



OFFICE OF INSPECTOR GENERAL

*Catalyst for Improving the Environment*

## **Quick Reaction Report**

# **Ineligible Federal Funds Drawn on EPA Grant No. XP98284701 Awarded to the City of Middletown, New York**

**Report No. 2007-2-00039**

**September 25, 2007**

**Report Contributors:**

Robert Adachi  
Richard Howard  
Janet Kasper

**Abbreviations**

EPA	U.S. Environmental Protection Agency
Grantee	City of Middletown, New York
OIG	Office of Inspector General
OMB	Office of Management and Budget
Grant	Grant No. XP98284701



# At a Glance

*Catalyst for Improving the Environment*

## Why We Did This Review

The U.S. Environmental Protection Agency (EPA) Office of Inspector General (OIG) conducted a review of earmarked grants known as Special Appropriation Act Projects issued to local and tribal Governments. The City of Middletown, New York, was selected for review.

## Background

The City of Middletown received an EPA Special Appropriation Act Project grant, XP98284701. The purpose of the grant was to provide Federal assistance of \$433,700 for the procurement of equipment for the grantee's drinking water treatment plant. The City of Middletown was required to provide local matching funds equal to 49 percent of the EPA-awarded funds.

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

To view the full report, click on the following link:  
[www.epa.gov/oig/reports/2007/20070925-2007-2-00039.pdf](http://www.epa.gov/oig/reports/2007/20070925-2007-2-00039.pdf)

## ***Ineligible Federal Funds Drawn on EPA Grant No. XP98284701 Awarded to the City of Middletown, New York***

### **What We Found**

The City of Middletown (grantee) claimed costs that were incurred prior to the timeframes provided for in Office of Management and Budget Circular A-87 and the Special Appropriation Act Projects guidance. These guidelines indicate that costs are eligible as of the beginning of the fiscal year when funds are appropriated. The grant funds were appropriated in Fiscal Year 2003; therefore, preaward costs incurred after October 1, 2002, were eligible for reimbursement. However, the grantee incurred the entire \$853,002 in total project costs prior to October 1, 2002. Also, the grant conditions only approved preaward costs 90 days prior to the grant award. The costs claimed by the grantee were incurred approximately 15 months prior to the grant award date. As a result, all costs claimed under the EPA grant are ineligible for Federal reimbursement and grants funds of \$433,700 must be repaid.

### **What We Recommend**

We recommend that the EPA Region 2 Regional Administrator require the City of Middletown to repay the \$433,700 in Federal funds drawn.



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

OFFICE OF  
INSPECTOR GENERAL

September 25, 2007

**MEMORANDUM**

**SUBJECT:** Ineligible Federal Funds Drawn on EPA Grant No. XP98284701  
Awarded to the City of Middletown, New York  
Report No. 2007-2-00039

**FROM:** Melissa M. Heist *Melissa M. Heist*  
Assistant Inspector General for Audit

**TO:** Alan J. Steinberg  
Regional Administrator  
EPA Region 2

This report contains a time-critical issue the Office of Inspector General (OIG) identified and recommends recovery of Federal funds drawn down by the recipient. 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 \$9,383.

**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 finding contained in this report before any formal resolution can be completed with the recipient. Your proposed decision is due in 120 days, or on January 23, 2008. To expedite the resolution process, please email an electronic version of your proposed management decision to [kasper.janet@epa.gov](mailto:kasper.janet@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 Janet Kasper, Director, Assistance Agreement Audits, at (312) 886-3059 or at the email address above.

## **Purpose**

During our review of Special Appropriation Act Projects, the following condition came to our attention that we believe requires immediate attention. The City of Middletown, New York (grantee) submitted drawdown requests to the U.S. Environmental Protection Agency (EPA) for preaward costs of \$853,002 that were ineligible for reimbursement. The costs were ineligible under Office of Management and Budget (OMB) Circular A-87, EPA's Fiscal Year 2003 Special Appropriation Act Projects guidance, and the grant terms and conditions. As a result, the entire grant amount of \$433,700 claimed by the grantee must be repaid to EPA.

## **Background**

Grant No. XP98284701 (grant) was awarded on September 30, 2003. The purpose of the grant was to provide Federal assistance of \$433,700 for the procurement of equipment for a prefabricated, complete "package" treatment plant, which was incorporated into the grantee's existing drinking water treatment plant. The \$433,700 represents EPA's contribution of up to 50.84 percent of the eligible project costs, and is limited by the amount of the congressional appropriation. The grantee was responsible for matching, at a minimum, 49.16 percent of the eligible project costs. Total project costs under the grant were \$853,002, which represent the equipment purchased for the treatment plant. The budget and project period for the grant was August 1, 2003, to August 1, 2004. Administrative Condition No. 11 of the grant authorized the grantee to charge preaward costs incurred up to 90 days prior to award date, provided that the costs were included in the approved grant application.

## **Scope and Methodology**

We performed our audit in accordance with generally accepted government auditing standards, issued by the Comptroller General of the United States, with the exception of gaining a complete understanding of internal controls as required under Section 7.11 and information control systems as required under Section 7.59. We did not obtain a complete understanding of the internal control system since the limited nature of our review focused on the source documents that support costs claimed under the grant. We also did not test the recipient's grant drawdown process or the recipient's process for entering information into its accounting system. We did not obtain an understanding of information control systems since the review of general and application controls was not relevant to the assignment objectives. We did not make site visits to the grantee; instead, the results were based on information in the EPA project files and interviews with EPA and grantee personnel. We conducted our field work between July 19, 2007, and August 13, 2007.

## **Finding**

The grantee did not incur its preaward grant costs during the period required by OMB Circular A-87 and the Special Appropriation Act Projects guidance. These guidelines indicate that costs are eligible as of the beginning of the fiscal year when funds are appropriated. The grant funds were appropriated in Fiscal Year 2003, so preaward costs incurred after October 1, 2002, could be eligible for reimbursement. However, the grantee incurred the entire \$853,002 in total project

costs prior to October 1, 2002. Also, the grant conditions only approved preaward costs 90 days prior to the grant award. The costs claimed by the grantee were incurred approximately 15 months prior to the grant award date. Therefore, all costs claimed under the EPA grant are ineligible for Federal reimbursement.

The *Award of Grants and Cooperative Agreements for the Special Projects and Programs Authorized by the Agency's FY 2003 Appropriations Act*, dated July 22, 2003, and issued by James Hanlon, Director – Office of Wastewater Management, states:

*Since 1995, EPA Headquarters (in accordance with established OMB and Agency procedures) have approved pre-award costs for more than 50 special Appropriations Act projects in the following two situations:*

*The pre-award costs were incurred after the start of the fiscal year for which the funds were appropriated but before grant award; and/or,*

*The pre-award costs were for facilities planning or design work associated with the construction portion of the project for which the grant was awarded.*

*Accordingly, effective April 1, 2000, the Regions have the authority to approve pre-award costs for the two situations described above. Any approval, of course, is contingent on the Regional Office determination that the pre-award costs in question are in conformance with the applicable Federal laws, regulations and executive orders that govern EPA grant awards and are allowable, reasonable and allocable to the project.*

The following table shows the sequence of costs incurred and claimed by the grantee under the grant for treatment plant equipment:

**Table 1: Schedule of Grantee Transactions**

<b>Date</b>	<b>Amount</b>	<b>Action</b>
June 3, 2002	\$ 75,000 778,002	According to two vendor invoices, date treatment system equipment ordered.
June 7, 2002	75,000	Purchase order issued for equipment ordered on June 3, 2002.
June 21, 2002	778,002	Purchase order issued for equipment ordered on June 3, 2002.
July 18, 2002	778,002 75,000	Both purchase orders recorded in grantee's electronic accounting system.
July 23, 2002	75,000	Invoice issued to grantee for equipment.
August 12, 2002	75,000	Check issued to vendor for equipment.
September 30, 2002	778,002	Invoice issued for equipment.
October 28, 2002	778,002	Check issued to vendor for equipment.
September 30, 2003	433,700	Special Appropriation Act Projects grant awarded to Middletown for reimbursement of equipment costs incurred in Fiscal Year 2003.
December 11, 2003	390,330	First drawdown of grant funds.
April 8, 2004	43,370	Final drawdown of 10 percent of withheld grant funds.

Source: Region 2 Middletown project file.

The City Treasurer stated that the accrual basis of accounting is used for financial reporting purposes. As defined by the Government Accounting Standards Board Section 1600.102, under the accrual basis of accounting, most transactions are recognized when they occur, regardless of when cash is received or disbursed. The grantee officials stated that they would have recognized the equipment orders as accounts payable as of the order date of June 3, 2002. In order for these costs to be eligible under the Fiscal Year 2003 appropriation, the costs had to be incurred after October 1, 2002. However, the entire amount was incurred prior to this date. The grantee ordered its equipment on June 3, 2002. It recorded the purchase orders for the equipment in its accounting system on July 18, 2002. Grantee officials informed us that they could not explain why there was a delay between the order date and the date the costs were recorded.

Administrative Condition 11 of the grant authorized the grantee to charge preaward costs incurred up to 90 days prior to award date, provided that the costs were included in the approved grant application. The grant was awarded on September 30, 2003. In order for preaward costs to be eligible for reimbursement, they had to be incurred between June 30, 2003, and September 30, 2003. Therefore, based on the criteria cited, the grantee claimed preaward costs of \$853,002 that were contrary to OMB Circular A-87, EPA guidance, and the terms and conditions of its grant award. As a result, the grantee must repay the entire grant amount of \$433,700 to EPA.

## **Recommendation**

1. We recommend that the Regional Administrator, EPA Region 2, require the City of Middletown, New York, to repay the \$433,700 in Federal funds drawn.

## **Auditee's Comments**

We held an exit conference with grantee representatives on September 5, 2007. The grantee representatives stated that they did not dispute the factual accuracy of the report, and would work with their congressional representatives and Region 2 officials to resolve the costs questioned.

## **OIG Response**

Our position remains unchanged since the grantee did not dispute the facts presented in this report.

## **Status of Recommendations and Potential Monetary Benefits**

RECOMMENDATIONS						POTENTIAL MONETARY BENEFITS (in \$000s)	
Rec. No.	Page No.	Subject	Status <sup>1</sup>	Action Official	Planned Completion Date	Claimed Amount	Agreed To Amount
1	3	Require the City of Middletown, New York, to repay the \$433,700 in Federal funds drawn.		Regional Administrator, EPA Region 2		\$434	

<sup>1</sup> 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.

## ***Distribution***

Regional Administrator, Region 2  
Director, Office of Wastewater Management, Office of Water  
Director, Office of Wastewater Management - Municipal Services Division, Office of Water  
Director, Office of Grants and Debarment  
Director, Grants and Interagency Agreements Management Division  
Agency Followup Official (the CFO)  
Agency Followup Coordinator  
Associate Administrator for Congressional and Intergovernmental Relations  
Associate Administrator for Public Affairs  
Region 2 Audit Followup Coordinator  
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Acting Inspector General