



U.S. ENVIRONMENTAL PROTECTION AGENCY

OFFICE OF INSPECTOR GENERAL

Spending Taxpayer Dollars

EPA Region 9 Needs to Improve Oversight Over Commonwealth of the Northern Mariana Islands Consolidated Cooperative Agreements

Report No. 16-P-0207

June 20, 2016



Report Contributors:

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Abbreviations

BECQ	Bureau of Environmental & Coastal Quality
CCA	Consolidated Cooperative Agreement
CFR	Code of Federal Regulations
CNMI	Commonwealth of the Northern Mariana Islands
CUC	Commonwealth Utilities Corporation
DCRM	Division of Coastal Resources Management
DEQ	Division of Environmental Quality
EPA	U.S. Environmental Protection Agency
FFR	Federal Financial Report
FY	Fiscal Year
IA	Interagency Agreement
OIG	Office of Inspector General

Cover photo: Agingan Wastewater Treatment Plant with view of the Pacific Ocean, Island of Saipan, CNMI. (EPA OIG photo)

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At a Glance

Why We Did This Review

The U.S. Environmental Protection Agency (EPA) has significantly increased its funding of environmental programs in the Commonwealth of the Northern Mariana Islands (CNMI), from approximately \$1 million in 2006 to \$8.5 million in 2013. We conducted this audit to determine whether the EPA:

- Has controls and processes in place to ensure proper oversight of CNMI assistance agreements.
- Is ensuring that the assistance agreements effectively and efficiently protect human health and the environment.

During the course of our audit, we decided to focus on consolidated cooperative agreements, as they involved the most funding.

This report addresses the following EPA goals or cross-agency strategies:

- *Protecting America's waters.*
- *Launching a new era of state, tribal and local partnerships.*

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EPA Region 9 Needs to Improve Oversight Over Commonwealth of the Northern Mariana Islands Consolidated Cooperative Agreements

What We Found

The internal controls of the CNMI Department of Environmental Quality (DEQ) and Commonwealth Utilities Corporation (CUC) over assistance agreements need improvement, as well as Region 9's oversight of CNMI's consolidated cooperative agreements. We identified the following areas requiring attention:

- DEQ and CUC labor charging practices do not comply with federal requirements.
- DEQ and CUC consolidated cooperative agreements have inconsistent terms and conditions on agreement payment.
- DEQ inconsistently reported-in-kind and interagency agreement costs.
- Region 9 project files were not readily available to third parties.

More than \$58 million in consolidated cooperative agreement funds are not being administered efficiently and effectively due to inadequate oversight and lack of internal controls.

Recipients are required to comply with consolidated cooperative agreement terms and conditions, as well as the Code of Federal Regulations (CFR) in 2 CFR Part 225 and 40 CFR Part 31. Without adequate internal controls and oversight, over \$58 million in consolidated cooperative agreements funds may not be administered efficiently and effectively, thus reducing the impact those funds could have on improving human health and the environment. As a result, CNMI agencies need to improve the management of EPA-funded projects, and the EPA needs to expand its internal controls accordingly.

Recommendations and Planned Agency Corrective Actions

We made eight recommendations to Region 9 regarding oversight and the need for other improvements, including:

- Disallowing and recovering over \$1.4 million in unsupported labor costs.
- Using appropriate grant payment methods and level of project officer review.
- Improving in-kind and interagency agreement expenditure reporting.
- Improving maintenance of Region 9 project officer files.

Region 9 concurred with all of the recommendations. Some concurrences included modifications, and Region 9 plans to complete the majority of the corrective actions by September 30, 2016.



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

THE INSPECTOR GENERAL

June 20, 2016

MEMORANDUM

SUBJECT: EPA Region 9 Needs to Improve Oversight Over Commonwealth of the Northern Mariana Islands Consolidated Cooperative Agreements
Report No. 16-P-0207

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: Alexis Strauss, Acting Regional Administrator
Region 9

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-FY14-0035. 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.

The following Region 9 offices share responsibilities regarding the Commonwealth of the Northern Mariana Islands: Pacific Islands Office; Infrastructure Section, within the Water Division; the Tribal and State Assistance Branch; the Grants Management Office; the Drinking Water Management Section; and the Enforcement Division.

Action Required

The agency provided acceptable corrective actions for addressing the recommendations, with completion milestone dates. Therefore, a response to the final report is not required. The OIG may make periodic inquiries on your progress in implementing these corrective actions. Please update the EPA's Management Audit Tracking System as you complete planned corrective actions. 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.

This report will be available at www.epa.gov/oig.

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Chapter 1

Introduction

Purpose

The Office of Inspector General (OIG) conducted an audit of the U.S. Environmental Protection Agency's (EPA's) assistance agreements with the Pacific Territory of the Commonwealth of the Northern Mariana Islands (CNMI). Our objectives were to determine whether the EPA:

- Has controls and processes in place to ensure proper oversight of CNMI assistance agreements.
- Is ensuring that the assistance agreements effectively and efficiently protect human health and the environment.

Background

Major environmental laws allow the EPA to authorize state, tribal and local governments, and U.S. territories to conduct permitting, inspection and enforcement activities. Authorized governments must have adequate personnel, funding and authority to carry out the program. The EPA may withdraw authorization if a government is not adequately carrying out the provisions of the law in administering or enforcing the program.

From fiscal years (FYs) 2008 through 2014, EPA Region 9 awarded the Pacific Territory of CNMI \$58 million in consolidated cooperative agreement (CCA) amounts for accomplishing wide-ranging goals such as planning, developing and continuing the implementation of environmental management and protection statutes, regulations and programs.

The Omnibus Territories Act of 1977, as amended, authorized federal agencies to extend to the governments of CNMI, Guam and American Samoa and their agencies and instrumentalities the ability to consolidate grant funding.

Map showing CNMI (Saipan, Tinian and Rota)



Source: EPA image.

CNMI consists of a volcanic and limestone archipelago of 14 islands extending in a generally north-south direction for 338 nautical miles, for a land area of 176 square miles. CNMI is located 16,259 flight miles from San Francisco, California. Saipan, with approximately 48,000 people, is the largest island (46 square miles), and is the urban, commercial and government center.



A sign showing an EPA-funded project on Saipan. (EPA OIG photo)

Thousands of people also live on the islands of Rota (32 square miles) and Tinian (39 square miles), which are largely rural. The median household income is 45 percent below the U.S. average. Growth has strained the ability of the local government to provide adequate infrastructure and environmental protection.

Region 9 collectively refers to CNMI, Guam and American Samoa as the “Pacific Territories.”

Region 9 awarded CCAs to address environmental challenges in CNMI involving the Clean Water Act and the Safe Drinking Water Act. CNMI has two entities involved in implementing the CCAs:

- **Bureau of Environmental & Coastal Quality (BECQ), Division of Environmental Quality (DEQ):** On November 13, 2013, the Governor of CNMI issued Executive Order No. 2013-24. The order reorganized and merged the DEQ (mostly funded by the EPA) and the Division of Coastal Resources Management (DCRM) (mostly funded by the U.S. Department of the Interior) to establish the BECQ. The purpose of the merger was to enhance efficiency and collaboration between the two environmental entities through integration of services and strategic goals, sharing of resources, and elimination of overlapping responsibilities.
- **Commonwealth Utilities Corporation (CUC):** CUC is a state government corporation. The CUC operates the electric, power, water and wastewater services on CNMI. CUC is a semi-autonomous agency of the CNMI government.

Starting in 2010, funding levels for CNMI have increased compared to prior years, and currently average over \$8.5 million per year. Funding was increased to address long-standing infrastructure and environmental needs. From FYs 2008 through 2014, Region 9 awarded more than \$58 million in environmental protection and construction funds to CNMI, as shown in Table 1.

Table 1: EPA CCAs to CNMI

Recipient	Agreement	Project period	Award amount
DEQ	M00915609	10/01/2008 – 09/30/2013	\$11,437,521
DEQ	M00915614	10/01/2013 – 09/30/2018	5,978,491
CUC	M00T33711	09/01/2010 – 08/31/2017	36,713,404
CUC	M00T33715	10/01/2014 – 09/30/2019	4,200,000
Total			\$58,329,416

Source: CCAs to CNMI.

Noteworthy Achievements

In March 2009, a District Court judge in the CNMI entered two stipulated orders requiring that CUC maintain compliance with the Clean Water Act/Safe Drinking Water Act. Stipulated order number one includes (1) reformation of CUC’s management, finances and operations; (2) development of a wastewater and drinking water master plan; and (3) construction of wastewater infrastructure. Stipulated order number two includes oil spill prevention, preparedness and response actions.

Responsible Offices

The following EPA Region 9 offices share responsibilities regarding CNMI:

- **Pacific Islands Office:** This office manages domestic programs and grants in the Pacific Territories, including for CNMI. CCAs fund the implementation of CNMI’s environmental protection programs. Region 9 reported that in addition to managing grant assistance programs, the Pacific Islands Office also coordinates with other offices in the region and nationally on regulatory and enforcement matters in the Pacific territories.
- **Infrastructure Section:** Within Region 9’s Water Division, the Tribal and State Assistance Branch has managed and supervised the EPA’s grants to the Pacific Territory public utilities since 2013. The section has expertise in managing drinking and clean water grants.

The Grants Management Office, the Drinking Water Management Section, and the Enforcement Division also share responsibilities regarding CNMI.

Scope and Methodology

We conducted this audit from April 16, 2014, to March 31, 2016, in accordance with generally accepted government auditing standards, issued by the Comptroller General of the United States. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

During the course of our review, we decided to focus on CCAs, as they involved the most funding. To answer our objectives, we reviewed:

- Omnibus Territories Act of 1977.
- The Code of Federal Regulations (CFR), specifically 2 CFR Part 225 (formerly Office of Management and Budget Circular A-87), *Cost Principles for State, Local, and Indian Tribal Governments*.
- Federal regulations at 40 CFR Part 31, *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*.
- Office of Management and Budget Circular A-123, *Management's Responsibility for Internal Control*.
- Region 9's Quality Management Plan.
- EPA's Assistance Agreement Almanac.
- EPA's Records Management Policy (CIO 2155.3).

We reviewed the active and recently closed Region 9 CCAs awarded to DEQ and CUC for the periods 2008 through 2019, as well as project officer End of Year reports from 2011 through 2014. We interviewed managers and staff in Region 9's Pacific Islands Office and Water Division. We also interviewed federal personnel outside the EPA involved in the Pacific Territories.

We conducted a 2-week site visit to CNMI. We interviewed staff and management from the Office of Public Auditor, DEQ and CUC. We obtained documentation concerning financial and operational matters from DEQ and CUC, including:

- Standard Operating Procedures.
- Detailed annual budget.
- Data on EPA-funded projects.
- Quarterly progress reports.
- Reimbursement request.
- Financial transactions.
- Cooperative agreement workplans.



Pump station at S-8 lift station, Saipan.
(EPA OIG photo)

We toured 18 project sites on CNMI. Sites included sewer replacements and connections, wastewater treatment plants, lift stations, water tank and waterline replacements, and a chlorine storage facility.



Interior view of wastewater treatment plant, Saipan. (EPA OIG photo)

We reviewed the Federal Managers' Financial Integrity Act Annual Assurance Letters from FYs 2012 through 2014 for Region 9 to determine whether those letters identified any weaknesses related to CNMI. The letters did not identify any weaknesses.

We reviewed the 2010 through 2014 Single Audit Act reports on CNMI for issues related to the operations of DEQ and CUC. The Single Audits noted a continual finding related to DEQ labor costs, which is addressed in Chapter 2 of this report.

Prior Audit Coverage on Pacific Territories

On May 9, 2016, the OIG issued Report No. [16-P-0166](#), *EPA Region 9 Needs to Improve Oversight Over Guam's Consolidated Cooperative Agreements*. We made 18 recommendations to Region 9 regarding oversight and the need for other improvements. Region 9 concurred with all the recommendations and plans to complete a majority of the corrective actions by September 30, 2016.

On May 23, 2016, the OIG issued Report No. [16-P-0181](#), *EPA Region 9 Needs to Improve Oversight Over American Samoa Consolidated Cooperative Agreements*. We made five recommendations to EPA Region 9 regarding oversight and the need for other improvements. Region 9 concurred with all the recommendations and plans to complete a majority of the corrective actions by September 30, 2016.

Chapter 2

DEQ and CUC Labor-Charging Practices Do Not Comply With Federal Requirements

DEQ and CUC did not comply with federal requirements for charging labor costs to the CCAs. DEQ's labor and fringe benefits were unallowable due to inadequate support and inadequate allocations of labor costs among multiple funding sources. CUC's labor and fringe benefits were unallowable due to the use of estimated allocations instead of actual activities performed. Federal regulations at 2 CFR Part 225 require that when employees work on multiple activities their salaries must be distributed and supported by personnel activity reports, which the employee must sign. In addition, labor charges are to be based upon an after-the-fact distribution of the actual activity and not budgets. DEQ staff believed they had corrected problems with labor charging practices by discontinuing timecards and implementing a labor distribution system. CUC staff believed their use of estimates was acceptable based on the Region 9 project officer's approval. As a result, for DEQ we questioned \$1,082,982 in unallowable labor and fringe benefit costs, and for CUC questioned \$402,197 in unallowable labor and fringe benefit costs.

Requirements for Documenting Labor Costs From Multiple Sources

Federal cost principles require that labor charges be based upon actual activities performed where employees work on more than one federal award or other funding source. Federal regulations at 2 CFR Part 225, Appendix B, Section 8.h.(4), require labor charges to be supported by personnel activity reports or equivalent documentation that meet the requirements of Section 8.h.(5) to be allowable for reimbursement under federal awards. Two of the requirements are that personnel activity reports must reflect an after-the-fact distribution of the actual activity of each employee, and must be signed by the employee. Budget estimates or other distribution percentages determined before the services were performed do not qualify as support for charges to federal awards.

DEQ Labor Charges Inadequately Supported

Continuing Single Audit Finding on DEQ/BECQ Labor Issues

There has been a continuing finding in the CNMI Single Audits¹ on DEQ/BECQ labor issues. The 2014 CNMI Single Audit reported that from 2009 through 2014

¹ In accordance with the Single Audit Act of 1984 and Office of Management and Budget guidance, nonfederal entities that expend more than \$750,000 in federal funds are required to have a comprehensive annual audit of their financial statements and compliance with major federal program requirements. The entities receiving the funds include states, local governments, tribes and not-for-profit organizations.

there has been a finding related to DEQ on lack of employee certifications. The finding in the 2014 Single Audit report stated that:

Tests of employee activities noted that required certifications are not obtained for employees working full-time on specified federal programs. Although employees are signing off on timecards or timesheets evidencing hours worked on a federal program, the sign off does not indicate if the employee actually performed activities solely for the one federal program.

BECQ's response to the 2014 finding stated that:

As of 2014, all BECQ employees began signing bi-weekly timesheets to evidence hours worked on federal grant activities. This year, BECQ will comply with 2 CFR Part 225 and will certify employee time worked solely on federal programs on a semi-annual basis to satisfy the requirement of OMB A-87.

Due to the ongoing Single Audit finding, the OIG included a review of DEQ/BECQ's payroll activities as part of our review.

Based on findings in the 2013 CNMI Single Audit, on July 30, 2014, the EPA OIG recommended that DEQ be placed on a high-risk designation. On February 5, 2015, EPA Region 9 made a determination that "due to the recipient's response and corrective actions that have been taken, we will not be considering the recipient to be high-risk at this time." However, as explained in the prior paragraph, the 2014 CNMI single audit included the continuing finding on lack of employee certifications.

Prior to Fiscal Year 2014

DEQ labor charges were inadequately supported prior to FY 2014 and are therefore unallowable. DEQ's timekeeping system prior to FY 2014 used a time clock system where employees punched in their time upon the start and end of their shift. This system had no provision for distribution of actual labor costs among funding sources and did not have employee or supervisor certifications, as required by 2 CFR Part 225, Appendix B, Section 8.h(3). As addressed in the prior paragraph, there has been a continual finding in the CNMI Single Audits from 2009 through 2014 on DEQ's noncompliance with required certifications for employees working full-time on federal programs. Despite the continuing Single Audit finding, the EPA project officer reported for 2011 through 2013 that DEQ was in full compliance with the Single Audit Act because issues in the Single Audit Act reports have been successfully resolved. There were four EPA awards to DEQ with budget periods beginning prior to 2014 (M00915609, 2P00T32709, L96981101 and OS83370401) that included funding for labor and fringe benefits. DEQ staff should have been allocating labor among funding sources.

Fiscal Year 2014

In response to the continuing CNMI Single Audit finding, as previously addressed, in FY 2014 DEQ changed its labor charging practices to a system that distributes labor among funding sources. Although the new system was an improvement over the former use of timecards, it still did not capture all funding sources for allocation purposes, as required by 2 CFR Part 225. DEQ's labor distribution system included only three funds (EPA Region 9 CCA funds, local funds, and Hazardous Materials Emergency Preparedness funds). DEQ had two EPA assistance agreements (M00915614 and OS83370401) that included funding for labor and fringe benefits. To comply with 2 CFR Part 225, all of DEQ's funding sources need to be included in the labor distribution system to enable employees to appropriately distribute actual labor costs. DEQ's new labor distribution system did not include award OS83370401; therefore, labor charges for FY 2014 to present are unallowable.



Logos of DEQ and DCRM before (top), and the BECQ logo after the merger. (CNMI website)

Impact of Merger

In November 2013, DEQ and DCRM were merged into the BECQ. DEQ did not ensure that actual labor costs for certain positions with cross-cutting responsibilities were properly distributed as required by 2 CFR Part 225. Staff with cross-cutting activities or both divisions include the administrator, deputy administrator and attorney, and may include information technology, laboratory and administrative staff. The labor charges for these positions should be based on an employee's actual work activity, and be charged to projects where work was performed. We found that these staff charged 100 percent of their actual labor cost to the Region 9 CCAs. These staff may need to distribute actual labor costs among DEQ funding sources, and must allocate actual labor costs to DCRM funding sources based on actual work performed. The EPA project officer agreed that the administrator, attorney and deputy administrator should be allocating only 50 percent, 80 percent and 90 percent of actual labor costs, respectively, to the EPA consolidated agreement. The EPA project officer also said other staff may need to allocate actual labor costs differently.

DEQ Was Unaware of Labor Charging Deficiencies

DEQ was unaware of deficiencies in its labor accounting practices both before and after the CNMI Single Audit. In addition, DEQ's internal procedures allowed labor and fringe benefits to be charged to federal awards without a labor distribution system. Such a system would allocate labor charges to all funding

sources based on an after-the-fact distribution of an employee’s actual activity, and be supported by employee-signed personnel activity reports or the equivalent.

CUC Labor Charges Inappropriately Based Upon Estimates

Some of CUC’s labor charging practices did not comply with 2 CFR Part 225, and, therefore, these costs are unallowable. Federal regulations at 2 CFR 225, Appendix B, Subsection 8.h.(4), require that where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation that meets the standards in Subsection 8.h.(5). Such documentary support will be required where employees work on more than one federal award. Subsection 8.h.(5) requires that the personnel activity reports must reflect an after-the-fact distribution of the actual activity of each employee, and also states that budget estimates or other distribution percentages determined before the services are performed do not qualify as support.

According to CUC’s accounting records, CUC charged labor costs to the CCA based on an estimated percentage of labor ranging from 65 to 90 percent of the employee’s salary for certain classes. These labor classes included the grant officer, grant specialist and chief engineer. Although CUC has multiple sources of funding, these employees do not allocate their time by pay period among different cost objectives or funding sources. Instead, estimates are set in advance for a 6-month timeframe, and there is no reconciliation by employees to actual activity. At the end of a 6-month cycle, CUC’s executive director signs a “verification of hours worked.” For example, in a November 28, 2012, memorandum, the executive director asserted that the grants officer and the grants specialist each dedicated 80 percent of their time, and the chief engineer dedicated 90 percent of his time, administering the CCA for pay periods covering May 5, 2012, to November 3, 2012.

CUC has been awarded over \$69 million in federal grant awards, as summarized in Table 2 below and detailed further in Appendix A. As CNMI CUC has multiple sources of funding, these certifications by CUC management are not allowable.

Table 2: Summary of grants awarded to CUC

Agency	No. of awards	Total funds awarded
Department of the Interior	22	\$26,515,926
Department of Commerce	2	1,779,292
EPA	2	40,913,404
Total	26	\$69,208,622

Source: CUC data provided to EPA OIG.

CUC Believed Estimated Labor Costs Were Allowable

CUC believed it was acceptable to charge labor and related charges based on estimates due to incorrect guidance by the EPA project officer. The project officer approved the use of estimated costs for charging of certain labor classes to the

Region 9 CCAs. In an email to CUC dated July 19, 2012, the project officer suggested the new chief engineer be paid 90 to 95 percent from the Region 9 CCA. In an email dated September 18, 2012, the project officer stated he estimated labor charges for the grants officer and grants specialist based on an administration percentage of 80 to 85 percent. While the labor costs for the three classes of labor discussed are allowable, the use of estimated percentages is not.

Over \$1.4 Million in Unallowable Labor Costs Claimed

As we explained above, as of September 30, 2014, we identified unallowable labor and related costs charged to three EPA grants (according to recipient accounting records) due to noncompliance of \$1,485,179 (see Table 3).

Table 3: Unallowable labor costs

Agreement	Labor and fringe benefits
DEQ	
M00915609 M00915614	\$1,082,982 <i>Note 1</i>
CUC	
M00T33711	\$402,197 <i>Note 2</i>
Total DEQ and CUC	\$1,485,179

Note 1: Questioned labor costs based on budget amounts set-aside in the workplan(s) for 14 split-funded employees.

Note 2: Questioned labor costs based on data provided by the EPA supporting six administrative staff with labor charges based on budget estimates.

Source: EPA Financial Data Warehouse and documentation provided by DEQ and CUC.

For DEQ, we questioned unallowable costs of \$1,082,982 based on budget amounts set aside in the workplans for 14 split-funded employees. These costs were questioned based on transactions provided by DEQ that were charged without adequate supporting documentation and did not comply with federal requirements.

For CUC, we questioned \$402,197 in unallowable labor and fringe benefit costs claimed on the CCA based on accounting records because they were charged based upon budget estimates and did not comply with federal requirements.

Recommendations

We recommend that the Regional Administrator, Region 9:

1. Disallow and recover the \$1,082,982 in DEQ unsupported labor costs unless DEQ provides support that complies with 2 CFR Part 225, Appendix B, Section 8.h, requirements and CCA terms.
2. Disallow and recover the \$402,197 in CUC unsupported labor costs unless CUC provides support that complies with 2 CFR Part 225, Appendix B, Section 8.h, requirements and CCA terms.
3. For future EPA agreements, verify that DEQ and CUC labor-charging cost practices comply with federal requirements under 2 CFR Part 225 and CCA terms.

Agency Response and OIG Evaluation

Region 9 concurred with Recommendations 1 through 3, in some instances with modification.

For Recommendation 1, Region 9 concurred with modification and stated:

The audit recommended disallowing up to the entire grant award amount for FY 2009-2014 of \$14,712,514 for the consolidated grants for DEQ. However the underlying finding is related more specifically to documenting labor costs from multiple sources and indirect costs. The audit states: "The questioned costs will be reduced based on the recipients providing detailed cost information." Accordingly, EPA recommends that the questioned costs be limited to the payroll costs for split-funded employees. Out of approximately 45 employees only 14 were split funded. Region 9 is proposing to limit the recommended disallowed labor costs to up to \$1,082,982, the budget amounts set aside in the workplans for split-funded employees.

In addition, the audit states that DEQ charged an unallowable overhead rate of 14 percent to the CCAs, contrary to the CCA terms. However, based on documentation and confirmation provided by DEQ, it does not appear that DEQ is charging 14% for indirect costs. Therefore, EPA will not pursue recovery of indirect costs.

For the labor cost component of the finding, Region 9 provided a planned completion date of September 30, 2017, for Recommendation 1. The OIG concurs with Region 9's proposal to modify the questioned labor cost to reflect the \$1,082,982 for 14 split-funded employees. The OIG concurs with the agency's

proposed actions. When implemented, the corrective actions should satisfy the intent of Recommendation 1. The recommendation will remain open pending completion of the proposed corrective action.

For the indirect cost component of the finding, Region 9 stated that "...based on documentation and confirmation provided by DEQ, it does not appear that DEQ is charging 14% for indirect costs. Therefore, EPA will not pursue recovery of indirect costs." The OIG concurs with Region 9's position, and based on supporting documentation provided by Region 9, we eliminated the indirect cost element of the finding from the report.

For Recommendation 2, Region 9 concurred with modification and stated:

Region 9 has reviewed selected invoices from the period in question and has concluded that CUC did not charge EPA grants for indirect costs. Although CUC appears to have set aside 3% of their budget under the category of indirect costs, it was only done for accounting purposes.... Therefore, Region 9 requests that the OIG narrow the recommendation to address only unsupported labor costs.

During the exit conference on May 25, 2016, Region 9 requested that the CUC questioned labor costs of \$823,963 be reduced to \$402,197, based on data obtained from CUC that indicated only six staff were charging labor costs based on budget estimates. Based on the OIG review of the data provided by the region, we have decreased the questioned cost to \$402,197.

For both indirect costs and labor costs, the OIG concurs with Region 9's position and approach. Based on supporting documentation provided by Region 9, we eliminated the indirect cost element of the finding from the report. The OIG believes the proposed actions by Region 9 address Recommendation 2. This recommendation will remain open pending completion of the proposed corrective action.

Region 9 concurred with Recommendation 3 and stated:

Region 9 POs [project officers] will review future payment requests to ensure all labor-charges comply with federal requirements per 2 CFR Part 225 and CCA terms. Region 9 POs for CUC will review all payment requests and supporting documentation to ensure there are no indirect costs being requested.

The OIG believes the proposed actions by Region 9 address Recommendation 3. This recommendation will be considered closed upon issuance of report. We will use the date of Region 9's response (May 4, 2016) as the completion date.

Region 9's complete response to the draft report is in Appendix B.

Chapter 3

DEQ and CUC CCAs Have Inconsistent Terms and Conditions on Agreement Payment

The Region 9 CCAs to DEQ and CUC have inconsistent terms and conditions on agreement payment requirements for the recipient to follow. In addition, Region 9 oversight over CCA payments is not consistent. Region 9 may require the reimbursement method for CCA payments as a special award condition, according to 40 CFR § 31.21(d). Region 9 included some reimbursement terms in the agreements by placing an extra measure of control over recipient funds by requiring the recipient to submit draw requests to the EPA project officer for review and approval prior to payment. However, this extra measure of control was never completely implemented. Consequently, there was confusion among DEQ, CUC and Region 9 staff about how agreement payments were to be made and whether the reimbursement method of payment was required.

Federal Requirements for Grant Payment Methods

Advance Method

The EPA's Assistance Agreement Almanac defines an advance as a payment to a recipient upon its request before outlays are made by the recipient. Federal regulations at 40 CFR § 31.21(c) and (d) stipulate that recipients and subgrantees should be paid in advance, provided they maintain the willingness and ability to maintain procedures to minimize the time elapsing between transfer of funds and distribution by the grant recipient or subgrantee. Section 5 of the EPA's General Terms and Conditions Applicable to EPA Assistance Agreement Recipients as of January 13, 2014, stipulates that the recipient agrees to draw cash only as needed for its disbursement. Failure on the part of the recipient to comply with this condition may cause the undisbursed portions of the assistance agreement to be revoked or financing method changed to a reimbursable basis. Section 5 applies to three of the four CCAs reviewed, and there was no similar condition prior to 2014.

Reimbursement Method

The reimbursement payment method is often associated with the high-risk designation, but this is not always the case. According to Section 4.5.2 of the EPA Assistance Agreement Almanac, there are instances where it may be in the agency's interest to place a recipient under the reimbursement payment method. Under 40 CFR § 31.21(c) and (d), the Award Official can require a recipient to be paid on a reimbursement basis if the recipient does not have adequate procedures in place to minimize the time elapsing between the transfer of funds from the EPA to the recipient and disbursement by the recipient to pay for costs. This would require placing a grant condition to that effect on the award. Some grant programs

with construction awards commonly place recipients on the reimbursement method. Under the reimbursement method, the federal agency may require the grantee to submit supporting documentation for requests for reimbursement to the project officer for review and approval prior to payment.

Special Award Conditions in the EPA Consolidated Agreements

Federal regulations at 40 CFR § 31.12 (a) permit additional requirements (special award conditions) in awards if an applicant or recipient has a history of poor performance, is not financially stable, has a management system that does not meet the standards prescribed in Part 31, has not conformed to the terms and conditions of a previous award, or is not otherwise responsible. One of the special award conditions may include payment on a reimbursement basis. Section 4.5.1 of the EPA Assistance Agreement Almanac stipulates that special award conditions may include requiring the EPA's prior approval for costs and activities that would not otherwise require such approval or converting a recipient to a reimbursement payment method from an advance payment method or using reimbursement payment at the outset.

High-Risk Designation

The EPA Assistance Agreement Almanac, Section 4.5.1, stipulates that recipients can be designated as high risk when administrative, programmatic capability, or performance issues are not significant enough to warrant an enforcement action, but EPA's financial and programmatic interests must still be protected. A high-risk designation increases EPA oversight of a recipient for identified areas of financial or programmatic weakness or risk. If a recipient is designated high risk and the reimbursement payment method is imposed, formal implementation would be required with the Las Vegas Finance Center.

Inconsistent Terms, Conditions and EPA Project Officer Reviews

There were inconsistent administrative and programmatic payment requirements in the agreements awarded to DEQ and CUC. Per 40 CFR § 31.3:

Administrative requirements mean those matters common to grants in general, such as financial management, kinds and frequency of reports, and retention of records. These are distinguished from programmatic requirements, which concern matters that can be treated only on a program-by-program or grant-by-grant basis, such as kinds of activities that can be supported by grants under a particular program.

As shown in Table 4, the administrative conditions in all four agreements to DEQ and CUC provided for the advance payment method, which allows the recipient to request payment of grant funds before outlays are made. However, programmatic

conditions in all four awards provided for some form of the reimbursement payment method, which requires the recipient to submit a payment request along with supporting documentation for project officer approval prior to payment. Our review also found that the EPA project officer did not perform the same level of review of the reimbursement requests.

Table 4: Payment methods and approval for CNMI agreements

Recipient	Agreement	Agreement administrative condition payment method	Programmatic conditions – approval requirements	Actual payment method used by recipient
DEQ	M00915609	Advance	Prior approval by the project officer required for certain travel, contracts, equipment and procurement	Advance
DEQ	M00915614	Advance	Prior approval by the project officer required for certain categories of travel and contracts	Advance
CUC	M00T33711	Advance	Project officer approval of reimbursement request only	Reimbursement – Payroll Advance – All other costs
CUC	M00T33715	Advance	Project officer approval of reimbursement request and supporting documentation	Reimbursement – Payroll Advance – All other costs

Source: CCAs, interviews with DEQ and CUC staff, and OIG analysis

Awards to DEQ

Two DEQ awards—CCA M00915609 for over \$11 million and CCA M00915614 for almost \$6 million—contain programmatic conditions requiring prior EPA project officer review and approval of some payment requests. However, despite the majority of the CCA funding being for personnel costs, the programmatic conditions in the agreements limit the EPA project officer to review and approval of reimbursement requests to non-payroll items such as off-island travel costs, contracts, equipment and sole source procurements (reimbursement terms). For both agreements, there is no requirement for the EPA project officer to review and approve personnel costs prior to payment. DEQ’s actual draw practice uses the advance method for all costs, where they incur the cost, request funds from Region 9, and pay the bill upon receipt.

Awards to CUC

CCA M00T33711 to CUC, for over \$36 million, included a programmatic condition for the EPA project officer to perform prior approval of reimbursement requests. However, there was no requirement for provision of supporting documentation. As the majority of costs are related to construction of water and wastewater infrastructure projects, involving millions of dollars, it is the OIG’s opinion that the supporting documentation is necessary for a detailed review.

CCA M00T33715 to CUC, for over \$4 million, included a programmatic condition requiring approval of payment reimbursement requests by the EPA project officer for projects costs only. However, there was a requirement for sufficient documentation to support costs being requested.

For both CCAs M00T33715 and M00T33711, CUC's actual draw practice for construction cost is the advance method, where it incurs the cost, requests funds from Region 9, and then pays the bill. For payroll, it uses the reimbursement method, where it incurs the cost, makes payment, and then requests reimbursement from Region 9 twice a year.

Inconsistent EPA Oversight on Payments

Our review also found that the Region 9 project officers did not perform the same level of review of reimbursement requests. The EPA project officer responsible for DEQ only reviewed a one-page payment request. Although the majority of the award is for personnel costs, the same EPA project officer told us he does not look at labor costs in the draw requests. In contrast, the EPA project officer for the Guam Environmental Protection Agency performed a detailed review of payment requests. In addition, the EPA project officer responsible for CUC reviewed supporting documentation for all payment requests. While there is no requirement for review of supporting documentation for the DEQ awards, we believe it would be an excellent practice.

Confusion Regarding Payment Method Required

There was confusion among DEQ, CUC and Region 9 about the CCA payment requirements. This arose due to conflicting language in the CCAs regarding the required payment method. All four awards contained administrative conditions providing for the as soon as possible/advance payment method, yet they also contained programmatic conditions requiring EPA project officer review and approval of certain costs.

DEQ staff stated that their reimbursement requests for all costs use the advance payment method. However, the EPA project officer for DEQ CCAs said it is on the reimbursement payment method. He does not perform a detailed review of reimbursement requests, and receives only one page of supporting documentation with limited information to review.

CUC staff stated the advance method is used for construction costs and the reimbursement method for payroll. Further, the EPA project officer for CUC CCAs said he handles reimbursement requests as if they are under the reimbursement payment method, and does a detail review before approving payment. He also said all the Pacific Territory CCAs use the reimbursement method.

Historical Problems in CNMI

In March 2009, a District Court judge in the CNMI entered two stipulated orders requiring that CUC maintain compliance with the Clean Water Act/Safe Drinking Water Act. In addition, on July 30, 2014, based on findings in the 2013 CNMI Single Audit, the OIG recommended that DEQ be placed on a high-risk designation. Despite continued challenges at both DEQ and CUC, Region 9 has not designated either agency as “high risk.” A high-risk designation may require CCA payments to be on the reimbursement payment method. As part of the reimbursement payment method, a federal agency may require prior review and approval of source documentation by the project officer before payment can be made. Because this extra measure of control was never completely implemented, the \$58,329,416 in agreement funds awarded to DEQ and CUC are at risk of fraud, waste and abuse. Also, the issues noted call into question whether the funds meet the intended purpose of protecting human health and the environment.

Recommendations

We recommend that the Regional Administrator, Region 9:

4. Review the CCAs to DEQ and CUC to determine the appropriate method of payment and update the CCAs accordingly.
5. Determine whether DEQ or CUC should be designated “high risk” and, if so, require formal implementation of the reimbursement payment method with the Las Vegas Finance Center.

Agency Response and OIG Evaluation

Region 9 concurred with Recommendation 4 and concurred with modification on Recommendation 5.

For Recommendation 4, Region 9 stated that:

EPA Region 9 concurs with the recommendation and, to ensure adequate internal control and oversight, has determined the appropriate method of payment for DEQ and CUC will continue to be the advance method with special award conditions.... The Infrastructure Section and Pacific Islands Office will work with the Grants Management Office to ensure implementation of this recommendation with the award of the current year’s CCAs by 09/30/2016. As recommended by the OIG, the Region will draft a note to the CCA files summarizing the method and ensure the grantee’s CFO is properly instructed of the method and processing.

Region 9 provided a planned completion date of September 30, 2016, for Recommendation 4. The OIG concurs with the agency's proposed actions. When implemented, the corrective actions should satisfy the intent of Recommendation 4. This recommendation will remain open pending completion of the proposed corrective action.

For Recommendation 5, Region 9 stated that:

At this time the comprehensive suite of programmatic grant conditions included in the DEQ and CUC CCAs provides adequate controls and oversight on the grantee. In addition, DEQ has implemented new time sheet procedures as a result of a finding from the FY2014 CNMI Single Audit. These time sheets comply with 2 CFR Part 225, Appendix B, Section 8h. Also, operating the environmental and water infrastructure programs on a reimbursement basis would unnecessarily reduce overall performance and effectiveness of federal grant funding. Therefore, the Region does not intend to designate CUC or DEQ as "high risk" at this time, but will continue to monitor their performance closely.

The OIG believes the agency's completed corrective actions satisfy the intent of Recommendation 5. This recommendation will be considered closed upon issuance of the report. We will use the date of Region 9's response (May 4, 2016) as the completion date.

Region 9's complete response to the draft report is in Appendix B.

Chapter 4

DEQ Had Inconsistencies in Reporting In-Kind and Interagency Agreement Costs

Our review identified inconsistencies in reporting on in-kind and interagency agreement (IA) costs by DEQ in the Federal Financial Reports (FFRs). Federal regulations and the Region 9 CCAs require accurate reporting of outlays in the FFRs. However, Region 9 did not provide adequate instructions to DEQ on reporting requirements for in-kind and IA costs. Specifically, Region 9 did not provide DEQ with procedures on how to obtain EPA-expended in-kind and IA cost data from the Cincinnati Financial Center. As a result, over \$1.8 million of in-kind and IA costs may have been misreported by DEQ.

Definitions of In-Kind and IA Costs

The EPA's Assistance Agreement Almanac Glossary defines "in-kind assistance" as the services or products of an EPA contractor or another federal agency under an IA that the agency provides to a recipient as a form of financial assistance as provided for in the Federal Grant and Cooperative Agreement Act and EPA Order 5700.1. The estimated cost for the in-kind assistance is included in the EPA approved budget for the agreement with the recipient.

The EPA Assistance Agreement Almanac Glossary defines "interagency agreement" as a written agreement between federal agencies under which goods and services are provided in exchange for funds, or in which federal agencies are authorized by statute to cooperate on a joint project that may involve providing funds for an assistance agreement.

Federal Regulations and Region 9 CCAs Require Accurate Reporting

Federal regulations at 40 CFR §31.41(b)(3) require grantees to submit FFR's for both construction and non-construction awards at least annually. It directs each grant recipient to report program outlays and program income. Federal regulations at 40 CFR § 31.3 define outlays as including the value of in-kind contributions. In addition, each Region 9 CCA includes an administrative condition for submission of interim financial reports, which requires a certification stating:

by signing this report, I certify that it is true, complete, and accurate to the best of my knowledge. I am aware that any false, fictitious, or fraudulent information may subject me to criminal, civil, or administrative penalties.

Inconsistencies in Reporting on In-Kind and IA Costs

We identified inconsistencies in reporting in-kind and IA costs by DEQ on the federal FFRs. For both awards to DEQ—CCA M00915609 and M00915614—DEQ reported budgeted amounts on the FFRs. This is contrary to the requirement to report actual amounts. In contrast, CUC reported actual amounts in the FFRs for CCA M00T33711.

Two of the CCAs awarded to DEQ included provisions for Region 9 to expend a portion of the agreement award amount for in-kind and IA assistance totaling over \$1.8 million. These funds are expended by Region 9 out of the recipient’s CCA funding for on-site technical assistance through inter-personnel agreements and the EPA IAs. The recipient has no control or authority over the use of these funds nor consistent access to the amount of in-kind and IA costs expended.

Region 9 Did Not Provide Adequate Direction to Grant Recipients on Reporting Requirements

The Region 9 CCAs to DEQ did not provide adequate direction to recipients on reporting requirements for in-kind and IA costs. Both of the CCAs reviewed include in-kind costs, as shown in Table 5.

Table 5: CNMI CCA in-kind costs

Recipient	CCA	Total CCA amount	In-kind			Recipient’s FFR reporting method
			Inter-personnel agreement	IA	Total	
DEQ	M00915609	\$11,437,521	\$868,226	\$279,000 <i>Note 1</i>	\$1,147,226	Reports budgeted instead of actual in-kind and IA amounts.
DEQ	M00915614	5,978,491	485,000	170,000 <i>Note 1</i>	655,000	Reports budgeted instead of actual in-kind and IA amounts
Total		\$17,716,012	\$1,353,226	\$449,000	\$1,802,226	

Note 1: The CCAs do not include IA costs as in-kind costs

Source: EPA CCAs and FFRs prepared by CUC and DEQ.

For CCAs M00915609 and M00915614 awarded to DEQ, there were no administrative conditions addressing in-kind or IA cost reporting requirements. In contrast, CCA M00T33711 awarded to CUC included an administrative condition that stated “the recipient shall identify actual EPA in-kind and/or IAG expenditures on the FFR under Section 12 remarks.” As a result, for the two CCAs awarded to DEQ, the EPA provided no instructions directing the recipient how to report data for in-kind and IA costs.

Over \$1.8 Million of In-Kind and IA Costs May Have Been Misreported

Region 9 did not provide adequate direction to DEQ on reporting requirements for in-kind and IA costs. As a result, over \$1.8 million in Region 9 in-kind and IA costs may have been misreported by DEQ. DEQ cannot make accurate and informed certification on the FFRs on how all of their CCA funds were expended without expended amounts for in-kind assistance. DEQ is responsible for tracking all expenditures on its CCAs, but does not always have information on how Region 9 expended its CCA funds for in-kind and IA assistance.

Recommendations

We recommend that the Regional Administrator, Region 9:

6. Provide DEQ guidance and instruction on how to obtain expended in-kind and IA cost data from the EPA Cincinnati Finance Center and report actual in-kind and IA costs on the FFR.
7. Verify that reporting of in-kind and IA cost funding in the Region 9 CCAs is consistent.

Agency Response and OIG Evaluation

Region 9 concurred with Recommendations 6 and 7.

For Recommendation 6, Region 9 stated that:

The (Region 9) Grants Management Office will work with the project officers for these CCAs in the Infrastructure Section and Pacific Islands Office to ensure DEQ and CUC are provided guidance and instruction on obtaining and recording actual expended in-kind and IA cost data. This effort will be completed in conjunction with the award of the FY16 CCAs by 09/30/2016.

Region 9 provided a planned completion date of September 30, 2016. The OIG concurs with the agency's proposed actions. When implemented, the corrective actions should satisfy the intent of Recommendation 6. This recommendation will remain open pending completion of the proposed corrective action.

For Recommendation 7, Region 9 stated that:

The (Region 9) Grants Management Office, Infrastructure Section, and Pacific Islands Office will ensure and verify consistent treatment of in-kind and IA funding in the CCAs beginning with this year's FY16 awards by 09/30/2016.

Region 9 provided a milestone date of September 30, 2016. The OIG concurs with the agency's proposed actions. When implemented, the corrective actions should satisfy the intent of Recommendation 7. This recommendation will remain open pending completion of the proposed corrective action.

Region 9's complete response to the draft report is in Appendix B.

Chapter 5

Region 9 Project Files Were Not Readily Available to Third Parties

Region 9 CNMI CCA project files were not readily accessible by others (third parties). The EPA Records Management Policy (CIO 2155.3) requires agency offices to maintain electronic records in an approved electronic records management system that allows access by staff who have a need to know the information for appropriate business reasons. The project officers did not follow EPA records management policies, and there is no assurance that relevant documents and other information are properly stored and easily accessible. We were only able to obtain information piecemeal, making it difficult to determine the adequacy of project officer performance. As a result, it was difficult to assure that Region 9 was effectively monitoring the \$58 million awarded to CNMI.

Requirements for Project Officer Files

The EPA Records Management Policy (CIO 2155.3) states that each office within the EPA is required to establish and maintain a records management program with the following minimum requirements:

- Create, receive and maintain records providing adequate and proper documentation and evidence of the EPA's activities.
- Manage records, in any format.
- Maintain electronic records in an approved electronic records system.
- Ensure non-electronic records are managed appropriately in paper-based official recordkeeping systems that facilitate preservation, retrieval, use and disposition if they are not appropriate for scanning (or digitization).
- Maintain records so they can be accessed by staff who needs to know information for appropriate business reasons.

Section 1.3 of the EPA's Assistance Agreement Almanac states that project officers must keep files for each of their executed grants. The file should include both official records and non-official copies of specified administrative records, such as the grant award document and amendments. Some administrative and programmatic records—such as applications, emails, electronic correspondence, funding recommendations, awards, administrative and programmatic monitoring reports, FFRs, and vouchers—are maintained in electronic systems like the Integrated Grants Management System and Compass. These electronic systems do not currently meet the requirements for an electronic recordkeeping system, so any records must be printed out and captured in a paper recordkeeping system or an approved electronic system.

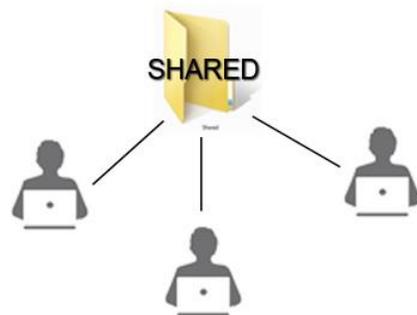
The EPA's Records Management Manual, February 2007, states that an office may choose to maintain specific types of records in a central location while maintaining other types of records at individual work stations. Records maintained at individual work stations are required to be identified in the recordkeeping system so that everyone in the office can locate the records. Computer drives, backup tapes, and software applications such as Lotus Notes are not recognized as recordkeeping systems. However, in the absence of an electronic recordkeeping system, offices may establish network directories using the agencywide file structure to facilitate access and retrieval of the electronic copy while maintaining the record copy in a paper recordkeeping system.

Region 9 Project Officer Files Were Not Readily Accessible or Retrievable

The project officer files for the CNMI CCAs were maintained on their computer desktops and were not readily accessible by others. Region 9 staff did not comply with records management policies.

During the course of the audit, the OIG requested the CCA project officer files. Official hardcopy project officer files are no longer maintained. Instead, the project officers store data electronically in multiple ways. At this time, there is no central database for project officer files allowing for access for independent third review. The Region 9 project officers provided data to the OIG upon request. However, the issue remains that project files are unavailable for an independent third party review.

CNMI DEQ project files are all electronic and maintained on the project officer's computer hard drive, not on a share drive. The project officer said that only he has immediate access to his computer and it would be difficult for others to review his files. The project officer was not aware of any file system other than the Integrated Grants Management System, yet most of his material was not in that system. The project officer was not aware of any paperless initiative in EPA Region 9. The project officer stated that he kept his project files on his computer desktop for convenience, and he thought the share drives have only been used within the last year.



Graphic illustrating the shared drive concept referred to by the project officer. (EPA OIG image)

The CUC project files are disorganized, but generally maintained in multiple electronic folders on the project officer's hard drive. The project officer said he had a folder for each drinking water and waste water project. He plans to move material to the share drive at some point in the future. The project officer was not

aware of an electronic records system requirement. The project officer stated that files kept on his computer desktop were for quick and easy use.

While the Region 9 project officers have been using the electronic format, they have not ensured that relevant documents and other information is stored in an organized and reviewable location that is easily accessible.

Limited Access to Files Makes It Difficult to Assess Project Officer Performance

The OIG obtained only limited access to the project files for DEQ and CUC. The project officer files were not readily available for OIG review. We were only able to obtain information piecemeal, making it difficult to determine the adequacy of project officer performance. As a result, it was difficult to assure that Region 9 was effectively monitoring the \$58 million in CCAs.

Recommendation

We recommend that the Regional Administrator, Region 9:

8. Require Region 9 project officers to implement EPA Records Management Manual policies concerning electronic project officer files.

Agency Response and OIG Evaluation

Region 9 concurred with Recommendation 8 and stated that:

EPA program offices have begun exploring a Sharepoint or similar tool where all award-related documents can be stored and easily shared among the various offices involved. In addition to the Sharepoint site, a standard operating procedure meeting EPA records management protocols will be developed by the end of FY16 to ensure consistent records management procedures across the 11+ programs involved in the consolidated cooperative agreements, to be coordinated by the project officers.

Additionally, in August 2015, EPA's national Grants Management Council agreed to develop a timetable with milestones and to identify and allocate resources for adopting electronic records management for all 10 EPA Regional Offices. As a result, the Office of Grants and Debarment, in collaboration with OEI, formed a national work group to identify and evaluate options from a "One EPA" perspective for an agency-wide electronic grants records system. This system would include all aspects of the grant file (programmatic, administrative and financial). Action on this topic is expected by 09/30/2016.

Region 9 provided a planned completion date of September 30, 2016. The OIG concurs with the agency's proposed actions. When implemented, the corrective actions should satisfy the intent of Recommendation 8. This recommendation will remain open pending completion of the proposed corrective action.

Region 9's complete response to the draft report is in Appendix B.

Status of Recommendations and Potential Monetary Benefits

RECOMMENDATIONS						POTENTIAL MONETARY BENEFITS (in \$000s)	
Rec. No.	Page No.	Subject	Status ¹	Action Official	Planned Completion Date	Claimed Amount	Agreed-To Amount
1	11	Disallow and recover the \$1,082,982 in DEQ unsupported labor costs unless DEQ provides support that complies with 2 CFR Part 225, Appendix B, Section 8.h, requirements and CCA terms.	O	Regional Administrator, Region 9	9/30/17	\$1,083	
2	11	Disallow and recover the \$402,197 in CUC unsupported labor costs unless CUC provides support that complies with 2 CFR Part 225, Appendix B, Section 8.h, requirements and CCA terms.	O	Regional Administrator, Region 9	9/30/17	\$402	
3	11	For future EPA agreements, verify that DEQ and CUC labor-charging cost practices comply with federal requirements under 2 CFR Part 225 and CCA terms.	C	Regional Administrator, Region 9	5/4/16		
4	17	Review the CCAs to DEQ and CUC to determine the appropriate method of payment and update the CCAs accordingly.	O	Regional Administrator, Region 9	9/30/16		
5	17	Determine whether DEQ or CUC should be designated "high risk" and, if so, require formal implementation of the reimbursement payment method with the Las Vegas Finance Center.	C	Regional Administrator, Region 9	5/4/16		
6	21	Provide DEQ guidance and instruction on how to obtain expended in-kind and IA cost data from the EPA Cincinnati Finance Center and report actual in-kind and IA costs on the FFR.	O	Regional Administrator, Region 9	9/30/16		
7	21	Verify that reporting of in-kind and IA cost funding in the Region 9 CCAs is consistent.	O	Regional Administrator, Region 9	9/30/16		
8	25	Require Region 9 project officers to implement EPA Records Management Manual policies concerning electronic project officer files.	O	Regional Administrator, Region 9	9/30/16		

¹ O = Recommendation is open with agreed-to corrective actions pending.
 C = Recommendation is closed with all agreed-to actions completed.
 U = Recommendation is unresolved with resolution efforts in progress.

Grants Awarded to CUC by Federal Agency

No.	Year	Agency	Grant	Amount	Category	Project title
1	2009	DOI-OIA	CNMI W/WW 2009	\$380,000	Water/Wastewater	Engineering & Management Services
2	2009	DOI-OIA	CNMI-CIP-2009	1,968,812	Water/Wastewater	Sadog Tasi & Agingan WWTP Rehab
3	2010	DOI-OIA	CNMI W/WW 2010	798,948	Water/Wastewater	CUC Water/Wastewater Master Plan
4	2010	DOI-OIA	CNMI-CIP-2010	1,000,000	Water/Wastewater	Sadog Tasi WWTP Rehab
5	2011	DOI-OIA	TA-CNMI-2011	1,041,000	Water/Wastewater	IT System Upgrade
6	2011	DOI-OIA	CNMI-CIP-2011	1,260,000	Water/Wastewater	Geothermal Energy
7	2011	DOI-OIA	CNMI-EIC-2011	500,000	Water/Wastewater	Geothermal Resource & Geophysical Assessment
8	2011	DOI-OIA	CNMI W/WW 2011	265,000	Water/Wastewater	Professional Services
9	2013	DOI-OIA	CNMI-EIC-2013	1,122,000	Water/Wastewater	Integrated Resource Plan, Prepaid Meters
10	2013	DOI-BOR	R13AP80017-0001-M	294,967	Water/Wastewater	Water Loss Reduction and Energy Saving
11	2010	DOI-OIA	CNMI-CIP-2010	1,374,375	Power Improvements	CUC Power Generation Improvements
12	2011	DOI-OIA	CNMI-CIP-2011	1,625,625	Power Improvements	CUC Power Generation Improvements
13	2012	DOI-OIA	CNMI-CIP-2012	1,247,116	Power Improvements	Rehab of Critical Power Generation & Distribution System
14	2010	DOI-OIA	CNMI-CIP-2010	3,568,830	Rota Power Improvements	Rota Power Generation Improvements
15	2010	DOI-OIA	CNMI-CIP-2010	4,050,000	S02 Project	Stipulated Order 2 Project
16	2011	DOI-OIA	CNMI-CIP-2011	2,154,000	Petroleum Pipeline	Replacement of Lower Base Pipeline
17	2012	DOI-OIA	CNMI-CIP-2012	232,000	Petroleum Pipeline	Tank Integrity
18	2012	DOI-OIA	CNMI-CIP-2012	800,000	Petroleum Pipeline	Replacement of Lower Base PR Pipeline
19	2013	DOI-OIA	CNMI-CIP-2013	350,000	Petroleum Pipeline	New Fuel Tank at Power Plant 1
20	2013	DOI-OIA	CNMI-CIP-2013	1,025,000	Petroleum Pipeline	Replace CUC's Existing Oil Pipeline
21	2013	DOI-OIA	CNMI-CIP-2013	725,000	Petroleum Pipeline	Replace CUC's Existing Oil Pipeline
22	2014	DOI-OIA	CNMI-CIP-2014	733,253	Petroleum Pipeline	Replace CUC's Existing Oil Pipeline
23	2014	EDA	07-79-07008	200,000	Sewer System	Design of Lower Base Sewer System
24	2014	EDA	07-01-07128	1,579,292	Sewer System	Sewer System Improvements
25	2010	EPA	M00T33711-9	36,713,414	Water/Wastewater	Consolidated Environmental Program
26	2014	EPA	M00T33715-0	4,200,000	Water/Wastewater	Consolidated Environmental Program
Total Grant Funding to CUC				\$69,208,632		
DOI-OIA: Department of the Interior, Office of Insular Affairs DOI-BOR: Department of the Interior, Bureau of Reclamation EDA: Economic Development Administration, under the Department of Commerce						

Source: CUC data provided to EPA OIG.

Agency Response to Draft Report



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
REGION IX
75 Hawthorne Street
San Francisco, CA 94105
MAY 04 2016

MEMORANDUM

SUBJECT: EPA Region 9 Written Response to the Findings and Recommendations of Draft Report: EPA Region 9 Needs to Improve Oversight over CNMI's Consolidated Cooperative Agreements
Project No. OA-FY14-0035

FROM:  Serena A. McIlwain
Assistant Regional Administrator
EPA Region 9

TO: Kevin Christensen
Assistant Inspector General for Audit
Office of Inspector General

EPA Region 9 has reviewed the subject draft report. We appreciate the opportunity to provide comments on the report and look forward to our continuing collaboration with the OIG to enhance EPA management of CNMI's environmental and construction grant programs.

In summary, EPA Region 9 either concurs, or concurs with modification, with each of the OIG's recommendations in the discussion draft report, and has begun to implement many of them.

Our comments on the recommendations and findings are attached.

If you have any questions regarding this response, please contact Mike Montgomery, Assistant Director, Water Division, at (415) 947-3537 or Bridget Coyle, Assistant Director, Land Division, at (415) 947-4286, or Craig Wills, Grants Management Officer, at (415) 972-3663. In regards to the coordination of the audit, please contact Magdalen Mak, Audit Follow-up Coordinator, EMD-4-1, at (415) 972-3773.

Attachment

cc: Michael D. Davis, Director, OIG
Heather Layne, Project Manager, OIG
Jennifer Hutkoff, Auditor, OIG
Jan Lister, Auditor, OIG

EPA Region 9's Comments on the OIG's Draft Report:
EPA Region 9 Needs to Improve Oversight Over CNMI's
Consolidated Cooperative Agreements

OIG Recommendations

1. Disallow and recover up to \$14, 712,514 in DEQ unsupported labor and indirect costs unless DEQ provides support that complies with 2 CFR Part 225, Appendix B, Section 8.h requirements and CCA terms.

Responsible: Grants Management Office (EMD) + Pacific Islands Office (LND)

Concurrence: Region 9 concurs with modification.

Status: The audit recommended disallowing up to the entire grant award amount for FY 2009-2014 of \$14,712,514 for the consolidated grants for DEQ. However the underlying finding is related more specifically to documenting labor costs from multiple sources and indirect costs.

The audit states: “The questioned costs will be reduced based on the recipients providing detailed cost information.” Accordingly, EPA recommends that the questioned costs be limited to the payroll costs for split-funded employees. Out of approximately 45 employees only 14 were split funded. DEQ has provided additional documentation to support employees who work solely on the consolidated grants.

Based on that, Region 9 is proposing to limit the recommended disallowed labor costs to up to \$1,082,982, the budget amounts set aside in the workplans for split-funded employees.

Region 9 has requested additional documentation from DEQ to determine compliance with 2 CFR Part 225, Appendix B, and will review the documentation and make a final determination of questioned costs by September 30, 2017.

In addition, the audit states that DEQ charged an unallowable overhead rate of 14 percent to the CCAs, contrary to the CCA terms. However, based on documentation and confirmation provided by DEQ, it does not appear that DEQ is charging 14% for indirect costs. Therefore, EPA will not pursue recovery of indirect costs.

2. Disallow and recover up to \$823,963 in CUC unsupported labor and indirect costs unless CUC provides support that complies with 2 CFR Part 225, Appendix B, Section 8. h requirements and CCA terms.

Responsible: Grants Management Office (EMD) +Infrastructure Section (WTR)

Concurrence: Region 9 concurs with modification.

Status: Region 9 has reviewed selected invoices from the period in question, and has concluded that CUC did not charge EPA grants for indirect costs. Although CUC appears to have set aside 3% of their budget under the category of indirect costs, it was only done for accounting purposes to create an Administrative Budget Category. CUC did not

charge EPA for any indirect costs in their invoices; only direct, itemized costs were included. Therefore, Region 9 requests that the OIG narrow the recommendation to address only unsupported labor costs.

Region 9 has asked the CUC to provide supporting documentation for past administrative staff labor costs charged to EPA grant(s) from 10/1/2010 through 9/30/2014. Region 9 will work with cue to clarify the request and help identify the types of information that would be appropriate to support the invoices.

Region 9 will review the supporting documentation and make a decision by September 30, 2017, as to how much, if any, funding does not comply with 2 CFR Part 225, Appendix B, Section 8.h requirements and should be disallowed and recovered.

3. For future EPA agreements, verify that DEQ and CUC labor-charging and indirect cost practices comply with federal requirements under 2 CFR Part 225 and CCA terms.

Responsible: Grants Management Office (EMD) + Infrastructure Section (WTR) + Pacific Islands Office (LND)

Concurrence: Region 9 concurs with recommendation.

Status: Region 9 POs will review future payment requests to ensure all labor-charges comply with federal requirements per 2 CFR Part 225 and CCA terms. Region 9 POs for CUC will review all payment requests and supporting documentation to ensure there are no indirect costs being requested.

4. Review the CCAs to DEQ and CUC to determine the appropriate method of payment, and update the CCAs accordingly.

Responsible: Grants Management Office (EMO) + Infrastructure Section (WTR) + Pacific Islands Office (LND)

Concurrence: EPA Region 9 concurs with the recommendation and, to ensure adequate internal control and oversight, has determined the appropriate method of payment for DEQ and CUC will continue to be the advance method with special award conditions.

Status: The Infrastructure Section and Pacific Islands Office will work with the Grants Management Office to ensure implementation of this recommendation with the award of the current year's CCAs by 09/30/2016. As recommended by the OIG, the Region will draft a note to the CCA files summarizing the method and ensure the grantee's CFO is properly instructed of the method and processing.

5. Determine whether DEQ or CUC should be designated "high risk" and, if so, require formal implementation of the reimbursement payment method with the Las Vegas Finance Center.

Responsible: Grants Management Office (EMD) + Infrastructure Section (WTR) + Pacific Islands Office (LND)

Concurrence: EPA Region 9 concurs with modification.

Status: At this time the comprehensive suite of programmatic grant conditions included in

the DEQ and CUC CCAs provides adequate controls and oversight on the grantee. In addition, DEQ has implemented new time sheet procedures as a result of a finding from the FY2014 CNMI Single Audit. These time sheets comply with 2 CFR Part 225, Appendix B, Section 8h.

Also, operating the environmental and water infrastructure programs on a reimbursement basis would unnecessarily reduce overall performance and effectiveness of federal grant funding.

Therefore, the Region does not intend to designate CUC or DEQ as "high risk" at this time, but will continue to monitor their performance closely.

6. Provide DEQ guidance and instruction on how to obtain expended in-kind and IA cost data from the EPA Cincinnati Finance Center and report actual in-kind and IA costs on the FFR.

Responsible: Grants Management Office (EMD) + Infrastructure Section (WTR) + Pacific Islands Office (LND)

Concurrence: EPA Region 9 concurs with this recommendation.

Status: Grants Management Office will work with the project officers for these CCAs in the Infrastructure Section and Pacific Islands Office to ensure DEQ and CUC are provided guidance and instruction on obtaining and recording actual expended in-kind and IA cost data. This effort will be completed in conjunction with the award of the FYI 6 CCAs by 09/30/2016.

7. Verify that reporting of in-kind and IA cost funding in the Region 9 CCAs is consistent.

Responsible: Grants Management Office (EMD) + Infrastructure Section (WTR) + Pacific Islands Office (LND)

Concurrence: EPA Region 9 concurs with this recommendation.

Status: Grants Management Office, Infrastructure Section, and Pacific Islands Office will ensure and verify consistent treatment of in-kind and IA funding in the CCAs beginning with this year's FY16 awards by 09/30/2016.

8. Require Region 9 project officers to implement EPA Records Management Manual policies concerning electronic project officer files.

Responsible: Grants Management Office (EMD) + Pacific Islands Office (LND) + Infrastructure Section (WTR)

Concurrence: EPA Region 9 concurs with this recommendation.

Status: EPA program offices have begun exploring a Sharepoint or similar tool where all award-related documents can be stored and easily shared among the various offices involved. In addition to the Sharepoint site, a standard operating procedure meeting EPA records management protocols will be developed by the end of FYI 6 to ensure consistent

records management procedures across the 11+ programs involved in the consolidated cooperative agreements, to be coordinated by the project officers.

Additionally, in August 2015, EPA's national Grants Management Council agreed to develop a timetable with milestones and to identify and allocate resources for adopting electronic records management for all 10 EPA Regional Offices. As a result, the Office of Grants and Debarment, in collaboration with OEI, formed a national work group to identify and evaluate options from a "One EPA" perspective for an agency-wide electronic grants records system. This system would include all aspects of the grant file (programmatic, administrative and financial). Action on this topic is expected by 09/30/2016.

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