



U.S. ENVIRONMENTAL PROTECTION AGENCY

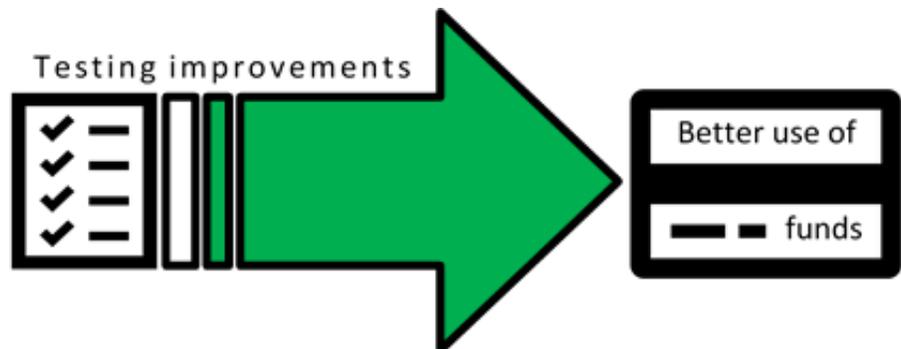
OFFICE OF INSPECTOR GENERAL

Financial Management

EPA Complied With Improper Payment Legislation, but Testing Can Be Improved

Report No. 17-P-0212

May 10, 2017



Report Contributors:

Doug LaTessa
Patrick McIntyre
Michael Petscavage
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Abbreviations

AFR	Agency Financial Report
CBOR	Compass Business Objects Reporting
CPS	Commodity Payments Statistics
CWSRF	Clean Water State Revolving Fund
DWSRF	Drinking Water State Revolving Fund
EPA	U.S. Environmental Protection Agency
FY	Fiscal Year
IPERA	Improper Payments Elimination and Recovery Act of 2010
OCFO	Office of the Chief Financial Officer
OIG	Office of Inspector General
OMB	Office of Management and Budget
RTP-FC	Research Triangle Park Finance Center, Financial Services Branch
SPITS	Small Purchase Information Tracking System
U.S.C.	United States Code

Cover image: Graphic illustrating how improved testing for improper payments can result in better use of funds for environmental and supporting programs. (EPA OIG image)

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At a Glance

Why We Did This Review

The Improper Payments Elimination and Recovery Act of 2010 (IPERA), as modified by the Improper Payments Elimination and Recovery Improvement Act of 2012, requires that each fiscal year the Inspector General of each agency determine whether the agency is in compliance with the law. In addition, Office of Management and Budget Memorandum M-15-02 states that the Office of Inspector General (OIG) may evaluate the accuracy and completeness of agency reporting and the agency's performance in reducing and recapturing improper payments. Our audit focused on the U.S. Environmental Protection Agency's (EPA's) compliance with these requirements.

This report addresses the following EPA goal or cross-agency strategy:

- *Embracing EPA as a high-performing organization.*

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Listing of [OIG reports](#).

EPA Complied With Improper Payment Legislation, but Testing Can Be Improved

What We Found

The EPA complied with improper payments legislation when reporting improper payments in fiscal year 2016. However, we noted issues of concern.

EPA Region 2 tested only 46 percent of the selected Hurricane Sandy grant expenditures for improper payments, instead of the 100 percent required. The Disaster Relief Appropriations Act of 2013 designated Hurricane Sandy disaster relief funding as susceptible to significant improper payments, requiring the EPA to develop a statistical sampling plan for testing Hurricane Sandy expenditures. Region 2 staff misunderstood the requirement to test all dollars associated with the four federal payments to the New York State Department of Environmental Conservation. Incomplete testing impacted the certainty that there were no improper payments in the sampled items for Hurricane Sandy grants payments.

Improved testing for improper payments will result in better use of funds for environmental and supporting programs.

Additionally, insufficient internal controls for commercial payments resulted in inaccurate information being reported. The EPA understated total dollar outlays for contract payments by \$33,877. Further, the EPA could not confirm the accuracy of the monthly and year-end total "Amount Paid" values, nor the improper payment error rate for commodity payments. During the course of our audit, the EPA took sufficient action to address this issue.

Recommendations and Planned Agency Corrective Actions

We recommend that the Chief Financial Officer revise its annual review guidance to include language to require testing of all dollars associated with statistically selected samples. The agency concurred with the recommendation and provided an estimated completion date of August 2017 to revise its annual review guidance. The recommendation is considered resolved with the corrective action pending.



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

THE INSPECTOR GENERAL

May 10, 2017

MEMORANDUM

SUBJECT: EPA Complied With Improper Payment Legislation, but Testing Can Be Improved
Report No. 17-P-0212

FROM: Arthur A. Elkins Jr.

A handwritten signature in black ink, appearing to read "Arthur A. Elkins Jr.", is written over the printed name.

TO: David Bloom, Acting Chief Financial Officer

This is our report on the subject audit conducted by the Office of Inspector General (OIG) of the U.S. Environmental Protection Agency (EPA). The project number for this audit was OA-FY17-0054. This report contains findings that describe the problems the OIG has identified and corrective actions the OIG recommends. This report represents the opinion of the OIG and does not necessarily represent the final EPA position. Final determinations on matters in this report will be made by EPA managers in accordance with established audit resolution procedures.

Action Required

You are not required to provide a written response to this final report because you provided agreed-to corrective actions and planned completion dates for the report's recommendation. Should you choose to provide a final response, we will post your response on the OIG's public website, along with our memorandum commenting on your response. Your response should be provided as an Adobe PDF file that complies with the accessibility requirements of Section 508 of the Rehabilitation Act of 1973, as amended. The final response should not contain data that you do not want to be released to the public; if your response contains such data, you should identify the data for redaction or removal along with corresponding justification.

We will post this report to our website at www.epa.gov/oig.

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Chapter 1

Introduction

Purpose

The purpose of the audit was to report on the U.S. Environmental Protection Agency's (EPA's) compliance with the Improper Payments Elimination and Recovery Act of 2010 (IPERA), and to evaluate the accuracy and completeness of agency reporting and performance in reducing and recapturing improper payments.

Background

Office of Management and Budget (OMB) Memorandum M-15-02¹ states that Inspectors General may evaluate (1) the accuracy and completeness of agency reporting, and (2) agency performance in reducing and recapturing improper payments. Also, Inspectors General are annually required to determine whether agencies are in compliance with the six requirements identified in IPERA.

IPERA requires agencies to conduct risk assessments of their programs or activities to determine whether they are susceptible to significant improper payments. IPERA defines significant improper payments as gross annual improper payments exceeding the statutory threshold of both 1.5 percent of program outlays and \$10 million of all program or activity payments during the fiscal year reported, or \$100 million. IPERA defines the term "payment" as any transfer or commitment for future transfer of federal funds such as cash, securities, loans, loan guarantees, and insurance subsidies to any non-federal person or entity, that is made by a federal agency, a federal contractor, a federal grantee, or a governmental or other organization administering a federal program or activity. For improper payment reporting, the EPA collects and reports improper payments by type of activity (i.e., payment stream).

For fiscal year (FY) 2016 reporting, the majority of the EPA's activities were determined to be at a low risk of significant improper payments. According to the EPA, three of the agency's risk-susceptible activities—the Clean Water State Revolving Fund (CWSRF), Drinking Water State Revolving Fund (DWSRF), and Hurricane Sandy—remain below statutory thresholds. OMB deemed the State Revolving Funds to be risk-susceptible, and the Disaster Relief Appropriations Act of 2013 (Public Law 113-2) designated Hurricane Sandy funding as susceptible to significant improper payments. In addition, grant payment activities have been newly identified as risk-susceptible based on the results of transaction testing

¹ OMB Memorandum M-15-02, dated October 20, 2014, modified OMB Circular No. A-123, Appendix C, *Requirements for Effective Estimation and Remediation of Improper Payments*.

performance in FY 2016. Therefore, the EPA stated that robust statistical sampling will be initiated for grant payments in FY 2017 and beyond to identify accurate improper payment rates and estimates.

Responsible Office

The Office of the Chief Financial Officer (OCFO) formulates and manages the EPA's annual budget and performance plan, coordinates the EPA's strategic planning efforts, develops the EPA's annual Performance and Accountability Report, and implements the Government Performance and Results Act. OCFO also provides financial services for the EPA and makes payments to the EPA grant recipients, contractors and other vendors. The office provides policy, reports and oversight essential for the financial operations of the EPA.

Scope and Methodology

We conducted this performance audit from November 2016 to April 2017 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The purpose of the audit was to report on the EPA's compliance with IPERA and evaluate the accuracy and completeness of agency reporting and performance in reducing and recapturing improper payments. To determine whether the EPA complied with IPERA, we reviewed the EPA's FY 2016 Agency Financial Report (AFR) and accompanying materials. We interviewed agency staff at the EPA headquarters for OCFO, the Office of Administration and Resources Management's Office of Grants and Debarment, and the Office of Water. We also interviewed OCFO staff from the Las Vegas, Research Triangle Park and Cincinnati Finance Centers.

We gained an understanding of the processes, procedures and controls used for improper payment and recovery reporting across the EPA—including State Revolving Funds, grants, commodities, contracts, payroll and Hurricane Sandy—and selected judgmental samples from each activity. We traced improper payments in our sample back to source documentation to test the accuracy of improper payment reporting in the EPA's FY 2016 AFR. For the State Revolving Funds, we reviewed the transaction testing worksheets to verify that they were completed in accordance with EPA policies. We reviewed all of the qualitative and quantitative risk assessments that the EPA prepared. We took steps to confirm the accuracy of both the Office of Grants and Debarment's and Las Vegas Finance Center's improper payment schedules to the EPA system-generated support data for the grants payment stream. For EPA activities that are currently

considered to be susceptible to significant improper payments, we reviewed a sample of negative draws, Program Evaluation Reports, and transaction testing reports and worksheets, to identify improper payments that were not reported.

We also used data systems, including the Grantee Compliance and Recipient Activity Database, Contract Payment System (CPS), Small Purchase Information Tracking System (SPITS), and Compass Data Warehouse. We verified the information in the systems to source documentation, and concluded that the information provided a reasonable basis for our findings and conclusions.

Prior Audit Coverage

During this audit, we followed up on agency corrective actions from EPA Office of Inspector General (OIG) Report No. [16-P-0167](#), *EPA Complied With Improper Payment Legislation, but Stronger Internal Controls Are Needed*, issued May 10, 2016. That report made seven recommendations. We verified that all corrective actions have been completed.

Chapter 2

EPA Complied With IPERA

The EPA complied with IPERA for FY 2016 reporting. IPERA established six requirements that must be met for agencies to be considered in compliance. We found that the EPA complied with all six conditions.

IPERA and OMB Provide Requirements for Compliance

IPERA and Part II, Section A(3), of OMB Memorandum M-15-02 established the following six mandatory steps for agency compliance:

- Publish an AFR or Performance and Accountability Report for the most recent fiscal year and post that report and any accompanying materials required by OMB on the agency website.
- Conduct a program-specific risk assessment for each program or activity that conforms with 31 U.S.C. Section 3321 (if required).
- Publish improper payment estimates for all programs and activities identified as susceptible to significant improper payments under its risk assessment (if required).
- Publish programmatic corrective action plans in the AFR or Performance and Accountability Report (if required).
- Publish, and meet, annual reduction targets for each program assessed to be at risk and estimated for improper payments (if required and applicable).
- Report a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published in the AFR or Performance and Accountability Report.

EPA Was in Compliance With IPERA

The EPA met the six requirements of IPERA, as shown in Table 1. Therefore, the EPA's FY 2016 improper payment reporting was in compliance with IPERA.

Table 1: EPA met the six requirements of IPERA

Requirement	Complied?	Description												
Published an AFR for the most recent fiscal year and posted it on the agency website.	Yes	The EPA published an AFR on the agency website on November 15, 2016.												
Conducted a program-specific risk assessment (if required).	Yes	<p>The EPA performed program-specific risk assessments for seven payment streams (listed below) based on OMB Memorandum M-15-02, which requires executive agencies to conduct risk assessments of their programs or activities to determine if they are susceptible to significant improper payments.</p> <ul style="list-style-type: none"> • CWSRF • DWSRF • Grants • Contracts • Commodities • Payroll • Hurricane Sandy 												
Published improper payment estimates for all programs and activities identified as susceptible to significant improper payments (if required).	Yes	<p>The CWSRF and DWSRF programs are considered to be risk-susceptible programs. The EPA reported improper payment estimates for both of these programs in Table 1 in the Improper Payments Compliance section of the AFR.</p> <p>Also, pursuant to the Disaster Relief Appropriations Act of 2013, all payments made under the act are automatically deemed susceptible to significant improper payments. As a result, the EPA designed and implemented a statistical sampling plan for testing Hurricane Sandy expenditures. The EPA reported improper payment estimates for the Hurricane Sandy payment stream in Table 1 in the Improper Payments Compliance section of the AFR.</p>												
Published programmatic corrective action plans in (if required).	Not Required	<p>The EPA did not meet the statutory threshold of \$10 million and 1.5 percent of program outlays, or \$100,000,000, and therefore the corrective action plan is not required. Improper payments reported for risk-susceptible programs were:</p> <ul style="list-style-type: none"> • CWSRF - \$80,000 • DWSRF - \$170,000 • Hurricane Sandy - \$0 												
Published and met annual reduction targets for each program assessed to be at risk and estimated for improper payments.	Yes	<p>The EPA published and met the annual reduction targets for FY 2016. Each year, the EPA establishes a targeted rate that is a reduction from the prior year's targeted rate. The actual improper payment rate was less than the targeted rate established as the reduction target for FY 2016.</p> <table border="1" data-bbox="695 1440 1252 1583"> <thead> <tr> <th>Payment Stream</th> <th>Targeted rate (percent)</th> <th>Actual rate (percent)</th> </tr> </thead> <tbody> <tr> <td>CWSRF</td> <td>1.45</td> <td>.01</td> </tr> <tr> <td>DWSRF</td> <td>1.99</td> <td>.01</td> </tr> <tr> <td>Hurricane Sandy</td> <td>1.5</td> <td>0</td> </tr> </tbody> </table>	Payment Stream	Targeted rate (percent)	Actual rate (percent)	CWSRF	1.45	.01	DWSRF	1.99	.01	Hurricane Sandy	1.5	0
Payment Stream	Targeted rate (percent)	Actual rate (percent)												
CWSRF	1.45	.01												
DWSRF	1.99	.01												
Hurricane Sandy	1.5	0												
Reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published in the AFR.	Yes	<p>The EPA reported gross improper payment rates of less than 10% for each payment stream.</p> <ul style="list-style-type: none"> • CWSRF: .01% • DWSRF: .01% • Hurricane Sandy: 0% 												

Source: OIG analysis of EPA data.

Chapter 3

Testing for Hurricane Sandy Improper Payments Needs Improvement

Testing for Hurricane Sandy improper payments needed improvement. EPA Region 2 staff did not test all grant expenditures corresponding to the selected Hurricane Sandy payments for improper payments. Region 2 staff tested only 46 percent of the expenditures corresponding to the four selected federal payments for the state of New York. The Disaster Relief Appropriations Act of 2013 designated Hurricane Sandy disaster relief funding as susceptible to significant improper payments, requiring the EPA to develop a statistical sampling plan for testing Hurricane Sandy expenditures. The EPA applied a stratified random sampling methodology in selecting payments to review. However, EPA Region 2 staff misunderstood that they were required to test all dollars associated with the four federal payments selected. Not testing 100 percent of the grant dollars associated with the four selected federal payments impacted the certainty that there were no improper payments in selected Hurricane Sandy grants.

Legislation and EPA Policy Provide Guidance on Sampling

The Disaster Relief Appropriations Act of 2013 designated Hurricane Sandy disaster relief funding as susceptible to significant improper payments. Per OMB M-13-07 requirements, the EPA developed a statistical sampling plan for testing Hurricane Sandy expenditures. The EPA applied a stratified random sampling methodology in selecting payments for review, as the EPA recognized that Hurricane Sandy expenditures are comprised of several categories, including, for example, grants and contracts. The sampling plan stated that the EPA would conduct estimates of these categories to identify potential weaknesses and vulnerabilities. As a result, the EPA applied a stratified random sampling methodology in selecting payments for review, which would increase the precision of the estimate of the percentage of erroneous payments. Within each category, the EPA's sampling methodology stated that a simple random sample of payments would be selected for review. The impact of this stratification was to maximize the total number of dollars being selected for review.

Region 2 Staff Did Not Test All Hurricane Sandy Grant Expenditures

EPA Region 2 staff did not test all (100 percent) selected Hurricane Sandy grant dollars for improper payments. EPA Region 2 tested only 10 of the 65 invoices, or \$118,141 of \$255,524 (46 percent) of the expenditures corresponding to the four selected federal payments for the state of New York. The EPA's OCFO statistician confirmed that the expectation in the sampling plan was that 100 percent of the underlying dollars in each selected payment would be tested. Region 2 staff did not understand that all dollars associated with the four selected Hurricane Sandy payments should have been tested. Instead, staff thought that

they needed to test at least a portion of each of those four federal payments. Therefore, Region 2 did not test all of the underlying dollars associated with those federal payments.

After reviewing the 10 invoices, staff informed us that it was clear that all evidence of documentation of costs was in order. Based on this, Region 2 staff stated that the documentation proved the validity of the recipient's internal control system and, as a result, there was no need to test the remaining invoices. However, the lack of 100-percent testing of the grant dollars impacted the certainty that there were no improper payments in the four payments for the Hurricane Sandy grants strata.

Actions Taken

On January 31, 2017, an EPA Region 2 grant specialist informed the OIG that all transaction testing had been completed and that no additional improper payments were identified. Thus, Region 2 indicated that as of January 31, 2017, all Hurricane Sandy dollars had been tested.

Recommendation

We recommend that the Chief Financial Officer:

1. Revise the annual guidance on improper payments reporting to include language requiring that 100 percent of all dollars associated with statistically selected samples are tested for improper payments.

Agency Comments and OIG Evaluation

The EPA agreed with the recommendation and will revise its annual guidance to include language requiring that 100 percent of all dollars associated with statistically selected samples are tested for improper payments. The EPA provided an estimated completion date of July 31, 2017, for the corrective action. The recommendation is considered resolved pending completion of the corrective action.

Chapter 4

Improvement Is Needed in Process of Collecting and Reporting Improper Payments for Contract and Commodity Payments

Insufficient internal controls lead to inaccurate information being collected and reported to stakeholders. Although the reported improper payments dollar amount and error rate was accurate for contract payments, the EPA understated total dollar outlays for contract payments by \$33,877. For commodities payments, the EPA could not confirm the accuracy of the monthly and year-end total “Amount Paid” values, nor the improper payment error rate. Internal control should provide reasonable assurance that reporting for internal and external use is reliable. The deficiencies noted occurred because the Standard Operating Procedure did not include sufficient detail for when software upgrades required the reporting process to change mid-year.

Internal Controls Needed to Achieve Reporting Reliability

Section OV1. 01 of the U.S. Government Accountability Office’s *Standards for Internal Control in the Federal Government* (GAO-14-704G), issued September 2014, defines internal control as:

A process effected by an entity’s oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved. These objectives and related risks can be broadly classified into one or more of the following three categories:

- Operations - Effectiveness and efficiency of operations
- Reporting - Reliability of reporting for internal and external use
- Compliance - Compliance with applicable laws and regulations

Internal Controls Were Not Sufficient to Detect Reporting Errors

Although we noted no exception in the reported improper payments dollar amount and error rate, the OCFO Research Triangle Park Finance Center’s (RTP-FC’s) quantitative risk assessment for the contract payments understated total dollar outlays by \$33,877. In addition, for 11 of 12 months, RTP-FC’s staff could not confirm the accuracy of the reported commodity payments values for the

“Amounts Paid,” nor the aggregate yearly total “Amounts Paid” value of \$214,790,300.

Internal controls were not sufficient to identify and correct the reporting errors caused by human errors that were made during the process. During RTP-FC’s data collection and reporting process for improper contract payments, RTP-FC did not use the correct improper payment reporting data for the total dollar outlay.

During the data collection and reporting process for commodities improper payments, RTP-FC encountered the following issues:

- EPA’s Compass Financial System was upgraded in February 2016. After the upgrade, RTP-FC staff discovered reporting errors in the Commodity Payments Statistics (CPS) reports from the Small Purchase Information Tracking System (SPITS). Therefore, Compass Business Objects Reporting (CBOR) reports were used in subsequent months.
- RTP-FC staff stated that a year-end CPS report was not generated from SPITS due to a system reporting error discovered after the February 2016 update to Compass. RTP-FC staff stated they could not rely on the data being reported from SPITS. Thus, no reconciliation was performed to account for subsequent monthly adjustments.
- RTP-FC staff did not generate either a year-end CPS or a CBOR report to reconcile monthly adjustments posted to the Compass Financial System for the “Amounts Paid” values reported in the monthly SPITS and CBOR reports. After the Compass Financial System update in February 2016, staff recognized errors in some of the data reported in the SPITS reports. Due to these reporting errors and not performing a year-end reconciliation, staff could not confirm the accuracy of the “Amounts Paid” values.
- RTP-FC staff could not confirm the accuracy of the year-end “Amounts Paid” values for 11 of 12 months, the aggregate year-end total “Amount Paid” value, or the 0.10 percent error rate. This occurred because RTP-FC did not account for adjustments to the “Amounts Paid” values that were made to the prior monthly SPITS and CBOR reports.

The RTP-FC’s Standard Operating Procedure - Improper Payments Reporting, December 6, 2016,² does not specifically identify the data from either the CPS, SPITS or CBOR reports that should be used to populate the commodity and contract payments quantitative risk assessments. The Standard Operating Procedure also does not include a requirement to track monthly adjustments in CBOR reports, and reconcile the accumulative monthly reports with the year-end report.

² Section G, "Improper Payment Reporting Requirements"; and Appendix C: Improper Payments QA Checklist.

As a result of the reporting errors for contract payments, and the unreliability of the commodities payments computed error rate of 0.10 percent, stakeholders—such as the public, Congress and other federal agencies—may not be able to rely on the accuracy of the information the EPA collected and reported.

Actions Taken

On February 2, 2017, RTP-FC amended the current Standard Operating Procedure to include the following:

- Clarify, with specificity, which documents are to be generated from each data system.
- Clarify, with specificity, which data field values from the generated reports are to be used to populate the quantitative risk assessment.
- Document the process to reconcile the monthly CBOR reports to the year-end values for the “Total Invoices Paid” and “Amounts Paid” values.

We are not making any recommendations regarding this issue because the agency took sufficient corrective actions to address this issue during the course of our audit.

Status of Recommendations and Potential Monetary Benefits

RECOMMENDATIONS

Rec. No.	Page No.	Subject	Status ¹	Action Official	Planned Completion Date	Potential Monetary Benefits (in \$000s)
1	7	Revise the annual guidance on improper payments reporting to include language requiring that 100 percent of all dollars associated with statistically selected samples are tested for improper payments.	R	Chief Financial Officer	7/31/17	

¹ C = Corrective action completed.
 R = Recommendation resolved with corrective action pending.
 U = Recommendation unresolved with resolution efforts in progress.

Agency Response to Draft Report

(Received April 26, 2017)

MEMORANDUM

SUBJECT: Response to Office of Inspector General Draft Audit Report No. OA-FY17-0054, “EPA Complied With Improper Payment Legislation, but Testing Can Be Improved,” dated April 11, 2017

FROM: David A. Bloom, Acting Chief Financial Officer
Office of the Chief Financial Officer

TO: Michael Petscavage, Director of Contracts and Assistance Agreement Audits
Office of Inspector General

Thank you for the opportunity to respond to the recommendation in the subject draft audit report. The following is a summary of the agency’s overall position on the report recommendation.

AGENCY’S OVERALL POSITION

The agency concurs with the recommendation in the draft audit report.

AGENCY’S RESPONSE TO DRAFT AUDIT RECOMMENDATION

Agreements

No.	Recommendation	High-Level Intended Corrective Action(s)	Estimated Completion
1	The Chief Financial Officer revise the annual guidance on improper payments reporting to include language requiring that 100 percent of all dollars associated with statistically selected samples are tested for improper payments.	Office of the Chief Financial Officer will revise the annual guidance to include language requiring that 100 percent of all dollars associated with statistically selected samples are tested for improper payments.	7/31/2017

CONTACT INFORMATION

If you have any questions regarding this response, please contact the OCFO’s Audit Follow-Up Coordinator, Benita Deane, at 202-564-2079.

cc: Jeanne Conklin
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