind contributions; \$1,002,109 of overclaimed employee costs; \$189,983 of overclaimed or duplicated costs for space, equipment and administration; and, \$41,248 of improperly allocated costs. The disagreed-on amount represents recommended refunds for unallowable third-party in-kind contributions. The State officials disagreed with the procedural recommendations in the report involving third-party in-kind contributions except for the recommendations involving the Refugee Resettlement program. The State officials also did not agree with our recommendation for identifying and refunding third-party contributions inappropriately claimed subsequent to our audit period. The basis for disagreement was generally the interpretation of the provisions of Federal regulations and other criteria for the various Federal programs included in the audit.

We have summarized the Department of Social and Health Services comments and the Office of Audit Services response to those comments, as appropriate, after each finding discussed in the report. The complete text of the comments is included as APPENDIX C to this report.

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INTRODUCTION

We performed an audit of training contract costs claimed for Federal reimbursement by the Washington State Department of Social and Health Services (DSHS). The objective of our audit was to determine whether costs claimed for Federal reimbursement by DSHS for staff training contracts were allowable under Federal regulations and policies.

BACKGROUND

The DSHS has the responsibility for the training of departmental personnel in the social and health service areas so that they have the necessary skills to accomplish the objectives of the programs administered by the Department. While many training needs were met through internal resources, a substantial amount of training was provided through contracts with educational institutions, consultants, and other independent contractors and organizations.

The training contract costs incurred by DSHS were allocated in part to Federal programs and claimed for reimbursement from the Federal Government. During the period covered by our audit, these Federal programs, as contained in the applicable titles of the Social Security Act, were as follows:

Title	Federal Program
IV-A	Aid to Families with Dependent Children (AFDC)
IV-D	Child Support Enforcement
IV-E	Foster Care and Adoption
IV-F	Job Opportunities and Basic Skills (JOBS)
XVI	Supplemental Security Income
XIX	Medicaid
XX	Social Services

In addition, DSHS charged training contract costs to the Refugee Resettlement program, authorized under title IV of the Immigration and Nationality Act, and to the Food Stamp program operated under the provisions of title 7, Chapter 51 of the United States Code.

The Federal Government participates in the costs of training provided under the above programs at various Federal financial participation (FFP) rates, generally ranging from 50 percent to 90 percent of allowable costs. The Refugee Resettlement program contains provisions for reimbursement at 100 percent of allowable costs. As a condition of receiving FFP, the State is required to operate its programs in accordance with federally-approved State plans and other applicable Federal requirements.

OBJECTIVE, SCOPE AND METHODOLOGY

We performed our audit in accordance with generally accepted government auditing standards. Our objective was to determine if staff training contract costs claimed by DSHS for Federal reimbursement were allowable under Federal regulations and policies. The audit focused on training of DSHS personnel and did not include contracts for non-DSHS personnel such as client training contracts. Specifically, we wanted to determine if DSHS:

- ▶ claimed third-party contributions as the State's required matching share of training contract costs only as allowed by Federal regulations,
- ▶ adequately documented and supported the matching share of training contract costs claimed for Federal reimbursement, and
- ▶ appropriately allocated training contract costs between federally participating and nonparticipating programs.

During the survey phase of the audit we identified 402 training contracts with performance periods occurring during the audit period, July 1, 1993 through June 30, 1995. We judgmentally selected 136 contracts from the 402 training contracts to obtain a representative number from each DSHS program component. For each selected contract, we reviewed the purpose and nature of the contract, the funding source, and how the training costs were allocated. We did not review the allowability of specific costs during the survey.

Of the 136 contracts selected, 89 were for DSHS staff training and received funding from Department of Health and Human Services (HHS) programs. With few exceptions, the 89 contracts were for relatively small dollar amounts and short term training sessions. Our survey disclosed relatively few long term contracts. The staff training contracts with the largest dollar value were with Western Washington University (WWU), and some covered multiple years.

Our survey of the contracts at WWU indicated problems involving third-party contributions claimed as matching costs and allocations between federally participating and nonparticipating programs. Our survey did not identify similar problems with the other contracts. Accordingly, the two WWU contracts were selected for additional audit procedures. Because of problems identified with the WWU contracts, we expanded our audit coverage to four additional WWU training contracts from earlier periods. Two of the four additional contracts had performance periods during State Fiscal Years (FY) 1990 through 1991 and the other two contracts had performance periods during State FYs 1992 through 1993.

Our evaluation of internal controls was limited to the specific objectives of the audit relating to DSHS's reporting of expenditures for staff training contracts. To the extent possible we relied on the work of others. This included the work of the Washington State Auditor's Office (SAO) and the Administration for Children and Families (ACF). We held discussions

with SAO staff and reviewed relevant SAO reports. We also reviewed ACF documents and held discussions with ACF staff.

We excluded from our review two contract training issues currently being resolved between ACF and DSHS. The areas concerned unallowable travel costs and misapplied indirect cost rates.

The audit work was performed at the offices of (i) DSHS in Olympia and Lacey, Washington, (ii) WWU in Bellingham, Washington, and (iii) ACF in Seattle, Washington during the period February 1996 through March 1997.

FINDINGS AND RECOMMENDATIONS

The DSHS claimed Federal reimbursement of \$5.6 million for unallowable costs relating to six staff training contracts with WWU during the period July 1, 1989 through June 30, 1995. We found that DSHS (i) used unallowable third-party contributions to meet the matching requirements under certain Federal programs, (ii) claimed costs for WWU employees in excess of actual costs incurred, (iii) claimed unallowable costs for facilities, equipment, and other miscellaneous items, and (iv) did not always properly allocate costs between federally participating and nonparticipating programs.

THIRD-PARTY CONTRIBUTIONS

The DSHS claimed unallowable third-party contributions totaling \$4,394,051 to meet its matching requirements under six training contracts with WWU. This consisted of \$4,208,922 for independent contractors and \$185,129 of miscellaneous vendor costs. The third-party contributions were claimed by DSHS for Federal reimbursement under the AFDC, Food Stamp, Medicaid, JOBS, and Refugee Resettlement programs. Although Federal regulations allow third-party contributions for meeting State cost sharing requirements in certain instances, DSHS claimed the costs when conditions stipulated by the regulations were not present.

Background Information

Provisions of Federal Regulations. Federal regulations allow third-party contributions for use in meeting State cost sharing requirements only if they meet certain specific conditions. The conditions vary depending upon the Federal program. The specific criteria for the programs included in our audit are summarized in APPENDIX B.

Billing and Cost Allocation Procedures. The WWU billed DSHS for the training provided under the contracts. The billings included both actual training expenditures which were claimed for reimbursement from DSHS, and contributions for use by DSHS as matching costs in meeting its cost sharing requirements for the programs. Examples of the contributions claimed are:

- ▶ A portion of university overhead allocated to training based on predetermined rates negotiated with the HHS Division of Cost Allocation.
- ▶ Amounts representing the difference between the actual cost of providing training, and estimates of the market value of the training. This includes training provided by WWU personnel, as well as outside contractors and vendors.

- The estimated value of facilities and other assets used in providing training, such as classroom space and equipment.

The above are examples of contributions claimed, and do not represent an all-inclusive list of all contributions.

The amounts billed, including the contributions, were then distributed to the various federally participating and nonparticipating programs that benefitted from the training. The distribution to the AFDC, Food Stamp, Medicaid, JOBS, Refugee Resettlement and State-only (nonparticipating) programs was based on cost allocation procedures using random moment time studies.

After the costs were distributed to the programs, the costs related to the Federal programs were then claimed for Federal reimbursement at the applicable FFP rate for each program. Except for the Refugee Resettlement program, the costs reported as contributions were claimed by DSHS as matching costs to meet Federal cost sharing requirements. The Refugee Resettlement program is a 100 percent federally funded program, and the contributions were claimed for full reimbursement.

Independent Contractors and Miscellaneous Vendors

The unallowable third-party contributions identified in our audit related to training provided by instructors engaged by WWU as independent contractors, and to services provided by miscellaneous vendors such as those providing consultant services in support of the training.

Independent Contractors. The DSHS claimed Federal reimbursement of \$4,208,922 for amounts identified as third-party contributions that related to training services provided by independent contractors engaged by WWU. In addition, the DSHS procedures for claiming third-party contributions for Federal matching purposes continued after our audit period ended June 30, 1995.

The following paragraphs describe the procedures followed for obtaining training services from independent contractors, and determining the value of the training services. We also describe market value studies used in the valuation of the training services.

Billing for Third-Party Contributions. The WWU contracted with independent contractors and paid them at a predetermined daily rate. However, WWU established a value for the training that was higher than the amount paid to the contractors, based on an analysis which WWU defined as a market value study. The difference between the amounts paid to the contractors, and the amounts established as the value of the training, was considered by WWU to be a contribution. The WWU billings to DSHS for training requested reimbursement only for the amounts paid to the contractors, but they also included the amounts calculated as contributions for use by DSHS in meeting its matching requirements for the various programs benefitting from the training.

The DSHS allocated the amounts billed by WWU, including the contribution amounts, to all benefitting programs. The DSHS then claimed Federal reimbursement at the FFP rate applicable to each program.

For example, during State FY 1995, WWU paid independent contractors \$425 per day for training services. However, WWU established a value for the training provided during that year at \$850 per day. According to WWU, the value was established based on a market value study performed by WWU. The difference of \$425 per day was considered to be a contribution for use by DSHS as matching costs to meet Federal cost sharing requirements.

According to Federal AFDC and JOBS regulations applicable during the audit period, these independent contractor contributions would not be allowable because there was no transfer of private funds contributed to the State or local agency. Similar Medicaid regulations were applicable through November 1992 which made the independent contractor contributions unallowable because there was no transfer of private funds contributed to the State or local agency. However, even after November 1992 Federal regulations relating to cost allocation plans stipulated that only actual costs could be claimed for services provided by one State agency to another.

With regard to the Food Stamp program, Federal regulations described in APPENDIX B specifically define the types of costs which may be used to meet Federal matching requirements. Independent contractor contributions to the State agency are not allowable for matching purposes under the Food Stamp regulations.

Under the Refugee Resettlement program, allowable costs are reimbursed at a rate of 100 percent and no matching costs are required. Procedures followed by the State allocated the contributed costs for matching purposes to all programs. The allocation of these contributed costs to the Refugee Resettlement program resulted in claims by DSHS in excess of the costs incurred by DSHS.

Market Value Studies. In addition to the provisions in Federal regulations which do not allow DSHS claims for third-party contributions, the market value studies referred to by WWU and used to support the value of trainers when calculating contributions to DSHS were inadequately documented. Further, the methodology used to gather the data was flawed.

Documentation provided by WWU for one study performed in 1991 indicated that the purpose of the market value study was to determine market rates that would prevail in private practices or businesses. To conduct the study, WWU sent questionnaires addressed to contract trainers which asked them to indicate how much they would typically charge for one day of private practice services. We were told that the results of the study indicated that most contract trainers charged between \$800 and \$1,000 per day, and that WWU selected as the value \$850 per day because it was toward the conservative end of the range. The WWU personnel provided us with copies of some of the questionnaires, but could not provide details on the overall methodology and the final statistics resulting from the study.

The questionnaires used for this study were flawed because they did not allow for contract trainers to indicate any amounts below a range of \$800-\$1,000 per day. The questionnaire asked trainers to indicate the market rates which were closest to what the trainers would typically charge for one day of their services and provided four ranges to select from. The smallest dollar range was \$800 - \$1,000 per day. The trainers were not given the option of listing a smaller daily rate. Although we did not interview trainers as to their typical billing rates, we did find a letter from one trainer during the time of the market study indicating that he usually received \$500 per day for training services.

In addition to the above survey, WWU representatives provided information on correspondence they had with two other governmental agencies during 1993. The correspondence covered the rates these governmental units paid for consulting and training services. While these governmental agencies indicated a range that in some instances exceeded the \$850 used by WWU, the information provided did not constitute a study supporting the courses that WWU was conducting for the employees of DSHS.

Miscellaneous Vendors. The DSHS claimed Federal reimbursement of \$185,129 for third-party contributions associated with several vendors which provided services in support of training DSHS personnel under four of six WWU training contracts reviewed. Examples of the third-party contributions included the value of services which were provided but not billed, and vendors' charges that were waived or reduced. The inclusion of these items as matching costs was inappropriate for the reasons cited under the independent contractor section above.

Recommendations

We recommend that DSHS:

1. Refund to the Federal Government \$4,394,051 inappropriately claimed for third-party contributions. (See APPENDIX A of this report for a summary of the Federal share amounts questioned by Federal program.)
2. Determine the amount of third-party contributions inappropriately claimed in subsequent periods, and make an appropriate refund.
3. Revise policies for charging costs to Federal programs to ensure that unallowable third-party contributions are not claimed.

DSHS Comments and Office of Audit Services (OAS) Response

The DSHS did not concur with the above findings and recommendations, except for their applicability to the Refugee Resettlement program. For this program, DSHS agreed to refund

\$53,818 (\$51,809 related to independent contractors and \$2,009 for miscellaneous vendors), and also to identify and refund other unallowable costs subsequent to our audit period and to make procedural improvements to preclude future unallowable claims. However, DSHS disagreed with the findings and recommendations relating to the balance of third-party contributions claimed totaling \$4,340,233 (\$4,394,051 less \$53,818).

Summaries of the DSHS comments and the OAS response to the comments are presented below.

DSHS Comments Relating to the AFDC Program. The DSHS written comments stated that the Federal criteria cited in the draft report refer to cash contributions from third parties and do not pertain to in-kind contributions; in-kind contributions were used for the claims in question.

In support of its position that the in-kind contributions were allowable, the DSHS stated that:

- ▶ Federal regulations (45 CFR 74.176)¹ provide that, where a State government awards a subgrant or cost-type contract to an institution of higher education, Office of Management and Budget (OMB) Circular A-21 (Cost Principles for Educational Institutions) will apply to costs incurred by the institution, even though OMB Circular A-87 will apply to the costs incurred by the State.

- ▶ Circular A-21 provides, in part, "The value of donated services and property may be used to meet cost sharing or matching requirements, in accordance with Circular A-110" (Uniform Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and other Nonprofit Organizations).

- ▶ Circular A-110, Attachment E states that all contributions, both cash and in-kind, shall be accepted as cost sharing and matching when stated criteria are met.

The DSHS commented that the in-kind contributions claimed as state match in the staff training contracts with WWU meet the stated criteria.

OAS Response to the DSHS Comments Relating to the AFDC Program. The criteria cited in the audit report contain the principles under which States may claim matching costs required under the AFDC program. While the above criteria cited by DSHS are applicable to costs incurred under subgrants or cost-type contracts awarded by a State government to an institution of higher education, the regulations and OMB circulars cited are not relevant to what States may claim to meet its cost sharing requirements for the AFDC program.

¹The provisions of this section of the regulations are presently contained in 45 CFR 74.27, revised in 1994).

The AFDC regulations cited in the report do not make any provisions for third-party in-kind contributions to be claimed as State matching costs. It is noted that, in some instances, other Federal regulations that are non-program specific make such an allowance in some cases. Subpart G of 45 CFR 74 (Administration of Grants²) contains rules for satisfying Federal requirements for cost-sharing or matching. It provides that, in some instances, the value of third-party in-kind contributions may be used to meet cost-sharing or matching requirements.

However, Federal regulations exempt the above provisions from applicability to the AFDC program. Under 45 CFR 201.5(e), the AFDC program is specifically excluded from the provisions of Subpart G of the above regulations.

DSHS Comments Relating to the Food Stamp Program. In the written response to the draft audit report, the DSHS referred to our citing of 7 CFR 277.4(c) as the criteria for determining allowable State agency costs for use as Federal matching funds. The DSHS commented that paragraph 277.4(d) of the same regulation states that all cash or in-kind contributions shall be allowable as part of the State agency's share of program costs when the stated criteria are met. It was contended that the in-kind contributions claimed as State match in the staff training contracts with WWU met the stated criteria.

The DSHS also maintained that its position on third-party in-kind contributions, and in particular on the Food Stamp program portion, is supported by a 1992 letter from the Department of Agriculture to the Oklahoma Department of Human Services. A copy of the letter was enclosed by the DSHS, and is included in Appendix C.

OAS Response to the DSHS Comments Relating to the Food Stamp Program. The Federal regulations for the Food Stamp program at 7 CFR 277.4(c) limit in-kind contributions of services and real or personal property for Federal funds to that donated by other nonfederal public agencies and institutions. There is no provision for donations by private parties such as the independent contractors and miscellaneous vendors as described in our audit report.

Paragraph 277.4(d), which was cited by the DSHS as supporting its claim for the in-kind contributions, does not make any reference to the allowability of such contributions by private third parties. The purpose of this section of the regulations is to list specific conditions which must be met for cash or in-kind contributions claimed as part of the State agency's share of program costs. To illustrate, such costs would need to be verifiable as well as necessary and reasonable for accomplishment of project objectives.

The 1982 letter to the Oklahoma Department of Human Services, which was included in the DSHS comments, pertains to the approval by the Department of Agriculture of a specific project funded in part by the Federal Government. The letter does not represent general

²The full title of this regulation is Uniform Administrative Requirements for Awards and Subawards to Institutions of Higher Education, Hospitals, Other Nonprofit Organizations, and Commercial Organizations; and Certain Grants and Agreements with States, Local Governments, and Indian Tribal Governments.

criteria for the allowability of in-kind matching from private parties under the Food Stamp program.

DSHS Comments Relating to the Medicaid Program. The DSHS stated that the Federal regulations cited in the report did not pertain to in-kind contributions, and commented that it was basing its position on the Medicaid program on the same CFR and OMB circulars cited above regarding the AFDC program. The DSHS maintained that those cites deal specifically with in-kind contributions, not cash funds, and are applicable to all HHS grants. The DSHS also stated that another Federal regulation - 45 CFR 92.24³ - provided that cost sharing or matching requirements could be satisfied by either cash or third-party in-kind contributions, and the regulation included Medicaid in its scope.

OAS Response to the State Comments Relating to the Medicaid Program. The position taken by DSHS regarding the AFDC program was essentially that the costs in question should be subject to Federal regulations and OMB circulars relating to institutions of higher education, and those criteria allow in-kind contributions for matching purposes. As we stated in our above comments regarding the AFDC program, the regulation and OMB circulars cited by DSHS do not relate to the State's cost sharing requirement for the AFDC program. Similarly, they also do not address this requirement for the Medicaid program.

Further, the cost sharing provisions of 45 CFR 92 cited by the DSHS which allow cash or third-party in-kind contributions for meeting cost sharing or matching requirements do not apply to the Medicaid program. (See 45 CFR 92.4.)

In addition, Federal regulations exempt the Medicaid program from the provisions of Subpart G of 45 CFR 74 (Administration of Grants) which allows, in some instances, the use of third-party in-kind contributions to meet State matching requirements. This exemption is contained in 42 CFR 430.30(e) in the Federal regulations for the Medicaid program.

In summary, the Federal regulations cited in our audit report in Appendix B describe when funds donated from private sources may be considered as the State's share in claiming FFP for the Medicaid program, and the regulations do not provide for third-party in-kind contributions in meeting this requirement.

DSHS Comments Relating to the JOBS Program. In its written comments, the DSHS referred to 45 CFR 250.73 which we cited as Federal provisions for the allowability of donated funds from private sources to meet matching requirements. The DSHS stated that another paragraph of this same section of the regulation provides that in-kind contributions are acceptable as match for the 90 percent FFP granted to the State (various FFP percentages are allowed under the JOBS program).

³45 CFR 92 is titled, "Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments."

The DSHS also stated that it is basing its position that the third-party in-kind contributions represent allowable costs for Federal matching purposes on the same criteria discussed above under the AFDC program, which was similarly used in the comments on the Medicaid program. Additionally, the DSHS stated that the use of third-party in-kind contributions was supported by 45 CFR 92.24, as described above in the comments relating to the Medicaid program.

OAS Response to the State Comments Relating to the JOBS Program. Although regulations provide that in-kind contributions may be used to meet the State's matching requirements for certain costs reimbursable at the 90 percent FFP rate, those regulations do not make any provisions for such contributions from private sources. The only provisions for meeting matching requirements from private sources relate to situations involving unrestricted transfers of funds as described in 45 CFR 250.73 and summarized in Appendix B to this report.

As we stated previously in our comments regarding the Medicaid program, the regulations and OMB circulars cited by DSHS do not relate to the State's cost sharing requirement for the AFDC program. Similarly, they also do not address this requirement for the JOBS program.

Further, the cost sharing provisions of 45 CFR 92 cited by the DSHS which allow cash or third-party in-kind contributions for meeting cost sharing or matching requirements do not uniformly apply to all programs. The various provisions of this regulation, including those involving in-kind contributions, do not apply where they are inconsistent with Federal statutes or other applicable Federal regulations.

DSHS Comments Relating to Market Value Studies. The DSHS disagreed with the comments in our report regarding the market value studies that were used to support the value of trainers in the calculation of the amount of in-kind contributions. The DSHS indicated that the studies which included information obtained from two government agencies were valid and provided sufficient information to determine a fair market value of the training. In addition, the DSHS indicated that the rates had been reviewed and agreed to by the State's Department of Personnel.

OAS Response to the DSHS Comments Relating to Market Value Studies. As stated in our report, WWU was not able to provide us with details on the overall market value study methodology, nor the final statistics resulting from the study. Further, the questionnaires that were filled out by the trainers did not provide an option for entering estimated market values of training at any amount lower than \$800 per day. In addition, the WWU had retained only a limited number of the completed questionnaires, and did not have documentation providing an overall summary of the results of the questionnaires.

WWU EMPLOYEE COSTS

The DSHS overclaimed Federal reimbursement totaling \$1,002,109 for WWU employees who provided training services relating to three of six training contracts included in our audit. The costs claimed for Federal reimbursement exceeded the actual costs incurred. This occurred because DSHS claimed Federal reimbursement based on WWU's determination of the market value of the services rather than actual costs incurred.

Federal regulation 45 CFR 95.507, concerning cost allocation requirements, provides in subsection (b)(6) that costs claimed by the State agency for services provided by a governmental agency outside the State agency will be based on the actual costs incurred.

The WWU training center⁴ entered into agreements with several university departments to furnish faculty members and other employees to provide training services required by the contracts with DSHS. According to the agreements, the services were being purchased by the training center at the established market value rather than the actual costs. The market value was established based upon the procedures described above for independent contractors. However, the WWU training center reimbursed the WWU departments based on the actual costs of employees providing the services. The remaining amount, representing the difference between the actual costs and the market value, was considered a contribution for use by DSHS as matching costs to meet cost sharing requirements of Federal programs.

The asserted value of the training services, actual costs plus contributions, was then billed to DSHS and used by DSHS to claim reimbursement for Federal programs (i.e., the AFDC, Food Stamp, Medicaid, JOBS, and Refugee Resettlement programs.) The DSHS reimbursed WWU only for its actual costs (i.e., the total billed less the matching amounts).

Effective with the contracts starting July 1993, the WWU training center no longer entered into agreements with other WWU departments for providing training services. Starting July 1993, services obtained by the WWU training center from WWU faculty and other employees were obtained through independent contractor arrangements such as those described in the previous finding.

Recommendation

We recommend that DSHS refund to the Federal Government \$1,002,109 inappropriately claimed for WWU employee costs. (See APPENDIX A of this report for a summary of the Federal share amounts questioned by Federal program.)

⁴The WWU training center is called the Center for Public Service Development and Training.

DSHS Comments

The DSHS officials concurred with our recommendation to refund to the Federal Government \$1,002,109 inappropriately claimed for WWU employee costs. They stated that the funds would be returned to the Federal agencies by reduction of future claims.

FACILITIES, EQUIPMENT, AND OTHER MISCELLANEOUS COSTS

The DSHS inappropriately claimed Federal reimbursement of \$189,983 for miscellaneous contributed costs reported in WWU billings which consisted of \$127,897 for classroom space and equipment, \$49,090 for administrative costs, and \$12,996 in duplicate billings under four of six training contracts reviewed. The inappropriate charges for the space, equipment and administrative costs for the four contracts occurred during the period July 1989 through June 1993. The WWU did not include these types of contributed costs on billings for the remaining two contracts, which were for the period July 1993 through June 1995.

Classroom Space and Equipment Costs. The DSHS claimed \$127,897 of unallowable Federal reimbursement relating to classroom space and equipment utilized by WWU in providing training. Examples of such space include:

- ▶ space provided in State-owned buildings, such as conference rooms in the DSHS community service offices where the staff being trained were located, and
- ▶ space provided by third parties, such as hotel conference rooms.

The equipment included items such as overhead projectors, video equipment, and extension cords. The equipment was furnished by the contributors of the classroom space, which included DSHS as well as third parties.

We reviewed DSHS records for the space and equipment provided by DSHS, and found that such building space and equipment costs had already been charged to Federal programs through the DSHS Departmentwide Cost Allocation Plan. Therefore, such contribution amounts represented a duplication of amounts already claimed for Federal reimbursement. These costs would not be allowable as charges to Federal programs under section C.1.f. of OMB Circular A-87 Attachment A, which states that to be allowable under a grant program, costs must not be allocable to or included as a cost of any other federally financed program in either the current or prior period.

For the space and equipment provided by the third parties, the costs would not be allowable as charges to the Federal programs based on criteria described in the above finding on third-party contributions.

The documentation provided by WWU in support of the amounts reported as contributions for space and equipment consisted of listings of the buildings in which the training was provided, and the equipment which was provided for the training sessions at those locations. However, the listings were not in sufficient detail to show, in all instances, whether the space was owned by DSHS or provided by third parties. Thus, the records at WWU were not sufficiently detailed to break out the costs between duplicated costs and third-party contributions.

Administrative Costs. The DSHS inappropriately claimed Federal reimbursement of \$49,090 for the salaries and fringe benefits of several WWU administrative staff performing services related to the DSHS training contracts. The services included activities such as contract accounting and billing.

The WWU had an indirect cost agreement with the HHS Division of Cost Allocation during the period of the training contracts. We found that the administrative staff salaries and fringe benefits were already being claimed by WWU under the HHS Division of Cost Allocation indirect cost agreement. The WWU used the indirect cost rate in billings submitted to DSHS for costs incurred under the training contract. Therefore, the salaries and benefits represented a duplication of amounts already charged.

Duplicate Billings. The DSHS claimed Federal reimbursement for duplicate billings of \$12,996. The \$12,996 overclaim resulted from WWU incorrectly including the same contributed costs twice in its billings for one of the six training contracts reviewed.

Recommendation

We recommend that DSHS refund to the Federal Government \$189,983 for the overclaim related to space and equipment costs, administrative costs, and the duplicate billings. (See APPENDIX A of this report for a summary of the Federal share amounts questioned by Federal program.)

DSHS Comments

The DSHS officials concurred with our recommendation to refund to the Federal Government \$189,983 for the overclaim related to space and equipment, administrative costs, and the duplicate billings. They stated that the funds would be returned to the Federal agencies by reduction of future claims.

ALLOCATION OF TRAINING COSTS

Our audit disclosed that training costs relating to an amendment to one of six training contracts reviewed were allocated only to the Medicaid program when in fact other federally

participating and nonparticipating programs benefitted from the training. Federal regulations require that costs be allocated to each program in terms of the benefits received by the programs. As a result, DSHS overclaimed Federal reimbursement of \$41,248. (See APPENDIX A for the reallocations needed to the AFDC, Food Stamp, Medicaid, JOBS, and Refugee Resettlement programs.)

Section C.2.a of OMB Circular A-87, Attachment A, states that a cost is allocable to a particular cost objective to the extent of benefits received by such objective. Further, section J.1 of the circular requires that a plan for allocation of costs will be required to support the distribution of any joint costs related to the grant program. The circular also provides that all costs included in the plan will be supported by formal accounting records which will substantiate the propriety of eventual charges.

One of the six training contracts reviewed included an amendment to train DSHS staff in the encouragement of client self-sufficiency. Although the contract amendment benefitted several programs, DSHS allocated all of the costs to the Medicaid program. The DSHS had a cost allocation procedure for distributing training costs among benefitting programs, but in this instance that procedure was not followed. The DSHS needs to ensure that its cost allocation procedures are consistently applied for training that relates to more than one program.

Recommendations

We recommend that DSHS:

1. Refund to the Federal Government \$41,248 that resulted from not allocating costs to the programs that benefitted from the training.
2. Ensure that DSHS cost allocation procedures are consistently applied.

DSHS Comments

The DSHS officials concurred with our recommendation to refund to the Federal Government \$41,248 that resulted from not allocating costs to the programs that benefitted from the training. They stated that a refund has already been made. However, they attributed the overclaim to an error in judgment rather than a problem in following established allocation procedures.

OAS Response

The circumstances involving the charging of training costs entirely to the Medicaid program when such training benefitted several programs indicated an inconsistency in following cost allocation procedures established by DSHS.

APPENDICES

APPENDIX A

STATE OF WASHINGTON
DEPARTMENT OF SOCIAL AND HEALTH SERVICES

SCHEDULE OF THE FEDERAL SHARE OF QUESTIONED
TRAINING CONTRACT COSTS BY FEDERAL PROGRAM
FOR THE PERIOD
JULY 1, 1989 THROUGH JUNE 30, 1995

Cost Category	AFDC Program	Food Stamp Program	Medicaid Program	JOBS Program	Refugee Program	Totals
Independent Contractors	\$1,513,313	\$1,489,022	\$1,055,538	\$ 99,240	\$51,809	\$4,208,922
Miscellaneous Vendors	69,892	70,888	42,202	138	2,009	185,129
WWU Employee Costs	324,758	269,729	287,410	99,707	20,505	1,002,109
Space & Equipment	43,858	39,245	35,388	6,928	2,478	127,897
Administrative Costs	16,482	14,222	13,821	3,576	989	49,090
Duplicate Billings	3,709	77	6,171	2,158	881	12,996
Allocation of Training Costs	<u>-90,933</u>	<u>-96,135</u>	<u>242,214</u>	<u>-11,700</u>	<u>-2,198</u>	<u>41,248</u>
Totals	<u>\$1,881,079</u>	<u>\$1,787,048</u>	<u>\$1,682,744</u>	<u>\$200,047</u>	<u>\$76,473</u>	<u>\$5,627,391</u>

Note: Numbers shown in bold with a minus sign represent upward adjustments.

FEDERAL REGULATIONS FOR THIRD-PARTY CONTRIBUTIONS

AFDC Program. Under 45 CFR section 235.66(b) - Private funds, funds donated from private sources may be considered as the State's share in claiming Federal reimbursement only if they meet certain specific conditions. These conditions are that the funds:

- ▶ are transferred to the State or local agency and are under its administrative control;
- ▶ are donated without any restriction which would require their use for the training of a particular individual or at particular facilities or institutions; and
- ▶ do not revert to the donor's facility or use.

Food Stamp Program. Under 7 CFR section 277.4(c) - Matching costs, State agency costs for Federal matching funds may consist of:

- ▶ charges reported on a cash or accrual basis by the State agency as project costs;
- ▶ project costs financed with cash contributed or donated to the State agency by other non-Federal public agencies and institutions; and
- ▶ project costs represented by services and real or personal property donated by other non-Federal public agencies and institutions.

Medicaid Program. Under 42 CFR section 433.45(b) - Private funds as State's share, funds donated from private sources may be considered as the State's share in claiming FFP only if they meet the following conditions:

- ▶ the private funds are transferred to the State or local Medicaid agency and are under its administrative control, and
- ▶ the private funds do not revert to the donor's facility or use unless the donor is a nonprofit organization, and the Medicaid agency, of its own volition, decides to use the donor's facility.

FEDERAL REGULATIONS FOR THIRD-PARTY CONTRIBUTIONS
(Continued)

Effective after November 1992, the Medicaid regulations were revised, and the new regulations no longer contained the criteria previously stipulated in 42 CFR section 433.45(b). However, Federal regulation 45 CFR 95.507, concerning cost allocation requirements, provides in subsection (b)(6) that costs claimed for services provided by a governmental agency (such as WWU) outside the State agency (such as DSHS) will be based on the actual costs incurred.

Also, the State Medicaid Manual Section 2500.7 states that the State agency should report only expenditures for which supporting documentation, in readily reviewable form, has been compiled and is immediately available.

JOBS Program. Under the provisions of 45 CFR section 250.73 - Matching rates, funds donated from private sources may be considered as the State's share in claiming FFP when the funds are:

- ▶ transferred to the State or local agency and under its administrative control;
- ▶ donated without any restriction which would require their use for assisting a particular individual or at particular facilities or institutions; and
- ▶ do not revert to the donor's facility or use.

Refugee Resettlement Program. Under 45 CFR 400.202 - Extent of Federal funding, the Refugee Resettlement program provides reimbursement of 100 percent of allowable costs of determining eligibility and providing assistance and other services. This program does not require State matching funds.



STATE OF WASHINGTON
DEPARTMENT OF SOCIAL AND HEALTH SERVICES
Olympia WA 98504-5000
July 9, 1997

Lawrence Frelot, Regional Inspector General
Department of Health & Human Services
Region IX, OIG
Office of Audit Services
50 United Nations Plaza, Room 171
San Francisco, California 94102

Re: TRAINING CONTRACT AUDIT (CIN) A-10-96-00004

Dear Mr. Frelot:

Thank you for your letter dated June 13, 1997, providing the opportunity to review your draft report on the audit of our training contract costs. Below is our response and comments to that draft. We are responding in the order of the recommendations presented in the draft.

THIRD-PARTY CONTRIBUTIONS

We concur with the findings and recommendations that pertain to the \$53,818 in Refugee Program questioned costs. The inclusion of the portion of the claim attributable to the Refugee Program in the same methodology used in other programs was an oversight on our part. These funds will be returned to the federal agency and revised claims will be submitted.

We do not concur with the findings and recommendations that pertain to the remaining federal grants. This is an issue we have been trying to resolve with Department of Health and Human Services (DHHS) for the past five years. We have not received a response since submitting our position in writing in December 1994. It is our understanding that DHHS Region X submitted the issue to the ACF headquarters office in Washington, D.C.

Our basis for nonconcurrency remains as previously stated in our earlier discussions and correspondence with DHHS. The following paragraphs will address your CFR citations with our position in the order that they are presented in Appendix B of your letter.

AFDC Program

Your letter cited 45CFR, Section 235.66(b) which refers to cash contributions from a third-party and does not pertain to in-kind contributions. The State has used only in-kind contributions for the claims in question.



Lawrence Frelot, Regional Inspector General
July 9, 1997
Page 2

In-kind contributions are covered in 45CFR Section 74.176 which states:

The cost principles applicable to a subgrantee or cost-type contractor under a HHS grant will not necessarily be the same as those applicable to the grantee. For example, where a State government awards a subgrant or cost-type contract to an institution of higher education, OMB Circular No. A-21 will apply to the costs incurred by the institution of higher education even though OMB Circular No. A-87 will apply to the costs incurred by the State.

Circular A-21, section J states, in part, "The value of donated services and property may be used to meet cost sharing or matching requirements, in accordance with Circular A-110."

Circular A-110, attachment E, section 3(b) states that all contributions, both cash and in-kind, shall be accepted as cost sharing and matching when stated criteria are met. The in-kind contributions claimed as state match in the staff training contracts with WWU meet the stated criteria.

Food Stamp Program

You have cited 7CFR, Section 277.4(c), which refers to matching costs. Paragraph (d) of this same cite states that all cash or in-kind contributions shall be allowable as part of the State agency's share of program costs when the stated criteria are met. The in-kind contributions claimed as state match in the staff training contracts with WWU meet the stated criteria.

Our position on this issue as a whole, and in particular on the Food Stamp Program portion, is supported by a 1992 letter from the Department of Agriculture, Southwest Region, to the Director of Oklahoma Department of Human Services. A copy of this letter is enclosed.

Medicaid Program

You have cited 42CFR, Section 433.45 (b) and 45CFR, Section 95.507, (b)(6). The first of these two cites refers to the donation of funds and is noted in your letter as being revised in 1992. The latter of the two cites addresses agency cost allocation plans and procedures. Neither of these two cites pertain to in-kind contributions.

As in the case with the AFDC program noted previously, we are basing our position on the CFR and OMB circulars cited. Those cites we referenced deal specifically with in-kind contributions, not cash funds, and are applicable to all DHHS grants.

Additionally, 45CFR, Section 92.24, which is applicable to all DHHS grants, states that cost sharing or matching requirements may be satisfied by either cash or third-party in-kind contributions. This section specifically includes Medicaid grants in its scope.

Lawrence Frelot, Regional Inspector General
July 9, 1997
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JOBS Program

Your letter cited 45CFR, Section 250.73, but referenced only those portions of the cite related to donated funds. The first paragraph of this section states that in-kind donations are acceptable as match for the 90 percent FFP granted to the state.

We are basing our position in this issue on the CFR and OMB circulars cited in our previous discussion of the AFDC program. Those cites we referenced deal specifically with in-kind contributions, not cash funds, and are applicable to all DHHS grants. Additionally, 45CFR, Section 92.24, which is applicable to all DHHS grants, states that cost sharing or matching requirements may be satisfied by either cash or third-party in-kind contributions.

Other Issues

The draft contained some discussion of the market value studies that were conducted to establish a market value of the contracted trainers services. It is unclear to us why this item is discussed since the recommendations assert that the claim for donated services based on market value is improper. Although it appears inappropriate to discuss this in the narrative findings, we do have comments on the content of this discussion. We do not agree with the comment that the methodology used in the studies was "flawed." There are no prescribed methods for surveys for these purposes and the survey or study was not used independently in determination of fair market value. As was pointed out in your draft, information was also obtained from two governmental agencies. This information alone would have been adequate to determine a fair market value. Considering that the low end of the average range was selected, there appears to be some conservatism in that selection. When a similar question arose on this issue earlier, an inquiry was made to our State's Department of Personnel to obtain the rates they pay trainers. Their rates confirmed the WWU's market value assessment.

WWU EMPLOYEE COSTS

We concur with the recommendation contained in your draft. The erroneous claiming of employee costs at market value rather than at cost was discovered during a prior review. These type of claims were discontinued after discovery. These funds will be returned to the federal agencies by reduction of future claims.

FACILITIES, EQUIPMENT, AND OTHER MISCELLANEOUS COSTS

We concur with the recommendation contained in your draft. The incorrect claiming of these costs was terminated in 1993. These funds will be returned to the federal agencies by reduction of future claims.

Lawrence Frelot, Regional Inspector General
July 9, 1997
Page 4

ALLOCATION OF TRAINING COSTS

In this item, while we concur that costs for federal reimbursement were over claimed, we believe that there is some inaccuracy and omission in the discussion of the circumstances and the resulting recommendations.

The first recommendation is the refund of \$41,248 to the Federal Government. This has already occurred and should be noted as such in both the narrative and the recommendation.

The third paragraph under this heading refers to cost allocation "procedure" and states that "procedure was not followed." The determination of how to allocate costs is not procedure driven and it was actually an error in judgment in determining benefiting programs that caused the error. The narrative should not have references to procedures. It would appear that the recommendation is inappropriate.

I hope that these comments are useful to you and your staff in completing the audit report. If further clarification is needed, or if additional questions arise, please contact Phyllis Hum at (360) 902-8200. Thank you again for this opportunity for review.

Sincerely,


LYLE QUASIM
Secretary

Enclosure

cc: Ronald P. Benoy
Department of Health and Human Services
OIG Office of Audit Services
2201 Sixth Avenue, M/S RX-80
Seattle, WA 98121-2500

Jerry Friedman, Assistant Secretary, ESA
Phyllis Hum, Director, Finance Division

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FNS CABINET OFFICE



United States
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Southwest
Region

1100 Commerce Street
Dallas, TX 75242-1005

DEC 22 1992

Mr. Benjamin Damps, Jr., Director
Oklahoma Department of Human Services
P. O. Box 25352
Oklahoma City, Oklahoma 73125-5352

Dear Mr. Damps:

Your November 5, 1992, letter requested our approval of your plans to develop a Satellite Training Network (SATTRN) for the Oklahoma Department of Human Services.

Your plans for SATTRN are very impressive. You and your staff should be commended for your foresight in developing a system that will provide training in a professional and consistent manner statewide. Based on our understanding of the way the system will work, SATTRN should also assist in reducing your Food Stamp Program error rate.

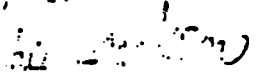
There are some cautions that you must keep in mind concerning the use of Federal funding.

1. The project services should be obtained under competitive bid conditions (OMB Circular A-102, paragraph 36).
2. If the total cost of the project (FNS/State/Private) exceeds \$500,000, you must submit an Advance Planning Document (APD). If a sole source procurement is contemplated, FNS Handbook 901, page 11-1, requires an APD if the total cost exceeds \$100,000.
3. The matching requirements may be met through the use of non-Federal grants or by cash donations from non-Federal third parties in place of the State's share. However, the requirements cannot be met with funds from another Federal grant (OMB Circular A-102, paragraph 24).
4. The matching requirements may also be met by private funding in the form of donated goods and services (in-kind contributions), provided that the same goods and services were not used to satisfy another matching requirement as well.
5. Any system developed using Food Stamp Program funds must be used for Food Stamp Program training commensurate with the funding; i.e., if Food Stamp Program funds are used to pay for 25 percent of the network's costs, it must be used for Food Stamp Program training at least 25 percent of time.

Mr. Benjamin Damps, Jr.
Page 2

We look forward to seeing this system in operation. If we
can be of further assistance, please let us know.

Sincerely,


RUTHIE JACKSON
Regional Administrator

cc: Carolyn Bryan ✓