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AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL
AREA DE ARCHIVO DIGITAL

MUNICIPIO DE CIDRA
AUDITORIA 2002-2003
30 DE JUNIO DE 2003

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA
SINGLE AUDIT REPORT
YEAR ENDED JUNE 30, 2003

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF CIDRA

YEAR ENDED JUNE 30, 2003

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF CIDRA

YEAR ENDED JUNE 30, 2003

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López-Vega, CPA, PSC

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- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

**To the Honorable Mayor and
the Municipal Legislature
Municipality of Cidra
Cidra, Puerto Rico**

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Cidra, Puerto Rico**, as of and for the year ended June 30, 2003, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and the provisions of the Office of Management and Budget Circular A-133, "*Audits of States, Local Governments, and Non-Profit Organizations*". Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Cidra, Puerto Rico**, as of June 30, 2003, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1, the Municipality has implemented a new financial reporting model, as required by the provisions of Governmental Accounting Standards Board ("GASB") Statement No. 34, Basic Financial Statements-and Management's Discussion and Analysis-for States and Local Governments, and has adopted paragraphs six to eleven of GASB Statement No. 38, Certain Financial Statements Note Disclosures, as of June 30, 2003.

INDEPENDENT AUDITORS' REPORT (Continued)

The Management's Discussion and Analysis on pages 3 through 10 and the Budgetary Comparison Schedule-General Fund on page 35 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2003 on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

Our audit was performed for the purpose of forming an opinion on the basic financial statements of the **Municipality of Cidra**, taken as whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the respective financial statements. The information in that schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented, in all material respects, in relation to the basic financial statements taken as a whole.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 20, 2003

Stamp No. 1942284 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

MANAGEMENT AND DISCUSSION ANALYSIS

YEAR ENDED JUNE 30, 2003

Management's Discussion and Analysis

Management of the Municipality of Cidra (the "Municipality") implemented Statement No. 34 ("Statement") of the Governmental Accounting Standards Board ("GASB"), Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments for the fiscal year ended on June 30, 2003. This Management's Discussion and Analysis (MD&A) is prepared as a result of the requirements of such Statement, and it has been designed accordingly with the following goals:

- a) Assist the reader in focusing on significant financial issues,
- b) Provide an overview of the Municipality's financial activity,
- c) Identify changes in the Municipality's financial position (its ability to address the next and subsequent year challenges),
- d) Identify any material deviations from the financial plan (the approved budget,) and;
- e) Identify individual fund issues or concerns.

Since the MD&A is designed to focus on the current year activities, resulting changes and currently known facts, please read it in conjunction with the Municipality's financial statements.

FINANCIAL HIGHLIGHTS

- The Municipality net assets increased by \$ 5,566,748.
- In the fund financial statements, the governmental activities revenue increased \$ 655,986 (or 3%) while governmental activities expenditures increased \$ 4,690,251 (or 18%).
- The General Fund (the primary operating fund) reflected, on a current financial resource basis, a decrease of \$ 60,605.
- On a budgetary basis, actual revenues exceeded actual expenditures by \$ 511,098.
- The Municipality issued bonds amounting to \$ 1,915,000 to finance mainly capital improvements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

Using This Annual Report

This annual report consists of a series of new financial statements with a change in the focus from previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

Government-Wide Financial Statements

The Government-Wide Financial Statements are designed to provide users of the financial statements with a broad overview of the Municipality's finances in a manner similar to private-sector companies.

The Statement of Net Asset presents information on all of the Municipality's assets and liabilities, with the difference between both reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

The Statement of Activities presents information showing how the Municipality's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the Statement of Activities that will only result in cash flows in future fiscal periods. The Statement of Activities is focused on both the gross and net cost of various activities, which are provided by the government's general tax and other revenues. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

Fund Financial Statements

The Fund Financial Statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only one kind of fund which is the governmental fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government Wide Financial Statements. However, unlike the Government Wide Financial Statements, Government Fund Financial Statements, focus on near term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

Fund Financial Statements (Continued)

Because the focus of governmental funds is narrower than that of the government wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government wide financial statements. By doing so, users of the basic financial statements may better understand the long-term impact of the Municipality's near term financial decisions. Both of the Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Infrastructure Assets

Historically, a government's largest group of assets (infrastructure-roads, bridges, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in government financial statements. GASB 34 requires that these assets be valued and reported within the Governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the modified approach) which periodically (at least every third year), by category, measures and demonstrated its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statement users in evaluating a local government and its performance over time.

The Municipality commenced the reporting of infrastructure assets during the current year. Also, the Municipality elected to depreciate infrastructure assets instead of using the modified approach.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The Municipality's combined net assets (excess of assets over liabilities) totaled \$ 26,579,773 at the end of 2003, compared to \$ 21,013,025 at the end of the previous year.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets (Continued)

Condensed Statement of Net Assets
June 30, 2003

Current assets	\$ 11,457,371
Capital assets	33,534,162
Other assets	<u>7,866,537</u>
Total assets	<u>52,858,070</u>
Current liabilities	9,636,778
Noncurrent liabilities	<u>16,641,519</u>
Total liabilities	<u>26,278,297</u>
Invested in capital assets, net of related debt	21,539,162
Restricted	9,187,963
Unrestricted	<u>(4,147,352)</u>
Total net assets	<u>\$26,579,773</u>

Changes in Net Assets

The Municipality's net assets increased by \$ 5,566,748. Approximately 52 percent of the Municipality's total revenue came from taxes, while 31 percent resulted from grants and contributions, including federal aid. Charges for Services provided 1 percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for health and welfare services, general government, public works, and economic development. In future years, when prior-year information is available, a comparative analysis of government-wide data will be presented.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

Changes in Net Assets (Continued)

**Condensed Statement of Activities
June 30, 2003 –**

Program revenues:	
Charges for services	\$ 366,397
Operating grants and contributions	3,932,255
Capital grants and contributions	4,598,301
General revenues:	
Property taxes	5,134,675
Municipal license tax	9,156,730
Grants and contributions not restricted to specific programs	3,202,253
Interest and investment earnings	428,414
Miscellaneous	<u>696,760</u>
Total revenues	<u>27,515,785</u>
Expense:	
General government	9,222,957
Public safety	1,724,886
Public works	5,194,724
Culture and recreation	890,728
Health and welfare	3,638,461
Economic development	301,307
Other	339,218
Interest on long-term debt	<u>636,756</u>
Total expenses	<u>21,949,037</u>
Change in net assets	5,566,748
Net assets, beginning of year	<u>21,013,025</u>
Net assets, end of year	<u>\$26,579,773</u>

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

As noted earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance related legal requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

MANAGEMENT AND DISCUSSION ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Governmental Funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$9,687,130, a decrease of \$1,420,853 in comparison with the prior year. There are reservations of fund balance amounting to \$9,405,506. This is the fund balance that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior fiscal year (\$668,391), 2) to pay debt service (\$ 1,661,738), 3) to pay for capital projects (\$5,326,685) and 4) for other purposes (\$ 1,748,692).

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2003, the general fund has a fund balance of \$ 499,167.

The Financial Sector had a better financial performance in comparison to previous years accordingly paid additional Municipal License Taxes to the Municipality.

GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the Municipality Council revised the Municipality's budget in order to include increases in revenues that were identified during the course of the fiscal year based on current developments that positively affected the Municipality's finances. Increases in budgeted expenditures were also made since the law mandates a balanced budget.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2003, amounts to \$ 51,049,548, net of accumulated depreciation of \$ 17,515,386, leaving a net book value of \$ 33,534,162. This investment in capital assets includes land, buildings, improvements, equipment, infrastructure and construction in progress. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The total increase in the Municipality's investment in capital assets for the current fiscal year was about 15% in terms of net book value. Depreciation charges for the year totaled \$ 1,461,598.

The Municipality finances a significant portion of its construction activities through bond issuances. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2003, the Municipality has \$4,955,878 of unexpended proceeds from bond issuances that are committed to future construction activities.

Debt Administration

The Puerto Rico Legislature has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged. See "Limitations on Ability of Municipalities to Issue General Obligation Debt-The Municipal Bonds" for a general description of such limitations.

The applicable law also requires that in order for a Municipality to be able to issue additional general obligation bonds and notes such Municipality must have sufficient "payment capacity". Act No. 64 provides that a municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, will be sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general obligation municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal grant revenues may vary if new grants are available but the revenue also is very predictable.

Those factors were considered when preparing the Municipality's budget for the 2003-2004 fiscal years.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer.

Commonwealth of Puerto Rico
Municipality of Cidra
Statement of Net Assets
June 30, 2003

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 10,797,482
Cash with fiscal agent	7,866,537
Accounts receivable:	
Municipal license tax	4,436
Intergovernmental	622,739
Other	32,714
Capital assets	
Land, improvements, and construction in progress	17,711,534
Other capital assets, net of depreciation	15,822,628
Total capital assets	<u>33,534,162</u>
 Total assets	 <u>52,858,070</u>
 Liabilities	
Accounts payable and accrued liabilities	987,946
Due to other governmental entities	84,627
Deferred revenues:	
Municipal license tax	8,153,704
Federal grant revenues	392,719
Other	17,782
Noncurrent liabilities:	
Due within one year	1,089,732
Due in more than one year	15,551,787
 Total liabilities	 <u>26,278,297</u>
 Net Assets	
Invested in capital assets, net of related debt	21,539,162
Restricted for:	
Capital projects	5,348,256
Debt service	1,661,738
Special revenue, non-grant	1,628,145
Federal and state grant funds	549,824
Unrestricted (deficit)	<u>(4,147,352)</u>
 Total net assets	 <u>\$ 26,579,773</u>

Commonwealth of Puerto Rico
Municipality of Cidra
Statement of Activities
For the Year Ended June 30, 2003

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 9,222,957	\$ 53,726	\$ 984,754	\$ -	\$ (8,184,477)
Public safety	1,724,886	2,955	115,575		(1,606,356)
Public works	5,194,724		1,474,391	3,698,841	(21,492)
Health and welfare	3,638,461	291,829	1,275,763		(2,070,869)
Culture and recreation	890,728	17,887	81,772	674,595	(116,474)
Economic development	301,307			224,865	(76,442)
Interest on long-term debt	636,756				(636,756)
Other	339,218				(339,218)
Total governmental activities	\$ 21,949,037	\$ 366,397	\$ 3,932,255	\$ 4,598,301	\$ (13,052,084)
General revenues:					
Property taxes					5,134,675
Municipal license tax					9,156,730
Grants and contributions not restricted to specific programs					3,202,253
Interest and investment earnings					428,414
Miscellaneous					696,760
Total general revenues					18,618,832
Change in net assets					5,566,748
Net assets - beginning					21,013,025
Net assets - ending					\$ 26,579,773

**Commonwealth of Puerto Rico
Municipality of Cidra
Balance Sheet
Governmental Funds
June 30, 2003**

	<u>General Fund (01)</u>	<u>Special Revenue Fund (02)</u>	<u>Capital Projects Fund (20)</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets					
Cash and cash equivalents	\$ 8,375,597	\$ 1,541,262	\$ 659,202	\$ 221,421	\$ 10,797,482
Cash with fiscal agent		1,248,921	4,955,878	1,661,738	7,866,537
Accounts receivable:					
Municipal license tax	4,436				4,436
Intergovernmental	133,205	297,364		192,170	622,739
Other	32,714				32,714
Due from other funds	827,292			89,397	916,689
Total assets	<u>\$ 9,373,244</u>	<u>\$ 3,087,547</u>	<u>\$ 5,615,080</u>	<u>\$ 2,164,726</u>	<u>\$ 20,240,597</u>
Liabilities and Fund Balances					
Liabilities :					
Accounts payable and accrued liabilities	\$ 635,746	\$ 27,766	\$ 165,824	\$ 158,610	\$ 987,946
Due to other governmental entities	84,627				84,627
Due to other funds		720,842	101,000	94,847	916,689
Deferred revenues:					
Municipal license tax	8,153,704				8,153,704
Federal grant revenues		177,043		215,676	392,719
Other				17,782	17,782
Total liabilities	<u>8,874,077</u>	<u>925,651</u>	<u>266,824</u>	<u>486,915</u>	<u>10,553,467</u>
Fund balances:					
Reserved for:					
Encumbrances	217,543	413,204	21,571	16,073	668,391
Capital projects			5,326,685		5,326,685
Other purposes		1,748,692			1,748,692
Reserved reported in nonmajor funds:					
Debt service fund				1,661,738	1,661,738
Unreserved:					
Undesigned	281,624				281,624
Total fund balances	<u>499,167</u>	<u>2,161,896</u>	<u>5,348,256</u>	<u>1,677,811</u>	<u>9,687,130</u>
Total liabilities and fund balances	<u>\$ 9,373,244</u>	<u>\$ 3,087,547</u>	<u>\$ 5,615,080</u>	<u>\$ 2,164,726</u>	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	33,534,162
Long-term liabilities are not due and payable in the current period, and therefore, are not reported in the funds	<u>(16,641,519)</u>
Net assets of governmental activities	<u>\$ 26,579,773</u>

The notes to the financial statements are an integral part of this statement.

Commonwealth of Puerto Rico
Municipality of Cidra
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2003

	General Fund (01)	Special Revenue Fund (02)	Capital Projects Fund (20)	Other Governmental Funds	Total Governmental Funds
Revenues					
Property taxes	\$ 4,218,299	\$ -	\$ -	\$ 916,376	\$ 5,134,675
Municipal license taxes	9,156,730				9,156,730
Licenses, permits and other local taxes	597,398				597,398
Intergovernmental	3,202,253	850,795	101,000		4,154,048
Rent of property	17,887				17,887
Fines and forfeitures	2,955				2,955
Interest	428,414				428,414
Federal grants		383,060		2,645,032	3,028,092
Miscellaneous	428,483	60,363		9,440	498,286
Total revenues	\$ 18,052,419	\$ 1,294,218	\$ 101,000	\$ 3,570,848	\$ 23,018,485
Expenditures					
Current:					
General government	8,120,462	713,899		428,971	9,263,332
Public safety	1,498,362	139,074			1,637,436
Public works	5,002,750	906,242	1,994,341	1,110,024	9,013,357
Health and welfare	2,293,783	147,998		1,099,403	3,541,184
Culture and recreation	750,729				750,729
Economic development	171,674	100,652			272,326
Other		338,375	843		339,218
Debt service:					
Principal				900,000	900,000
Interest	77,664			559,092	636,756
Total expenditures	17,915,424	2,346,240	1,995,184	4,097,490	26,354,338
Excess (deficiency) of revenues over (under) expenditures	136,995	(1,052,022)	(1,894,184)	(526,642)	(3,335,853)
Other financing sources (uses)					
Transfers in		38,622	264,269		302,891
Transfers out	(197,600)	(105,291)			(302,891)
Long-term debt issued		1,915,000			1,915,000
Total other financing sources (uses)	(197,600)	1,848,331	264,269	-	1,915,000
Excess (deficiency) of revenues over expenditures and other financing sources (uses)	(60,605)	796,309	(1,629,915)	(526,642)	(1,420,853)
Fund balance, beginning	559,772	1,365,587	6,978,171	2,204,453	11,107,983
Fund balance, ending	\$ 499,167	\$ 2,161,896	\$ 5,348,256	\$ 1,677,811	\$ 9,687,130

The notes to the financial statements are an integral part of this statement.

Commonwealth of Puerto Rico
Municipality of Cidra
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2003

Net Change in Fund Balances - Total Governmental Funds	\$	(1,420,853)
<p>Amounts reported for governmental activities in the Statement of Activities are different because:</p>		
<p>Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period.</p>		3,427,540
<p>Depreciation expense on capital assets is reported in the Government-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds</p>		(1,461,598)
<p>Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in Governmental Funds.</p>		(205,932)
<p>Some revenues reported in the Statement of Activities do not provide current financial resources in Governmental Funds.</p>		4,497,301
<p>Change in landfill accrual</p>		1,745,290
<p>The issuance of long-term debt provides current financial resources to Governmental Funds, while the repayment of principal of long-term debt consumes current financial resources. This is the amount by which debt proceeds exceed debt service principal payments.</p>		(1,015,000)
Change in Net Assets of Governmental Activities	\$	<u>5,566,748</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Cidra (the Municipality) was founded on the year 1917. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a fourteen-member Municipal Legislature who are elected for four-year terms.

The Municipality provides public safety, public works, culture and recreation, health and welfare, urban development, education, economic development, and other miscellaneous services.

The accounting policies and financial reporting practices of the Municipality conform to accounting principles generally accepted in the United States of America ("GAAP") as applicable to governmental units. With this financial report, the Municipality has changed its financial reporting to comply with the provisions of GASB Statement No. 34, Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments. As part of the implementation of GASB Statement No. 34, the Municipality adopted a prospective reporting of its general infrastructure assets. The Municipality has applied the retroactively presentation of the historical costs of infrastructure assets during the fiscal year ended June 30, 2003.

In conjunction with the implementation of GASB Statement No. 34, the Municipality has also implemented paragraphs six to eleven of GASB Statement No. 38, Certain Financial Statements Note Disclosures, which rescinds some and modifies other financial statement disclosure requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

A. Component Units

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, The Financial Reporting Entity, of the GASB. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

B. Government-wide and fund financial statements

Financial information of the Municipality is presented in this report as follow:

1. Management's discussion and analysis introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.
2. The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all the activities of the Municipality and its component unit. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-typed activities, if any, which rely to a significant extent on fees and charges for support. Interfund activity has been removed from these statements to minimize the duplicating effect on assets and liabilities within the governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenue. Direct expenses are those that are charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

B. Government-wide and fund financial statements

particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

3. Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. The Municipality reports the following major governmental funds:

General Fund- is the accounting entity in which all governmental activity, except that which is required to be accounted for in another fund, is accounted for. Its revenues consist mainly of taxes, licenses and permits, intergovernmental revenue, charges for services and other.

Special Revenue Fund - (02) - is the accounting entity in which revenues derived from federal and state grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Capital Project Fund - (20) Local, State and Federal Grants - is the accounting entity in which revenues derived from local funds, state and federal grants or other restricted revenue sources related to capital projects, is accounted for. The uses and limitations of each capital project fund are specified by Municipality ordinances or federal and state statutes.

4. The notes to the financial statements provide information that is essential to a user's understanding of the basic financial statements.
5. Required supplementary information such as the budgetary comparison schedule-general fund and other types of data required by GASB.
6. Notes to the budgetary comparison schedule-general fund.

C. Financial reporting presentation

The accounts of the Municipality are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Fund types are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

C. Financial reporting presentation

General Fund- The General Fund is the general operating fund of the Municipality. It is used to account for all governmental activity, except those required to be accounted for in another fund.

Special Revenue Funds- Special Revenue Funds are used to account for revenues derived from grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Debt Service Funds- Debt Service Funds are used to account for the accumulation of resources for and the payment of, general long-term debt principal, interest, and related costs.

Capital Projects Funds- Capital Project Funds are used to account for financial resources used for the acquisition or construction of major capital facilities.

D. Measurement focus, basis of accounting and financial presentation

Except for budgetary purposes, the basis of accounting used by the Municipality conform to accounting principles generally accepted in the United States of America ("GAAP") as applicable to governmental units. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The Municipality has elected not to apply all Statements and Interpretations issued by the Financial Accounting Standard Board after November 30, 1989, in accordance with GASB Statement No.20.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

D. Measurement focus, basis of accounting and financial presentation

considers revenues to be available if they are collected within the current period or soon enough thereafter. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures when payment is due. General capital asset acquisitions are reported as expenditure in governmental funds. Proceeds from issuance of general long-term debt reported as other financing sources.

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash.

Private-sector standards of accounting and financial reporting issue prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The Municipality has elected not to follow subsequent private-sector guidance.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants, and contributions, and 3) capital grants and contributions, including special assessments, if any. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources, as they are needed.

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

- 1. Cash, cash equivalents, and cash with fiscal agent-** The Municipality's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

Cash with fiscal agent in the debt services fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law.

- 2. Receivables and payables-** Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables in the general fund represent mostly contributions from the Puerto Rico Electric Power Authority, which contribute a specific percentage of their revenues as payment in lieu of taxes. Intergovernmental receivable in the special revenue fund represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs and the amount in the debt service fund represent the distribution of property tax collected by the Municipal Revenue Collection Center (CRIM), which is restricted for the debt service.

- 3. Inventories-** Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net assets.
- 4. Capital assets-** Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. The Municipality defines capital asset as assets with an initial, individual cost of more than \$25 and an estimated useful life in excess of one year. Such assets are

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets of the Municipality, as well as the component unit, are depreciated using the straight-line method over the following estimated useful lives:

Description	Useful Life	Capitalization threshold
Buildings and site improvements	40 years	\$ 1
Infrastructure	40 years	\$ 1
Works of art	10 years	\$ 1
Vehicles	5 years	\$ 1
Furniture and fixtures	5 years	\$ 25
Machinery and equipment	3 to 5 years	\$ 25

- 5. Long-term obligations-** The liabilities reported in the government-wide financial statements include the general and special obligation bonds, bank and long-term notes, other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities and landfill closure and post closure care costs.

In the fund financial statements, governmental fund types recognize bond issuances cost, during the current period. The face amount of debt issued is reported as other financing sources, while bond issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the general fund.

- 6. Compensated absences-** Employees accumulate vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. All vacation pay it is accrued when incurred in the government-wide financial statements.

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

7. **Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.
8. **Reservation of fund balance-** Reservations of fund balance in the fund financial statements, represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The municipality has the following reservations of fund balance:
 - a. *Capital Projects-* Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
 - b. *Encumbrances-* Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
 - c. *Debt Service Fund-* Represents net assets available to finance future debt service payments.
 - d. *Other Purposes-* Represents net assets available for specific use and/or legally segregated for other specific future use.
9. **Interfund and intra-entity transactions-** The Municipality has the following types of transactions among funds:
 - a. *Operating Transfers-* Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
 - b. *Intra-Entity Transactions-* Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.
10. **Risk financing-** The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

gross property tax collections by the CRIM for the year ended June 30, 2003 amounted to approximately \$ 406,000. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$276,000 for workers compensation insurance covering all municipal employees.

- 11. Reconciliation of Government-Wide and Fund Financial Statements-** Explanation of certain differences between the Governmental Fund Balance-Total Governmental Funds and Net Assets-Governmental Activities as reported in the Government-Wide Statement of Net Assets. One element of that reconciliation explains that "long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds." The details of this \$4,646,519 are as follows:

Accrued compensated absences	\$ 2,800,609
Landfill closure and post closure care costs	1,047,000
Other long-term debt	<u>798,910</u>
Net adjustment to reduce fund balance total governmental funds to arrive at net assets-governmental activities	<u>\$ 4,646,519</u>

2. DEPOSITS

Under Puerto Rico statutes public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

The Municipality's bank balances in commercial banks of approximately \$ 8,400,000 in the general fund were fully collateralized at June 30, 2003. In the other governmental funds there were deposits with commercial banks of approximately \$ 1,500,000, \$700,000 and \$ 200,000 respectively, that were fully collateralized.

The deposits at GDB of approximately \$ 6,200,000 that are restricted principally for capital projects, and the \$ 1,661,738 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

3. RECEIVABLES

- a. **Municipal License Tax-** The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$ 1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2003, the tax rates were as follows:

- Financial business- 1.50% of gross revenues
- Other organizations- 0.50% of gross revenues

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2003, net of allowance for uncollectibles.

Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

- b. **Intergovernmental Receivables-** Intergovernmental receivables in the general fund principally consist of the amounts due from the Puerto Rico Electric Power Authority ("PREPA"). This represents the amount resulting from the revenues the Municipality is entitled to receive in lieu of payment of taxes. The amounts receivable from other governmental entities are as follows:

Amount presented in the debt service fund represents the ad valorem tax restricted for debt service collected by the CRIM during 2003, which was transferred to the Governmental Development Bank for Puerto Rico in July 2003.

Intergovernmental receivable in the Special Revenue Fund (02) and the Other Governmental Funds represents mainly expenditures incurred not yet reimbursed by the Federal government. Following is a detail of the intergovernmental receivable:

Program Description	Amount
Rural Self-Help Housing Technical Assistance	\$ 207,967
Section 8 Housing Choice Vouchers	21,552
Others	260,015
Total	<u>\$ 489,534</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

3. RECEIVABLES (CONTINUED):

c. Other- Other accounts receivable as of June 30, 2003 are as follows:

	<u>Governmental Type Funds</u>		
	General Fund	Other Governmental Funds	Total
Medical Plans	\$ 23,441	\$ -	\$ 23,441
Other	9,273	-	9,273
	\$ 32,714	\$ -	\$ 32,714
Total other receivables	\$ 32,714	\$ -	\$ 32,714

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2003 are summarized as follows:

a. Due from/to other fund:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Special Revenue Fund (02)	\$ 827,292
	Other Governmental Funds	<u>89,397</u>
Total		<u>\$ 916,689</u>

b. Transfer in/out to other fund

Following is a summary of interfund transfers for the year:

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund (02)	Transfer of funds for Capital Outlays	\$ 158,978
	Capital Projects Fund (20)	Transfer of funds for Capital Outlays	36,622
Special Revenue Fund (02)	Capital Projects Fund (20)	Transfer of funds for Capital Outlays	<u>105,291</u>
Total			<u>\$ 302,891</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

5. CAPITAL ASSETS

Capital assets; those with an estimated useful live of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2003, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

Governmental Activities:	Balance July 1, 2002	Additions	Retirements	Balance June 30, 2003
Capital asset, not being depreciated:				
Land	\$ 14,033,622	\$ 3,677,912	\$ -	\$17,711,534
Total capital assets not being depreciated	<u>14,033,622</u>	<u>3,677,912</u>	<u>-</u>	<u>\$17,711,534</u>
Capital assets, being depreciated:				
Buildings and building improvements	9,613,054	1,833,007	-	11,446,061
Infrastructure	11,914,522	1,357,494	-	13,272,016
Equipment	3,444,963	502,309	138,670	3,808,602
Works of art	185	0	-	185
Vehicles	4,257,030	554,120	-	4,811,150
Total capital assets being depreciated	<u>\$ 29,229,754</u>	<u>\$ 4,246,930</u>	<u>138,670</u>	<u>33,338,014</u>
Less accumulated depreciation for:				
Buildings and building improvements	\$ 4,127,246	\$ 260,958		\$ 4,388,204
Equipment	2,439,005	389,106		2,828,111
Infrastructure	6,515,479	319,032		6,834,511
Works of art	137	19		156
Vehicles	2,971,921	492,483		3,464,404
Total accumulated depreciation	<u>16,053,788</u>	<u>1,461,598</u>		<u>17,515,386</u>
Total capital assets being depreciated, net	<u>13,175,966</u>	<u>2,785,332</u>	<u>138,670</u>	<u>15,822,628</u>
Governmental activities capital assets, net	<u>\$ 27,209,588</u>	<u>\$ 6,463,244</u>	<u>\$ 138,670</u>	<u>\$ 33,534,162</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

5. CAPITAL ASSETS (CONTINUED):

Depreciation expense was charged to functions/programs of the Municipality as follows:

Governmental activities:

General government	\$ 206,178
Public safety	93,018
Public works	904,923
Culture and recreation	149,755
Health and welfare	82,862
Economic development	<u>24,862</u>
Total depreciation expense-governmental activities	<u>\$ 1,461,598</u>

6. PROPERTY TAXES

The personal property tax is self assessed by the taxpayer on a return which is to be filed by May 15 of each year with the CRIM, a governmental entity created by the government of Puerto Rico as part of the Municipal Governmental Autonomous Law of August 1991. Real property tax is assessed by the CRIM on each piece of real estate and on each building.

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. The CRIM issued the final liquidation noting that the collections exceeded advances by \$29,229. Such amount was included as intergovernmental receivables in the General Fund.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

6. PROPERTY ASSETS (CONTINUED):

Puerto Rico Treasury Department assumes payment of the basic tax to the Municipalities, except for property assessed at less than \$ 3,500 for which no payment is made. As part of the Municipal Autonomous Law of 1991, the exempt amount to be paid by the Puerto Rico Treasury department to the Municipalities was frozen as of January 1, 1992. In addition, the law grants a tax exemption from the payment of personal property taxes of up to \$50,000 of the assessed value to retailers having annual net sales of less than \$150,000.

The annual tax rate is 8.08% for real property and 6.08% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.25% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund. The Commonwealth also contributes an annual tax rate of 0.2% of the property tax collected and such amount is accounted for similar to item (a) above.

7. DUE TO OTHER GOVERNMENTAL ENTITIES:

The amounts due to other governmental entities in the General Fund include the following:

General Services Administration	\$ 2,123
Puerto Rico Telephone Company	77,434
Puerto Rico Aqueduct and Sewer Authority	<u>5,070</u>
Total	<u>\$ 84,627</u>

The Municipality reached an agreement with the Municipal Revenue Collection Center for the payment of a debt on a long-term basis. This liability is presented in the Statement of Net Assets as a non-current liability.

8. DEFERRED REVENUES

- a. **Municipal License Tax-** The deferred revenues of approximately \$8,153,704 in the general fund relates to municipal license tax collected in fiscal year 2002-03 that will be earned in fiscal year 2003-04.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

8. DEFERRED REVENUES (CONTINUED):

b. **Federal Government-** The deferred revenues presented in other governmental funds represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

Program Description

Section 8 Housing Choice Vouchers	\$ 175,174
Library Services and Technology Grant	30,754
Child Care and Development Block Grant	20,549
Local Law Enforcement Block Grants	17,437
Other	<u>148,805</u>
Total	<u>\$ 392,719</u>

9. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2003, was as follows:

	Beginning Balance	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds Payable	\$10,980,000	\$1,915,000	\$(900,000)	\$11,995,000	\$915,000
Notes Payable	325,000	-	(325,000)	-	-
Advances from CRIM	1,035,301		(236,391)	798,910	9,432
Compensated Absences	2,594,677	205,932		2,800,609	118,300
Landfill obligation	<u>2,792,290</u>		<u>(1,745,290)</u>	<u>1,047,000</u>	<u>47,000</u>
Total	<u>\$17,727,268</u>	<u>\$2,120,932</u>	<u>\$(3,206,681)</u>	<u>\$16,641,519</u>	<u>\$1,089,732</u>

- a. **Legal debt margin-** The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment if property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues if the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds payable, is paid with unrestricted funds.
- b. **Bonds payable-** The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities. During the current year, the Municipality issued bonds for approximately \$1,900,000. Bonds payable outstanding at June 30, 2003 are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

9. LONG-TERM LIABILITIES (CONTINUED):

Type of bonds	Maturity date	Original amount	Range of Interest rates	Balance at June 30, 2003
1992 Series	7-1-06	\$ 1,530,000	3.2% to 6.3%	\$ 630,000
1994 Series	7-1-03	1,120,000	5.0% to 7.8%	160,000
1996 Series	7-1-21	605,000	4.8% to 6.7%	550,000
1997 Series	7-1-06	1,435,000	4.8% to 6.7%	710,000
1999 Series	7-1-03	585,000	4.8% to 6.3%	135,000
2000 Series	7-1-24	260,000	2.7% to 7.8%	245,000
2000 Series	7-1-24	710,000	2.7% to 7.8%	680,000
2000 Series	7-1-25	555,000	2.7% to 7.8%	360,000
2000 Series	7-1-25	6,440,000	2.7% to 7.8%	6,255,000
2001 Series	7-1-06	430,000	5.0% to 8.0%	355,000
2002 Series	7-1-06	1,335,000	4.8% to 6.7%	1,335,000
2002 Series	7-1-26	580,000	5.0% to 6.5%	<u>580,000</u>
Total general obligation bonds				<u>\$ 11,995,000</u>

These bonds are payable from the ad valorem property tax of 1.25% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

Annual debt service requirements to maturity for bonds payable are as follows:

Year Ending June 30,	Principal	Interest
2004	\$ 915,000	\$ 582,277
2005	715,000	564,314
2006	775,000	534,461
2007	705,000	499,378
2008	245,000	476,248
2009-2013	1,535,000	2,178,526
2014-2018	2,210,000	1,700,113
2019-2023	3,010,000	968,015
2024-2028	1,885,000	167,090
Total	<u>\$ 11,995,000</u>	<u>\$ 7,670,422</u>

- c. **Advances from CRIM-** This amount represents the balance owed to CRIM at June 30, 2003 will be repaid partially through a financing obtained by the CRIM with GDB and other part will be deduct from the gross property tax collections by the CRIM in the next fiscal year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

9. LONG-TERM LIABILITIES (CONTINUED):

- d. **Compensated absences-** The government-wide statement of net assets includes approximately \$ 2,800,000 of accrued vacation and sick leave benefits, representing the Municipality's commitment to fund such costs from future operations.

- e. **Landfill obligation-** State and federal laws and regulations require the Municipality to place a final cover on its landfill site since 1994, when it stopped accepting waste, and perform certain maintenance and monitoring functions at the site for 30 years after closure. In accordance with Statement No. 18 of the GASB, "Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Costs", the Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. Based on this study, the Municipality has recognized \$ 1,047,000 as the Municipality's estimated current cost for landfill post-closure costs as of June 30, 2003. The annual estimate of post closure costs has been assessed approximately to be \$ 47,000 for a period of approximately 22 years. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations. The balance of post-closure costs are reported in the government-wide statement of net assets.

10. PENSION PLAN

The Employee's Retirement System of the Commonwealth and its Instrumentalities (the Retirement System) is a cost-sharing multiple defined benefit pension plans sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Municipality under 55 years of age at the date of employment become members of the Retirement System as a condition to their employment.

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

Members who have attained 55 years of age and have completed at least 25 years of creditable service or members who have attained 58 years of age and have completed ten years of creditable service are entitle to an annual benefit payable monthly for life.

The amount of the annuity shall be one and one-half percent of the average compensation, as defined, multiplied by the number of years of creditable service up to twenty years, plus

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

10. PENSION PLAN (CONTINUED)

two percent of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65 percent of the average compensation, as defined; otherwise they will receive 75 percent of the average compensation, as defined. No benefits are payable if the participant receives a refund of his/her accumulated contributions.

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions to the above-mentioned plans during the year ended June 30, 2003 recorded as pension expenditures were approximately \$ 528,000. This amount represents 100% of the required contribution for the fiscal year ended June 30, 2003.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employee's participation in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Municipality on or after January 1, 2000, will only be allowed to become members of System 2000. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2003

10. PENSION PLAN (CONTINUED)

Additional information on the Retirement System is provide in its financial statements for the year ended June 30, 2003, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42003, San Juan, PR 00940

11. COMMITMENTS AND CONTINGENCIES

A. Federal grants:

The Municipality participates in a number of Federal Financial Assistance Programs. Although the Municipality's grant programs have been audited in accordance with the provisions of the Single Audit Act of 1996, through June 30, 2003, these programs are still subject to financial and compliance audits by the granting agencies and the resolution of previously identified questioned costs. The amount, if any, of expenditures which may be disallowed by the grating agencies cannot be determined at this time, although the Municipality expects such amounts, if any, not to be material.

B. Claims and lawsuits:

The Municipality is a defendant in several legal proceedings that arise in the ordinary course of the Municipality's activities. Certain of these claims are covered by insurance. The administration believes that the ultimate liability, if any, would not be significant. As a result, the accompanying general-purpose financial statements do not include adjustments, if any, that could result from the resolution of these legal proceedings.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

BUDGETARY COMPARISON SCHEDULE- GENERAL FUND

YEAR ENDED JUNE 30, 2003

	<u>Budgeted Amounts</u>		<u>Actual Amounts (Budgetary Basis) (See Note 1)</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
REVENUES:				
Property taxes	\$3,878,154	\$ 4,072,639	\$ 4,189,070	\$ 116,431
Municipal license tax	8,800,000	9,154,124	9,156,730	2,606
Licenses, permits and other local taxes	503,000	576,125	597,398	21,273
Intergovernmental	3,098,277	3,098,277	3,098,277	
Rent of property	4,200	29,751	17,887	(11,864)
Fines and forfeitures	1,000	2,295	2,955	660
Interest	300,000	377,662	428,414	50,752
Miscellaneous	234,000	387,671	428,483	40,812
Budgeted carryover		<u>362,396</u>	<u>362,396</u>	
Total revenues and budget carryover	<u>16,818,631</u>	<u>18,060,940</u>	<u>18,281,610</u>	<u>220,670</u>
EXPENDITURES AND OTHER FINANCING USES:				
Current:				
General government	7,367,497	8,132,462	8,096,370	36,092
Public safety	1,461,808	1,510,779	1,498,535	12,244
Public works	5,271,922	5,000,060	4,669,205	330,855
Health and welfare	1,283,564	2,325,735	2,298,163	27,572
Culture and recreation	1,049,434	760,537	761,301	(764)
Economic development	255,806	253,703	171,674	82,029
Interest	128,600	77,664	77,664	
Transfer to other fund			<u>197,600</u>	<u>(197,600)</u>
Total expenditures and other financing uses	<u>16,818,631</u>	<u>18,060,940</u>	<u>17,770,512</u>	<u>290,428</u>
EXCESS OF REVENUES OVER EXPENDITURES			<u>\$ 511,098</u>	<u>\$511,098</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis)"available for appropriation" from the budgetary comparison schedule				\$ 18,281,610
Differences-budget to GAAP:				
Budgeted carryover				(362,396)
Nonbudgeted revenues				<u>133,205</u>
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 18,052,419</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis)"total charges to appropriations" from the budgetary comparison schedule				\$ 17,770,512
Differences-budget to GAAP:				
Transfer to other funds are outflows of budgetary resources but are not expenditures for financial reporting purpose				(197,600)
Nonbudgeted expenditures				406,584
Prior year encumbrances recorded as current year expenditures for GAAP basis				153,471
Current year encumbrances recorded as expenditures for budgetary purposes				<u>(217,543)</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 17,915,424</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES OF BUDGETARY COMPARISON SCHEDULE- GENERAL FUND

YEAR ENDED JUNE 30, 2003

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

a. Budgetary Control

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with GAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

The Municipality prepares its annual budget including the operations of the general fund.

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year.

The unencumbered balance of any appropriation at the end of the fiscal year will lapse at the end of such fiscal year. Other appropriations, mainly capital project appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2003 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2003.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2003

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Federal Expenditures</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Programs:			
Section 8 Housing Choice Vouchers :	14.871		\$ 1,021,422
Community Development Block Grants- Entitlement Grants	14.218	B-00-MC-72-0021 B-01-MC-72-0021 B-02-MC-72-0021	1,280,923
Pass-through Commonwealth of Puerto Rico Department of the Family: Emergency Shelter Grants Program	14.231	S-99-DC-72-0001	<u>6,208</u>
Total U.S. Department of Housing and Urban Development			<u>2,308,553</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Federal Expenditures
U.S DEPARTMENT OF AGRICULTURE:			
Direct Programs:			
Rural Business Enterprise Grants	10.769		100,652
Rural Self-Help Housing Technical Assistance	10.420		93,960
Rural Housing Site Loans and Self-Help Housing Land Development Loans	10.411		<u>158,644</u>
Total U.S. Department of Agriculture			<u>353,256</u>
U.S DEPARTMENT OF JUSTICE:			
Universal Hiring Program	16.710		17,437
Pass-through the Commonwealth of P.R. Department of Justice Local Law Enforcement Block Grants Program	16.592	NOT AVAILABLE	94,690
Total U.S. Department of Justice			<u>112,127</u>
U.S DEPARTMENT OF TRANSPORTATION:			
Pass-through the Commonwealth of Puerto Rico Highway Authority Formula Transit: Formula Grants	20.507		293,060
Pass-through the Commonwealth of Puerto Rico Highway Safety Commission Alcohol Traffic Safety and Drunk Driving Prevention Incentive Grant	20.601		4,300
Total U.S. Department of Transportation			<u>297,360</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Federal Expenditures
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico -Administration for Children and Families:			
Child Care and Development Block Grant	93.575	NOT AVAILABLE	<u>143,151</u>
Total U.S. Department of Health and Human Services			<u>143,151</u>
U.S. DEPARTMENT OF EDUCATION:			
Pass-through the Commonwealth of Puerto Rico -Department of Education:			
Library Services and Technology Grant	N/A	NOT AVAILABLE	<u>4,363</u>
Total U.S. Department of Education			<u>4,363</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$3,218,810</u>

The accompanying notes are an integral part of this schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2003

A. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the **Municipality of Cidra** and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the fund financial statements. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

B. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Special Revenue and Other Governmental Funds in the Municipality's basic financial statements. The reconciliation between the expenditures in the basic financial statements and the disbursements in the Schedule of Expenditures of Federal Awards is as follows:

<u>Description</u>	<u>Special Revenue (02)</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Per Schedule of Expenditures of Federal Awards	\$1,392,223	\$1,826,587	\$3,218,810
Non federal programs Expenditures	<u>954,017</u>	<u>2,270,903</u>	<u>3,224,920</u>
Total expenditures in the basic financial statements	<u>\$2,346,240</u>	<u>\$4,097,490</u>	<u>\$6,443,730</u>



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Cidra
Cidra, Puerto Rico**

We have audited the basic financial statements of the **Municipality of Cidra** as of and for the year ended June 30, 2003, and have issued our report thereon dated December 20, 2003, which was unqualified. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the **Municipality of Cidra's** basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of basic financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality of Cidra's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting.

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS (CONTINUED)**

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose reportable conditions that are also considered to be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted certain matters involving the internal control over financial reporting, which we have reported to management of the **Municipality of Cidra** in a separate letter dated December 20, 2003.

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 20, 2003

Stamp No. 1942285 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.





López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

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**INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133**

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Cidra
Cidra, Puerto Rico**

Compliance

We have audited the compliance of the **Municipality of Cidra** with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2003. The **Municipality of Cidra's** major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the **Municipality of Cidra's** management. Our responsibility is to express an opinion on the **Municipality of Cidra's** compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the **Municipality of Cidra's** compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the **Municipality of Cidra's** compliance with those requirements.

In our opinion, the **Municipality of Cidra** complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2003. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements that is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings and questioned costs as items **03-01** through **03-08**.

INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133
(CONTINUED)

Internal Control Over Compliance

The management of the **Municipality of Cidra** is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the **Municipality of Cidra's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matter involving the internal control over compliance and its operation that we consider to be reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the **Municipality of Cidra's** ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. Reportable condition is described in the accompanying Schedule of Findings and Questioned Costs as items **03-01** through **03-08**.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees on the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weakness. However, we believe that reportable condition described above is not a material weakness. We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the **Municipality of Cidra** in a separate letter dated March 5, 2004.



**INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133
(CONTINUED)**

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
March 5, 2004

Stamp No. 1942286 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2003

Section I – Summary of Auditors’ Results

Financial Statements

Type of auditors’ report issued: **Unqualified**

Internal control over financial reporting:

Material weakness identified? Yes _____ No X

Reportable conditions identified
not considered to be material weaknesses? Yes _____ None reported X

Noncompliance material to financial statements
noted? Yes _____ No X

Federal awards

Internal Control over major programs:

Material weakness identified? Yes _____ No X

Reportable conditions identified not considered
to be material weaknesses? Yes X None reported _____

Type of auditors’ report issued on compliance
for major programs: **Unqualified**

Any audit findings disclosed that are required
to be reported in accordance with Circular
A-133, Section .510(a)? Yes X No _____

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
14.218	Community Development Block Grant – Entitlement Grants
14.871	Section 8 Housing Choice Voucher
Dollar threshold used to distinguish between Type A and Type B programs \$ 300,000	
Auditee qualified as low-risk auditee? Yes <u>X</u> No _____	

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-01
Program	Community Development Block Grant - Entitlement Grant (CFDA. No. 14.218); U.S. Department of Housing and Urban Development
Requirement	Reporting
Statement of Condition	<p>During our audit of the Federal Cash Transaction Report (SF-272), we noted the following:</p> <ul style="list-style-type: none">a. For the period ended 9/30/02, reported credit withdrawals (line 11a) did not reconcile with the credit withdrawals recorded in the accounting records.b. For the periods ended 12/31/02, 3/31/03 and 6/30/03. reported credit withdrawals and total receipts did not reconcile with the accounting records.c. The reports ended in the period 3/31/03 and 6/30/03 was submitted several months after the due date.
Criteria	<p>OMB Common Rules, Subpart C, Section 85.20 (b) (1), and 85.41 (c) (4) states that the grantee must maintain internal control procedures that permits proper tracing of funds to accounting records. Also it requires that grantees must submit the report no later than 15 working days following the end of each quarter.</p>
Cause of Condition	<p>There is no adequate internal control procedures to assure the accurate completion and the timely submission of the Federal Cash Transaction Report.</p>
Effect of Condition	<p>The Municipality did not comply with the 24 CFR, Section 85.20 (b) (1) and 85.41 (c) (4).</p>
Recommendation	<p>We recommend that the Municipality should implement procedures in order to assure that the report only present the cash advances and the outlay information for the grants.</p>
Questioned Costs	<p>None</p>
Management Response and Corrective Action Plan	<p>The Municipality concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Mayor Federal Award Program Finding and Questioned Cost

Finding Reference	03-02
Program	Community Development Block Grants - Entitlement Program (CFDA. No. 14.218); U.S. Department of Housing and Urban Development.
Requirement	Sub-recipient Monitoring
Statement of Condition	The Municipality did not perform the necessary monitoring procedures to obtain a reasonable assurance that the sub recipient administers program funds in compliance with Federal requirements.
Criteria	Code of Federal Regulations 24, Section 570.503 states that the Municipality must perform monitoring activities in order to review the financial information and observes that operations of the sub-recipients are realized in accordance with the agreement.
Causes of Condition	There are no adequate internal controls procedures to assure that sub-recipient complies with Program requirements.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Section 570.503.
Recommendation	We recommend management to follow monitoring system procedures to obtain a reasonable assurance that the funds administers by the sub recipient are in compliance with Federal requirements.
Questioned Costs	None
Management Response and Corrective Action Plan	The Municipality concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-03
Program	Community Development Block Grants - Entitlement Grants (CFDA. No. 14.218); U.S. Department of Housing and Urban Development
Requirement	Special Test - Housing Rehabilitation
Statement of Condition	<p>During our examination of twenty-five (25) Housing Rehabilitation Participant's files, we noted the following:</p> <ol style="list-style-type: none">a. In two (2) instances the files did not contain an evaluation sheet signed by Municipality's inspector to ascertain that the pre-rehabilitation inspection was performed or a document that describes the participant housing unit deficiencies to be corrected.b. In twenty-three (23) cases the rehabilitation contract did not specify which where the participant housing unit deficiencies to be corrected. The contract made reference to the Purchase Order.c. In one (1) case the rehabilitation file did not present the eligibility application.d. In eighteen (18) cases the income and employment status of participants have not been properly verified.e. In three (3) cases the rehabilitation file did not present evidence of the applicant disability.f. In four (4) cases the rehabilitation file did not present evidence of the family composition.g. In three (3) cases the income of the participants exceeds the income limit settled down by the Municipality.h. In one (1) case the rehabilitation file did not present the eligibility determination.i. In fifteen (15) cases, we noted that the grantee did not perform the final inspection of the rehabilitation work during the period established in the housing rehabilitation contract. The inspections of the rehabilitation work were performed between six and fourteen months after the culmination of the rehabilitation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-03 (continued)
Requirement	Special Test - Housing Rehabilitation j. Four (4) files did not include evidence of the final inspection in order to assure the rehabilitation work was realized according to the agreement.
Criteria	24 CFR, Section 570.506 states that when CDBG- Entitlement Grants funds are used for rehabilitation, the grantee must assure that the work is properly completed and appropriate documentation is maintained.
Cause of Condition	The program has not established adequate internal control procedures to assure that rehabilitations are duly completed as required by regulations and appropriate documentation is maintained.
Effect of Condition	The Municipality is not in compliance with 24 CFR, Section 570.506.
Recommendation	We recommend the Program to establish the following procedures: a. Realize pre-rehabilitation inspection describing the participant housing unit deficiencies to be corrected. b. Assign a staff to inspect the rehabilitation work upon completion to assure that is carried out in accordance with contracts specifications. c. Assure that all participant files include all required documentation such as eligibility determination and adequate evidence of family income.
Questioned Costs	None
Management Response and Corrective Action Plan	We are currently in an audit with HUD Caribbean from San Juan. Major corrections are being made as this single audit is being performed. The Mayor has hired two new employees in this area for the purpose of placing this program in compliance. HUD is waiting for our program director to indicate when HUD can return to finalize the audit. It is the Mayor desire to comply with all compliance recommendation as soon as possible.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-04
Program	Section 8 Housing Choice Vouchers (CFDA 14.871), U.S. Department of Housing and Urban Development
Requirement	Cash Management
Statement of Condition	We realized Cash Management Test and after our procedures we found that the Program maintained an excessive average cash balance in books.
Criteria	OMB Common Rules, Subpart C, Section 85.20 (b) (7), which requires a cash management system, in order to minimize the time elapsed between the transfer of funds from the U.S. Treasury and disbursement by the grantee.
Cause of Condition	The Federal Program Department did not maintain appropriate cash management procedures in order to request funds to federal agencies only for immediate needs.
Effect of Condition	The Municipality did not comply with the OMB Common Rules, Subpart C, Section 85.20, (b) (7).
Recommendation	We recommend that management should strengthen it's procedures to minimize the time elapsed between the transfer of funds from the federal agency and the disbursements made by the Municipality.
Questioned Costs	None
Management Response and Corrective Action Plan	This situation was corrected as per the HUD monitoring procedures.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-05
Program	Section 8 Housing Choice Vouchers (CFDA 14.871), U.S. Department of Housing and Urban Development
Requirement	Eligibility Test
Statement of Condition	<p>We performed an eligibility test and examined a sample of twenty-five (25) participant files. The following summarize the deficiencies found:</p> <ul style="list-style-type: none">a. Nine (9) files did not include a Privacy Act Notice. Also in four (4) files the document didn't present the date when it was signed.b. In seven (7) cases the members of the family with 18 years or older did not sign the release forms to allow the PHA to obtain information from third parties related to employment information.c. In the twenty-two (22) cases the eligibility determination was not approved by an authorized official using the documentation from third partiesd. There were seven (7) tenant files which did not contain complete evidence supporting tenant's income included in the Family Report.e. There were nine (9) tenant files which did not contain accurate evidence or the evidence available has errors and did not agree with the Family Report.f. There were five (5) tenant files which did not provide the necessary information to determine how the tenant was selected from the waiting list.g. Seven (7) of the files did not contain rent reasonableness documentation.h. Nine (9) of the files did not document adequately the determination of reasonable rent.i. In three (3) of the files the annual inspection was not realized on a timely basis or the files did not contain documentation indicating the required unit inspections had been performed.j. There were two (2) files which did not contain evidence which supports that the repairs were realized before the deadline.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-05 (Continued)
Program	Section 8 Housing Choice Vouchers (CFDA 14.871), U.S. Department of Housing and Urban Development
Requirement	Eligibility Test (continued)
Criteria	Code of Federal Regulations 24, Sections 2.212, 5.230, and 5.601 through 5.617 states that as a condition of admission or continued occupancy, it requires the tenant and other family members to provide necessary information, documentation and releases for the PHA to verify income eligibility. As part of this regulation the participant and other members of the family who are at least 18 years old must sign an application form, one or more releases forms, a Federally prescribed general release form for employment information and a Privacy Act Notice.
Cause of Condition	The Municipality does not have adequate internal control procedures to assure that the participant's files include all required documentation and releases required by federal agencies.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Sections 2.212, 5.230, and 5.601 through 5.617.
Recommendation	We recommend the Program to establish the following procedures: <ol style="list-style-type: none">a. Provide an application form to be completed by the participant and signed by all family members who are at least 18 years old.b. Provide a Federally prescribed general release form for employment information and a Privacy Act Notice to be signed by all members of the family who are at least 18 years old.c. Implement internal control procedures to assure that the participant's files include all required documentation required by federal agencies.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-05 (Continued)
Program	Section 8 Housing Choice Vouchers (CFDA 14.871), U.S. Department of Housing and Urban Development
Requirement	Eligibility Test (continued)

Management Response and Corrective Action Plan	<p>HUD audited our office on July 16, 2002. These same factors were found. Since January 2003 on all corrections have been made. According to HUD we are complying with their regulations. Such is this, that we are no longer categorized as a "troubled" Municipality</p> <p>As mentioned before, all inspections are up-to-date. Effective January 2003 and on, all inspections have been performed on a timely basis.</p> <p>Effective January 2003 all files are complete with the required documentation.</p>
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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-06
Program	Section 8 Housing Choice Vouchers (CFDA 14.871), U.S. Department of Housing and Urban Development
Requirement	Special Test - Selection from the Section 8 Waiting List
Statement of Condition	During our waiting list examination, we noted that the PHA did not maintain a waiting list in accordance with HUD regulations that is easily auditable.
Criteria	Code of Federal Regulations 24, Section 982.204 states the waiting list proper organization and preparation.
Cause of Condition	The program did not maintain adequate internal control procedures to assure the proper preparation of the waiting list.
Effect of Condition	The Municipality is not in compliance with 24 CFR section 982.204.
Recommendation	The program should prepare and organize the waiting list following the parameters established in the Administrative Plan.
Questioned Costs	None
Management Response and Corrective Action Plan	We were under the understanding that the waiting list was supposed to be done according to priority. This is the way the waiting list was handed in to HUD. We are now organizing the waiting list as you requested, on a first serve basis. (By date & time)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-07
Program	Section 8 Housing Choice Vouchers (CFDA 14.871), U.S. Department of Housing and Urban Development
Requirement	Reporting – Financial Reporting
Statement of Condition	During our examination of financial reporting requirements, we noted the following exception: a. We noted that the Voucher for Payment of Annual Contribution and Operation Statement did not trace to the accounting records.
Criteria	OMB Common Rules, Subpart C, 24 CFR 85.20 (b)(1), require that accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or sub-grant. Also, Subpart C, 24 CFR 85.20 (b) (2), state that the grantee must maintain records, which adequately identify the source and application of funds, provided for financially assisted activities.
Cause of Condition	The Municipality did not establish effective internal control over the transactions recorded on its accounting records.
Effect of Condition	Municipality is not in compliance with OMB Common Rules, Subpart C, 24 CFR 85.20 (b)(1 and 2).
Recommendation	We recommend to the Municipality's Management to implement controls procedures over Section 8 Rental Program financial activities in order to assure the accountability of all financial transactions, including accounting records in accordance with Generally Accepted Accounting Principles. Such action should permit the preparation of accurate, current, and complete financial reports.
Questioned Costs	None
Management Response and Corrective Action Plan	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	03-08
Program	Section 8 Housing Choice Vouchers (CFDA 14.871), U.S. Department of Housing and Urban Development
Requirement	Special Test - Utility Allowance Schedule
Statement of Condition	During our Utility Allowance Schedule Test, we noted that the PHA did not maintain an updated utility schedule.
Criteria	Code of Federal Regulations 24, Sections 982.503, 982.517 and 982.405 states that the PHA must develop, review and maintain an updated utility schedule.
Cause of Condition	The PHA did not maintain an updated utility schedule for the determination that the utility allowance is reasonable.
Effect of Condition	The Municipality is not in compliance with 24 CFR sections 982.503, 982.517 and 982.405.
Recommendation	We recommend the PHA develop, review and maintain an updated utility schedule. It must review the utility rate it has obtained within the last twelve (12) months, and adjust its allowance schedule to reflect changes of 10% or more.
Questioned Costs	None
Management Response and Corrective Action Plan	The Utility Study was conducted and finalized on February 2004. the new amounts will be placed into effect on July 1, 2004, when the new budget is entered.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2003

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
02-02	14.218	<u>The Municipality should follow monitoring system procedures developed, including obtaining contractor and subcontractor's weekly payrolls to be reviewed weekly by responsible Municipal Employee. Also, interview contractor and subcontractor's laborers periodically (up to ten percent (10%) of the workers on long term projects) to establish the degree of compliance and the nature and extend of violations, if any. Also, we recommend management to communicate contractors promptly any failure found in the payroll process.</u>
02-03	14.218	Corrective action was taken. <u>The Municipality should strength its procedures in order to assure that the contracts contain all provisions requested by federal agencies.</u>
02-04	14.218	Corrective action was taken. <u>The Municipality should establish the following procedures: realize pre-rehabilitation inspection describing the participant housing unit deficiencies to be corrected; assign a staff to inspect the rehabilitation work upon completion to assure that is carried out in accordance with contracts specifications; assure that all participant files include all required documentation, such as eligibility determination and adequate evidence of family income.</u>
02-05	14.871	No corrective action was taken. See current year finding number 03-03. <u>The Municipality should strengthen it's procedures to minimize the time elapsed between the transfer of funds from the federal agency and the disbursements made by the Municipality.</u>
02-06	14.871	No corrective action was taken. See current year finding number 03-04. <u>The Municipality should establish adequate internal controls in order to assure that the program complied with federal regulations and maintain proper records to support SEMAP Report answers.</u>
02-07	14.871	Corrective action was taken. <u>The Municipality should establish the following procedures: provide an application form to be completed by the participant and signed by all family members who are at least 18 years old; provide a Federally prescribed general release form for employment information and a Privacy Act Notice to</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CIDRA**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS - (CONTINUED)

YEAR ENDED JUNE 30, 2003

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<u>be signed by all members of the family who are at least 18 years old; implement internal control procedures to assure that the participant's files include all required documentation required by federal agencies.</u>
02-08	14.871	No corrective action was taken. See current year finding number 03-05. <u>The Municipality should prepare and organize the waiting list following the parameters established in the Administrative Plan.</u>
02-09	14.871	No corrective action was taken. See current year finding number 03-06. <u>The Municipality should implement controls procedures over Section 8 Rental Program financial activities in order to assure the accountability of all financial transactions, including accounting records in accordance with Generally Accepted Accounting Principles. Such action should permit the preparation of accurate, current, and complete financial reports.</u>
02-10	14.871	No corrective action was taken. See current year finding number 03-07. <u>The Municipality should develop, review and maintain an updated utility schedule. It must review the utility rate it has obtained within the last twelve (12) months, and adjust its allowance schedule to reflect changes of 10% or more.</u>
01-02	14.218	No corrective action was taken. See current year finding number 03-08. <u>Failure to document the Housing Rehabilitation Participant's files</u> No corrective action has been taken. The Municipality will improve the procedures established for housing rehabilitation activities. See current year finding number 03-03.

Corrective Action Plan of Single Audit for year ended June, 2003.

Its my understanding that part of a single audit and when ever possible the independent auditor should when possible allow for reasonable time to take corrective action with the intention of correcting the findings prior the the final report and once corrected under federal guidelines should not appear in the final report.

Over the past three years the Department of Federal Affairs has not been given reasonable time (at least a couple of weeks to a month) to correct any finding prior to the final report which is due March 31 of each year.

The Director has discussed this important issue with the Mayor, the Finance Director and our internal Auditor and recently with the independent auditor. The following recommendations and changes to the independent auditor (CPA) contract will be studied and recommended to the mayor for approval.

1. The auditor will audit the Department of Federal Affairs first.
2. All findings will be reported to the Director of Federal Affairs within 90 days of the commencement of the contract and no later than 90 days from the due date. (March 31 of each year).
3. Any finding that is corrected and within federal compliance should not appear in the final report.
4. The final draft will be available for review no later than 60 days from the final report.

With these recommendations and changes the independent auditor will greatly enhance the Department of Federal Affairs ability to aggressively comply with OMB- Circular A-133.

It is the Mayors intention to take the necessary steps and changes in enhancing our methods to fully comply and exceed OMB- Circular A-133. The Mayor always strives to be the best in everything the federal government requests. We understand that with these changes we will start steering our auditing methods in a positive direction to excellence.

02 JUN 13 AM 2003

CPA DIVISION



**Schedule of findings Award finding and Questioned Cost
Year Ending June 30, 2003**

Section III- Finding Reference 03-01 Page 47

Corrective Action Taken:

During the audit for Federal Cash Transaction Report (SF 272) in areas "A+B" this finding was produced in the process of generation the necessary signatures with the purchase component. We have recommended to the Department of Federal Affairs accountant and the finance director to possible color code this component alerting both parties the importance of acquiring the necessary signatures on a timely basis. This finding we understand is rear and we feel should not happen again.

In area "C" of the finding I have instructed our accountant in the Department of Federal Affairs to implement the following suggestion and avoid this finding in the future.

1. Develop a calendar with quarterly date indicating when quarterly reports are due and refer to this calendar on a regular basis.
2. To use and develop a software program which Microsoft Office so that when the computer is turned on it will indicate to the accountant when quarterly reports are due via the computer automatically.

Schedule of findings Award finding and Questioned Cost Corrective Action Response

Finding Reference 03-02 Page 48

Corrective action taken:

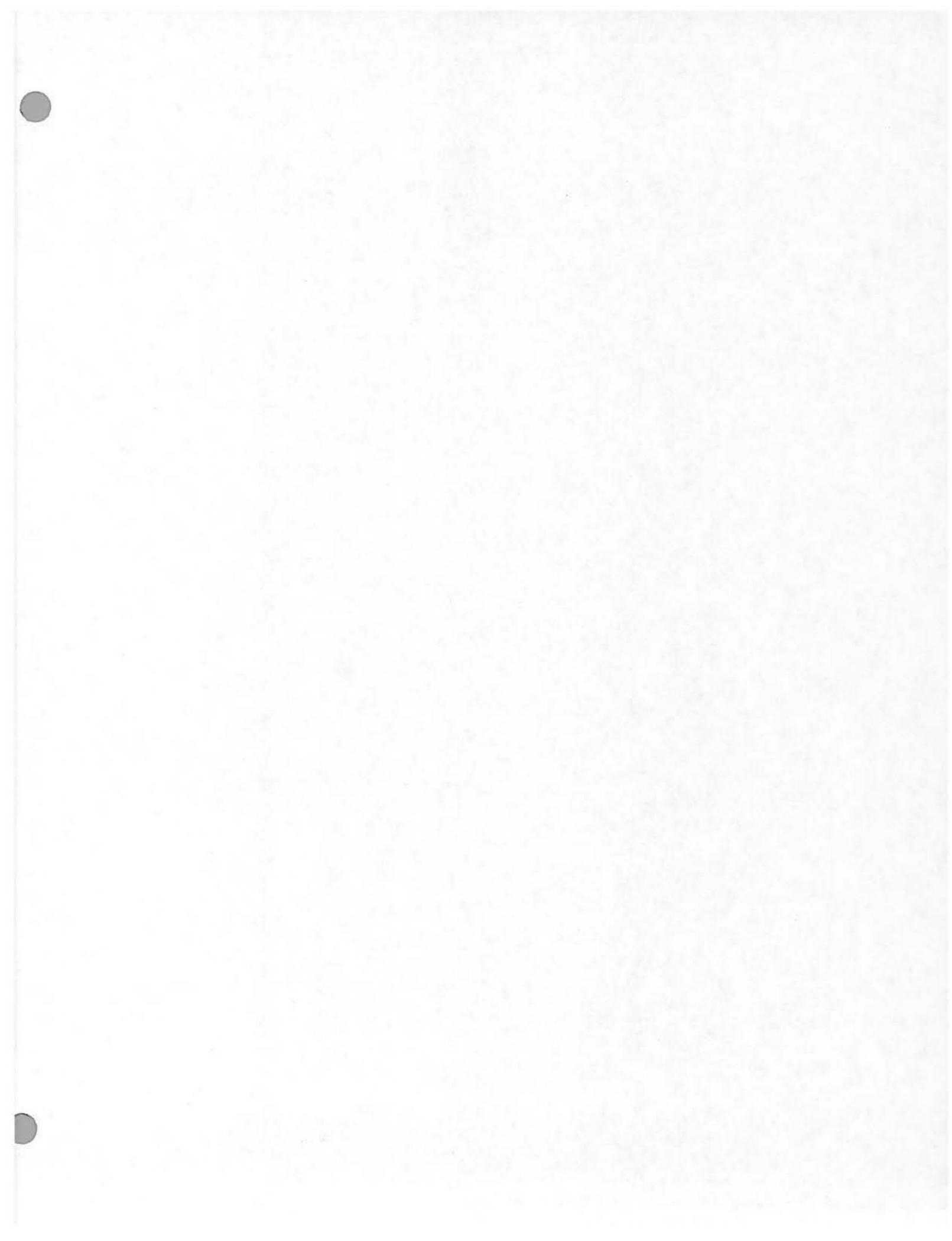
Before, during and after the Single Audit the Department of Federal Affairs was conducting periodic visits to all three sub-recipients, the purpose of these visits were to confirm Municipal funding was being spent as stated in each proposal and under federal guidelines.

All three sub-recipients were following requested guidelines and regulations. They all supplied complete documentation photos for all three projects. All three are complying with federal rules governing sub-recipients, checks and balances are confirmed.

The Department of Federal Affairs was in the process of gathering the necessary documentation when the single audit was taking place. The CPA firm conducting the audit only allowed for a few days to take corrective action prior to the final report. As we stated in our cover letter; if the CPA firm conducting the single audit allowed for reasonable time to take corrective action this finding and most if not all of the findings for fiscal year 2002-2003 would not have appeared in the final report and we would have been granted an excellent performance rating which will be the direction we will take for fiscal year audit 2003-2004.

As additional corrective action pertaining to sub recipients in the future the Municipal Government of Cidra will implement the following changes to sub-recipient grants.

1. The municipality will establish bank accounts for each sub-recipient.
2. The municipality will no longer grant donation in the form of a check.
3. The municipality will disburse funds only when the sub-recipient demonstrates that the work projected in the proposal was carried out.
4. Each sub-recipient will turn in as part of their file photos, canceled checks and any documentation that we understand is necessary to justify any disbursement of funds.
5. Each sub-recipient will be required to submit a quarterly progress report.
6. The municipality will conduct a closeout monitoring visit to each sub-recipient.



7. The municipality will use the manual titled "Techniques for Monitoring Federal Sub-award as a guide". Copy attached as attachment 1.

Section III- Finding Reference program 03-03 Page 49.

Special Test- Housing Rehabilitation

The Mayor has hired a new program coordinator, Rehabilitation Inspector and a secretary. The program is now fully staffed with four employees. A new administrative manual has been developed and submitted and approved by our CPD representative Lourdes Moreno. We have implemented all recommendations from HUD during and after the audit. It's our understanding that the office of Housing Rehabilitation has made mayor improvements on the administration of the program. On April, 2004 we received a communication in letter format from Carmen R. Cabrera (see Attachment 2) indicating we can commence to reopen the program with three additional suggestions. These suggestions are being and/or have been incorporated into the programs administration manual. We understand that all findings have been corrected with our desire to comply with all federal requirements pertaining to the program and with the new staff we are now headed in that direction.

**MINUTES OF CITIZEN PARTICIPATION
COMMUNITY BLOCK DEVELOPMENT GRANT
FUNDING FISCAL YEAR 2004**

The municipal government of Cidra held four (4) public hearing for the purpose of receiving community input on how and where these funds should be spent.

The four (4) public hearings were held on separate dates and times with the purpose of offering the general public various options to attend.

Unfortunately no one appeared at the four (4) hearings. An additional hearing was held during the Section 8 public hearing. At this hearing, where over 150 people attended, we took advantage of the hearing and discussed the CDBG funding for fiscal year 2004. Only a few who attended mainly requested infrastructure improvement in the wards (street re-pavement). Others requested illumination and water improvement in their wards.

Attachment I

TECHNIQUES FOR MONITORING FEDERAL SUBAWARDS:



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1 Origins of Federal Rules for Monitoring Subawards

Federal agencies award billions of dollars every year to state and local governments, colleges and universities and other organizations to administer a myriad of federal assistance programs. Through hundreds of federal programs, these agencies carry out federal mandates and public policies created by executive order of the president or legislation enacted by Congress. For the most part, federal agencies rely on their grant recipients to implement these programs by adhering to program rules and governmentwide policies for administering federal grant dollars — the “strings attached.” Grant recipients have to comply with a plethora of these federal rules, ranging from restrictions on how much “overhead” they can charge to a federal grant, to parameters for the types of scientific study that can be funded with federal research dollars, to the income limits of families whose children can receive subsidized meals at school. Federal agencies use various methods — financial reports, progress reports and audits — to ensure grant recipients’ proper stewardship of federal funds.

In many cases, grant recipients do not administer these programs themselves. Rather, they subaward or “pass-through” some or all of their federal funds to subrecipients that often run the programs, such as when a large university receives federal grant funds to study global climate change and subawards half of the funds to a nonprofit research institute to conduct a large portion of the research program. In this scenario, the university would agree to comply with the terms of the grant agreement as a condition of receiving the federal funds. In turn, the nonprofit subrecipient must comply with the requirements of the subaward agreement that include many (if not all) of the terms of the federal agency/university agreement as well as any other conditions imposed by the university. Even though a grant recipient might pass-through federal grant dollars to subrecipients (sometimes as much as 90 percent of federal funds received), it is ultimately the primary grantee’s responsibility to ensure that federal funds are spent according to the prescribed federal requirements, including any subgranted funds.

Subrecipient Monitoring: New Tool But Old Requirement

For many years, grant recipients (or “pass-through entities”) have had to ensure that their subrecipients adhere to governmentwide and program-specific requirements set forth in the grant agreement. This has been especially true since the devolution of federal grant administration to the states in the early 1980s (also known as “new federalism”). At that time, many federal assistance programs (e.g., the Community Development Block Grant) were revamped so that agencies awarded more federal funds to states and other large organizations that in turn subgranted the funds to smaller recipients. A few key policies were issued to address this increase in subawarded federal funds. The U.S. Office of Management and Budget (OMB) in 1988 revised its grant administration rules for state, local and tribal governments to, among other things, incorporate provisions that reflect this shift in grant administration. OMB later revised its governmentwide rules for universities and nonprofits to include similar provisions. Currently, both the common rule for state and local grant administration and OMB Circular A-110 (grant administration rules for colleges, universities and other nonprofit

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organizations) specifically mandate that federal grant recipients monitor “each program, function or activity” funded with federal grant dollars — including subawards.

With passage of the Single Audit Act in 1984, federal agencies and grant recipients had a new tool — the single audit report — for monitoring and ensuring grantee and subgrantee compliance, respectively. The act required single audits of governments receiving more than \$100,000 in federal funds in a year. (Universities and other nonprofit organizations were not at that time within the purview of the act or its implementing policy, OMB Circular A-128.) Governments that received between \$25,000 and \$100,000 could have either a single audit or an audit “in accordance with federal laws and regulations governing the programs they participate in.” Here, again, these audits of smaller awards were used to review and assess compliance.

But Congress amended the act in 1996 to change the audit coverage in three key ways: by raising the single audit threshold to \$300,000, by applying the act to universities and other nonprofit organizations that had been covered by a hybrid single audit policy since 1990 and by barring grantees from using federal funds to cover the cost of single audits of exempt subrecipients. Provisions in the amended statute and its implementing policy, OMB Circular A-133, *Audits of States, Local Governments and Nonprofit Organizations* (1997), specifically exempt grant recipients and subrecipients that spent less than \$300,000 a year in federal awards from federal audit requirements. Instead, those recipients must make their records available for review by pass-through entities and federal awarding agencies.

From a federal standpoint, the raised audit threshold was an efficient and effective way to concentrate audit coverage on the larger federal awards and subawards, but it placed more of a compliance burden on primary recipients. Recognizing that fewer recipients and subrecipients would be covered by single audit requirements, Congress specifically required pass-through entities to monitor all of their subrecipients. This is especially challenging for recipients whose subrecipients fall below the audit threshold, because there is no single audit report to review. Thus, primary grantees have to use other tools to ensure their subawarded funds are being spent properly. And it is these tools that auditors performing single audits will test (using new guidance in the *OMB Circular A-133 Compliance Supplement*) to determine whether primary grantees are effective in ensuring proper stewardship of federal funds.

Techniques for Monitoring Federal Subawards discusses the variety of compliance monitoring tools that grant recipients and subrecipients can use and provides practical guidance for executing them. Chapter 2 explains the role of the key participants in the subaward process, starting with the pass-through entity’s responsibilities for monitoring subrecipients, as well as vendors and commercial organizations. It also addresses the subrecipient’s various administrative and reporting responsibilities. The chapter concludes with a look at the resources of the federal awarding agency available to the pass-through entity and the subrecipient.

Chapter 3 describes the key provisions of an effective subaward agreement that will achieve monitoring goals. Explaining first the importance of a well-written scope of work and budget, the chapter then describes the various types of program-related and administrative laws and regulations that should be included in the agreement to ensure that subrecipients comply with the necessary requirements while carrying out federal program purposes. It also provides a brief discussion on structuring the agreement.

Chapter 4 provides an in-depth look at the monitoring techniques that pass-through entities and subrecipients have found to be useful. It discusses factors pass-through entities

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should consider before selecting a monitoring activity, describes and compares the various tools available, including single audits, limited-scope audits, onsite visits and document reviews, and provides tips on choosing the best ones.

Chapter 5 addresses a vital part of the monitoring process — effective communication — that is sometimes overlooked or ignored. Looking at the myriad forms communication can take, the chapter discusses everything from the importance of the subaward agreement and federal agency guidance issued at the start of the subaward to the need for ongoing, informal contact between the pass-through entity, subrecipient and federal awarding agency throughout the subaward.

Emphasizing the importance of follow-up, chapter 6 describes the best ways pass-through entities can inform subrecipients about monitoring findings and provides advice to subrecipients on taking corrective action. Chapter 7 reviews the aspects of a pass-through entity's monitoring procedures that auditors will test. It identifies the types of findings auditors might report and describes how to avoid them.

To help make the subrecipient monitoring process easier, *Techniques for Monitoring Federal Subawards* also includes sample subaward agreements, excerpts of OMB circulars and the *Circular A-133 Compliance Supplement*, and a glossary of common terms relevant to subrecipient monitoring issues. These are located in the appendices.

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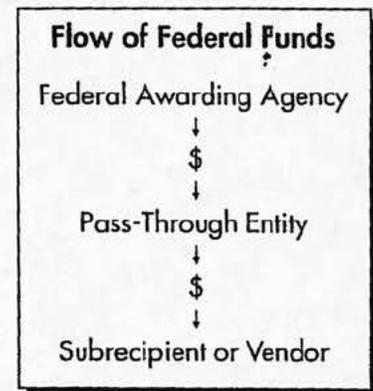
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2 Roles and Responsibilities of Key Participants

Understanding the relationship and responsibilities of the participants involved in the subaward process is essential to creating a successful subrecipient monitoring relationship.

Federal funds originate from a federal awarding agency that is authorized by a grant-enabling statute to develop and administer a federal assistance program. Based on the statute, the federal agency awards federal funds to grant recipients such as state and local governments, colleges and universities, or nonprofit organizations, to carry out the federal program. Some grant recipients perform all of the federal grant activities themselves, but many recipients pass through federal funds either to subrecipients that administer many of the program functions and objectives, or to vendors that provide goods and services under the program (see discussion below).

While the federal funds originate from a federal awarding agency, the participants most directly involved in subrecipient monitoring are the pass-through entity (or primary recipient) and the subrecipient because they are parties to a subaward agreement (see Chapter 3).



Pass-Through Entity Responsibilities

A pass-through entity is responsible for ensuring that all of the federal funds it receives, including those passed through to subrecipients, are used only for program-related purposes as described in the pass-through entity's original grant agreement. But before a pass-through entity makes a subaward, it should verify that the program laws and regulations allow subawards. Some program laws prohibit subawards or limit the amount of funds that grant recipients can pass-through to subrecipients. Other program laws may limit the amount of funds that primary recipients may keep for administrative costs, guaranteeing the majority of the funds are distributed to subrecipients. To determine if subawards are permitted, a pass-through entity should first review its original grant agreement, which may address the question. Beyond the agreement, a pass-through entity can review the program legislation or contact a federal agency program official to get an answer.

Even if a primary recipient is authorized to make a subaward, it should determine if a subaward is the best instrument for awarding federal funds. A subaward is defined as an award of financial assistance in the form of money, or property in lieu of money, made under a grant by a grantee to an eligible subgrantee. Generally, a primary recipient makes a subaward to provide public assistance or achieve a public purpose authorized by a federal law. For example, the Workforce Investment Act (WIA) is designed to provide job training, education and employment services to dislocated workers and other individuals. Therefore, state agencies that receive WIA funds from the U.S. Department of Labor would subaward the funds to nonprofit organizations that actually train individuals to join the workforce.

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However, in some instances it may be more appropriate for a primary recipient to enter into a procurement contract with a vendor. A procurement contract generally is used when a primary recipient buys goods or services for its own use or benefit. For example, a state agency would award a procurement contract to a vendor to buy file cabinets to store its WIA records. While the state agency generally could charge all or part of the cost of the cabinet to the WIA program, it would not be considered a subaward. Still, another example of a contract under a grant would be an agreement between a sponsor of adult day care centers, receiving funds under the U.S. Department of Agriculture Child and Adult Care Food Program, and a food service company to provide meal service for eligible senior citizens and other adults at those day care centers (for a discussion of procurement procedures, see Chapter 3, Page 19).

Once a pass-through entity has determined that it can award federal money to a subrecipient, it should award the funds, usually through a competitive solicitation process, unless the program regulations require otherwise, to an eligible subrecipient. The solicitation should identify the eligibility requirements a subrecipient must satisfy, the activities to be performed, the size of the award, the duration of the program, and refer to any applicable laws, regulations and guidelines. A subrecipient should read the entire solicitation and review the applicable laws and regulations to make sure that it can meet all of the program requirements before it applies for the subgrant.

Subrecipients vs. Vendors

It is not always clear when the pass-through entity should award federal funds to a subrecipient or a procurement contract to a vendor.

A subrecipient is a state or local government, college, university or nonprofit organization that expends federal awards received from a pass-through entity to carry out a federal program. Under a subaward, a subrecipient generally:

- determines who is eligible to receive federal financial assistance;
- has its performance measured against whether the objectives of the federal programs are met;
- has responsibility for programmatic decision-making;
- has responsibility for adherence to applicable federal program compliance requirements; and
- uses federal funds to carry out a program of the organization as compared to providing goods or services for a program of the pass-through entity.

In contrast, a vendor is a dealer, distributor, merchant or other seller providing goods or services that are necessary for conducting a federal program. These goods or services may be for an organization's own use or for the use of beneficiaries of the federal program. Under a procurement contract, a vendor:

- provides goods or services within normal business operations;
- provides similar goods or services to many different purchasers;
- operates in a competitive environment;
- provides goods or services that are ancillary to the operation of the federal program; and
- is not subject to compliance requirements of federal programs.

Because there may be exceptions to these characteristics, pass-through entities should look at the substance of the relationship to determine whether to award a subaward to a subrecipient or a contract to a vendor. Also, because not all of the characteristics may be present, pass-through entities must use their judgment in determining whether an entity is a subrecipient or vendor.

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Pass-through entities should keep in mind that the solicitation process is the first step to ensuring that subrecipients carry out the program activities and requirements. The pass-through entity should review the subrecipient's proposal for completing the project, including its budget for performing the program activities to determine if the entity can properly manage the project and if its proposed costs are reasonable, allowable and allocable under the program regulations and the Office of Management and Budget (OMB) cost principles (Circulars A-21, A-87 and A-122).

State and local governments that are passing through funds to subrecipients are encouraged to use application requirements that are no more detailed or burdensome than those prescribed for federal granting agencies in the grants management common rule.

Pass-through entities should be aware that they cannot make subawards to organizations that have been suspended, debarred or otherwise deemed ineligible to participate in federal assistance programs. (The General Services Administration maintains a list of parties that are suspended or debarred, which is online at: <http://www.arnet.gov/epl> or is available from the Government Printing Office at (202) 512-1800.) They should require all of their subrecipients to submit certifications that they are not suspended, debarred or otherwise ineligible as part of their application.

When a pass-through entity makes the subaward, it must identify the origin of the federal assistance by informing each subrecipient of the *Catalog of Federal Domestic Assistance* (CFDA) title and number, award name and number, award year, if the award is research and development (R&D) and the name of the federal agency. When any of this information is unavailable, the pass-through entity must provide the best information available to describe the federal award. A pass-through entity also must advise subrecipients of any requirements imposed on them by federal laws, regulations and the provisions of contracts or grant agreements, as well as any additional requirements imposed by the pass-through entity. For example, many public policy laws that are included in the original grant from the federal awarding agency to the pass-through entity such as the Americans With Disabilities Act or Section 504 of the Rehabilitation Act of 1973 flow down to the pass-through entity and must be included in the subaward agreement (see Chapter 3).

A grantee that passes through funds to subrecipients is responsible for monitoring their activities to ensure that federal awards are used for authorized purposes in compliance with the federal program laws, regulations and grant agreements and that performance goals are achieved. Monitoring can include document reviews, onsite visits, training or telephone calls (for a complete discussion of monitoring tools, see Chapter 4). Pass-through entities having a single audit performed must prepare a schedule of expenditures of federal awards and, if practical, identify the amount provided to subrecipients from each award. If a pass-through entity has an adequate monitoring system in place, it should be able to identify its subawards in the schedule.

As part of their monitoring responsibilities, pass-through entities must ensure that any subrecipients spending at least \$300,000 in federal awards during the subrecipient's fiscal year have an audit performed in accordance with Circular A-133.

Once monitoring is complete, pass-through entities must communicate the results to their subrecipients, including any problems that need to be corrected, recommendations for improvement and other advice. Similarly, pass-through entities must issue a management decision on audit findings disclosed in a subrecipient's single audit report within six months after receipt of the report and ensure that the subrecipient takes appropriate corrective action.

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In addition, a pass-through entity must consider whether it should adjust its own records as a result of any subrecipient audits.

Finally, the pass-through entity should require each subrecipient to permit the pass-through entity and its auditor to have access to the subrecipient's records and financial statements as necessary for the pass-through entity to comply with Circular A-133 and its monitoring responsibilities.

Checklist of Pass-Through Entity Responsibilities

- ✓ Identify and provide information about federal awards (e.g., CFDA information) to subrecipients.
- ✓ Inform subrecipients about compliance requirements.
- ✓ Monitor subrecipient activities.
- ✓ Ensure subrecipients have single audits, if required.
- ✓ Provide technical advice and training, if necessary and feasible.
- ✓ Issue management decisions within six months on subrecipient single audit findings and ensure subrecipients take corrective action.
- ✓ Consider whether pass-through entity records must be adjusted as a result of subrecipient audits.
- ✓ Require subrecipients to permit the pass-through entity and its auditors access to their records for monitoring and audit purposes.

Special Considerations

In contrast with awards of federal funds to subrecipients, payments for goods and services to vendors using federal program money generally are not subject to Circular A-133 audit or other monitoring requirements. In most cases, the pass-through entity's compliance responsibility for vendors is only to ensure that the procurement, receipt and payment for goods and services comply with laws, regulations and the provisions of contracts or grant agreements. Program compliance requirements normally do not flow down to vendors.

However, when the vendor's performance of its contract affects the pass-through entity's ability to comply with program requirements, the pass-through entity must monitor the vendor's performance to ensure it will satisfy the affected program requirements. For example, under the student financial assistance (SFA) program, many universities contract with service centers to administer student loans. Although the service centers are vendors, they perform a function that is integral to the SFA program objectives such as disbursing SFA funds or cutting off assistance when a beneficiary is no longer eligible. Therefore, the university must ensure that the service center is disbursing funds or performing other duties in compliance with SFA regulations. When these vendor transactions relate to a major program, the scope of the pass-through entity's audit must include determining whether the vendor transactions comply with laws, regulations and the provisions of contracts or grant agreements for that program.

Like vendors, for-profit subrecipients are not subject to Circular A-133's audit requirements. However, both pass-through entities and subrecipients should be aware that the U.S. Departments of Justice and Health and Human Services (HHS) expanded the scope of Circular A-133 to apply to commercial recipients and subrecipients when they adopted the circular into their regulations. HHS permits commercial organizations to choose between a Circular

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A-133 audit or a financial-related audit of the HHS programs performed in accordance with *Government Auditing Standards*.

Nonetheless, pass-through entities must establish requirements to ensure that their for-profit subrecipients comply with the applicable program regulations. A pass-through entity's subaward agreement with the for-profit entity should describe the applicable compliance requirements and the subrecipient's compliance responsibilities. To ensure compliance by for-profit subrecipients, pass-through entities should consider pre-award audits, monitoring during the subaward, and post-award audits.

Primary recipients should incorporate any monitoring requirements into the grant agreement. Primary recipients that subaward a large amount of federal funds (e.g., more than \$300,000) to for-profit subrecipients may want to require that those subrecipients have a Circular A-133 audit or an audit in accordance with *Government Auditing Standards* as a term of the subaward agreement. As an alternative, a primary recipient may require a for-profit subrecipient to have an agreed-upon procedures engagement performed by an independent public accountant (IPA) (see Chapter 4). The IPA would perform certain procedures to test the subrecipient's compliance with various program-related regulations. The primary recipient and subrecipient also should specify in the subaward agreement who arranges and pays for the audit or engagement. (They should also verify that the cost of such audits are chargeable to the federal award.) Additionally, primary recipients may require periodic reports from or make site visits to for-profit subrecipients.

Subrecipient Responsibilities

A subrecipient is awarded federal funds to perform the services or activities described in the subaward agreement. It must ensure that when performing those services or activities that it complies with all of the requirements of the subaward agreement. A subrecipient should set up systems for managing the subaward activities. It should establish a grant accounting system to trace federal fund expenditures to show the money has been spent according to program requirements and produce required financial reports. An accounting system also should help a subrecipient maintain the necessary records that identify receipts, disbursements, assets, liabilities and balances should a pass-through entity, federal awarding agency or some other entity want to review them. Strong internal controls are vital to safeguarding its

Checklist of Subrecipient Responsibilities

- ✓ Administer the grant from award to closeout.
- ✓ Develop internal policies and systems to ensure effective management of federal funds and compliance with public policy requirements.
- ✓ Ensure the organization has a financial management system and any other systems that are appropriate such as procurement and property management systems.
- ✓ Establish a budget of the costs required to perform the program and a method for monitoring actual costs against the budget.
- ✓ Keep abreast of changes in policies, procedures or requirements and advise staff of any changes.
- ✓ Request prior approvals when necessary.
- ✓ Make the most of site visits by the pass-through entity by showing organizational strengths and successes.
- ✓ Prepare necessary reports.
- ✓ Keep the pass-through entity aware and informed about subaward project progress.

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assets, ensuring the reliability of accounting data and complying with management policies and grant terms and conditions.

Beyond the grant accounting system, a subrecipient should consider establishing other grants management systems, including a procurement system for making purchases using subaward money, a property management system and a reporting and recordkeeping system that addresses not only financial records and reports, but also program income and performance requirements.

Once a subrecipient has its grants management systems in place, it should do some self-assessment to ensure that the systems are working. Are the proper records being included in the files? Have the necessary financial and progress reports been submitted to the pass-through entity? Is the subrecipient prepared for a monitoring visit or audit by the pass-through entity or an auditor?

In addition to setting up grants management systems, the subrecipient must ensure it complies with any public policy requirements included in the subaward. Those requirements may include federal requirements such as the Freedom of Information Act and Section 504 of the Rehabilitation Act of 1973 that flow down from the grant agreement between the pass-through entity and the federal awarding agency to the subrecipient (see Chapter 3). The agreement also may include additional requirements imposed by the pass-through entity such as accounting and reporting requirements. To ensure compliance, the subrecipient should establish internal policies (e.g., for hiring and employing individuals with disabilities) and properly train its staff.

The subrecipient also must keep up with and implement any changes in the program requirements that affect its grants administration. To learn about changes to program or agency requirements, a subrecipient can review the *Federal Register*, which is available online at <http://www.access.gpo.gov/> or the CFDA, which is online at <http://www.gsa.gov/fdac/>. Also, the subrecipient should contact its pass-through entity about any changes to program requirements.

If a subrecipient passes through funds it receives to their own subrecipients, they should set up a plan for monitoring those subrecipients' use of the funds.

Subrecipients often must obtain prior approval from the pass-through entity when required by the subaward agreement such as when there is a change in the scope of work or an unexpected large expenditure. Otherwise, the pass-through officials might disallow the costs and the subrecipient would have to absorb the costs of any unallowable activities. Beyond obtaining prior approval, the subrecipient should have regular contact with the pass-through entity (see Chapter 5). If a subrecipient has questions or problems with a subaward, the pass-through entity may be able to provide technical advice to remedy the situation. The subrecipient should also share its successes, such as achieving program goals earlier than expected, with pass-through officials.

By communicating with the pass-through entity on a regular basis, the subrecipient can ask questions about upcoming monitoring visits or required reports and prepare the specific information that the pass-through entity has requested. And once the monitoring visit is complete, the subrecipient will be better able to follow up on any problems identified in their reports or during a visit.

Subrecipients that spend \$300,000 or more in federal awards also must have a single audit performed in accordance with OMB Circular A-133. They must engage the auditor to perform the audit, prepare the necessary documentation, such as the financial statements, and

submit the single audit reporting package, which includes the auditor's opinion and reports, to the pass-through entity and the Federal Audit Clearinghouse. As with monitoring visits, the subrecipient must follow-up on any findings identified during the audit by describing the corrective action it plans to take and actually making the corrections.

Federal Awarding Agency Responsibilities

The federal agency that awarded the funds to the prime recipient has no direct contractual relationship with the pass-through entity's subrecipients. Nonetheless, it wants to confirm that federal funds ultimately are used for program objectives and, therefore, wants to know that the prime recipient is monitoring its subrecipients. The federal agency can rely on the pass-through entity's single audit to determine if the pass-through entity is adequately monitoring its subrecipients. A single audit report with no findings should assure the federal awarding agency that the pass-through entity's monitoring procedures are sufficient. When there are findings, the federal agency can work with the pass-through entity to improve its monitoring procedures. It can suggest additional programs and compliance areas to review. Also, the federal agency can suggest additional monitoring techniques that have been successful for other pass-through entities.

While federal agencies usually do not interact with subrecipients, most subaward agreements give the federal awarding agency the right to review the subrecipient's records and inspect its operations. Federal agencies that are concerned about the use of federal funds by subrecipients may consider performing spot checks of actual subrecipients, particularly with the increase in the single audit threshold and the number of subrecipients that do not have to have a single audit performed. Subrecipients should maintain their records and operations in compliance with the subaward agreement because the federal awarding agency, as well as the pass-through entity, can make site visits or request documents for review.

The federal awarding agency also may be a good source of information for both pass-through entities and subrecipients. Agency officials can answer questions that either a pass-through entity or a subrecipient has about program requirements. For example, they can clarify whether certain activities or costs proposed by the subrecipient are allowable under the subaward. In many instances, subrecipients must obtain prior approval (see Chapter 4) before taking certain actions such as making major changes to the budget. If the pass-through entity has any question about the subrecipient's planned action, it may want to get approval from the federal awarding agency, ensuring that the activity is indeed allowable.

Federal agencies also can inform recipients and subrecipients about any programmatic changes that are made during the subaward, such as setting up a new type of accounting system or completing new reports, and help with their implementation.

A few federal agencies provide guidance on monitoring subrecipients under a particular program. For instance, the U.S. Department of Housing and Urban Development has guidance for monitoring Community Development Block Grant (CDBG) program subrecipients. The guidance emphasizes the areas that a pass-through entity should focus on when monitoring CDBG subrecipients.

In addition to answering questions about specific program requirements, federal agency officials also can help recipients and subrecipients with questions about grants administration in general. Many of the officials are familiar with OMB's grants administration and cost principle circulars and can answer questions about their requirements such as establishing a recordkeeping system or calculating indirect costs.

3 The Subaward Agreement

The subaward agreement potentially is a primary recipient's most important tool for monitoring subrecipient activities. In the agreement, the primary recipient should describe the services or benefits that the subrecipient must provide when administering the federal program. It also should identify the various laws and regulations that the subrecipient must comply with as a condition of the subaward. This includes program-specific requirements such as eligibility criteria and matching obligations, public policy laws for protecting civil rights and the environment, governmentwide administrative mandates affecting the subrecipient's accounting and recordkeeping systems, and state and local laws imposed by the pass-through entity.

The agreement also should describe the pass-through entity's monitoring rights and responsibilities, the areas that the pass-through will monitor, the types of monitoring activities the pass-through entity plans to use such as prior approvals, financial reports and onsite visits and, if possible, the frequency of those activities.

By drafting a clear subaward agreement, pass-through entities can prevent problems and help ensure that subrecipients carry out the requirements of the subaward, work to achieve related performance objectives and comply with the applicable program requirements or strings attached to the subgrant. Additionally, a well drafted agreement will help subrecipients prepare for any monitoring activities because they will know the areas to be covered, the procedures the pass-through entity plans to use and when the activities will occur.

Components of a Subaward Agreement

Each subaward agreement is different because each one involves different organizations, programs and activities. Nonetheless, pass-through entities that make many subawards should consider developing a standard agreement for each of the different federal grant programs that they administer. These agreements can be used for awarding program funds to different subrecipients to provide for more uniform administration of such funds by subrecipients. Pass-through entities must include certain information in the subaward agreement: the CFDA program name and number, the award name and number, the award year, if the award is for research and development, and the name of the federal awarding agency.

If any of this information is unavailable, the subaward agreement must provide the best information available to describe the federal award. A subaward agreement should describe the federal program requirements imposed on the subrecipient by program laws, regulations and the provisions of contracts or grant agreements, as well as any supplemental requirements imposed by the pass-through entity. Auditors performing a pass-through entity's single audit must perform tests to ensure the pass-through entity provided this information to its subrecipients.

As part of the standard language, the agreements generally should incorporate additional basic information such as the names of grantee and subgrantee, the duration of the agreement, contact persons and the funding amount. Beyond this information there are

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several key provisions that a pass-through entity should consider including in the subaward agreement to ensure that subrecipients are aware of their responsibilities and carry out the program properly and to enable the pass-through entity to monitor the subrecipient's activities.

Scope of Work and Budget

Each subaward agreement should include a scope of work, which describes the services or benefits that the subrecipient will provide. It also should clarify where and how the subrecipient will provide the services or benefits. The pass-through entity also should include a proposed budget of the costs of providing those services and benefits.

All of the activities described in the scope of work must conform with the federal program requirements and objectives. For example, the scope of work included in a CDBG subaward for day care services must be consistent with the CDBG program objectives of helping low- and moderate-income persons and supporting community development. The scope of work, therefore, might describe the subrecipient's major tasks such as:

- maintaining the facilities in conformance with applicable laws and regulations;
- informing the moderate- and low-income communities of the availability of services;
- accepting applications and making eligibility determinations for children seeking to enter day care; and
- offering day care services.

With the passage of the Government Performance and Results Act, federal agencies must establish program performance objectives and measure their achievement. Many federal agencies are including such performance requirements in their grant awards, which in turn flow down to subrecipients. Thus, the scope of work may specify certain levels of accomplishment or goals that the subrecipient must achieve for each activity to be performed for a specific time period (e.g., monthly) and the related costs. This could include identifying the number of beneficiaries served. A subaward agreement for job training, for example, might require that the subrecipient provide:

- job training to 30 eligible individuals per month;
- counseling and job search advice to 20 eligible individuals per month; and
- job placement for 15 eligible individuals per month.

Each scope of work is unique. It must reflect the purpose of the federal program and the methods proposed by the subrecipient to administer the federal program. Thus, the scope of work in another CDBG subaward agreement would be completely different if the purpose is to build a public housing facility. It would include a detailed description of the building plans and a work schedule that identifies the major performance benchmarks, associated costs and corresponding dates in the construction process.

The scope of work may be written directly in the agreement or it may be incorporated by reference. Often, the scope of work has been proposed by the subrecipient in its application for the subaward. In such cases, the pass-through entity may incorporate the subrecipient's application, with a few modifications, into the subaward agreement as an exhibit or attachment.

Regardless of whether the scope of work is specifically included in the contract or incorporated by reference, when monitoring a subrecipient, a pass-through entity would

perform procedures to ensure that the subrecipient is performing the activities described in the agreement's scope of work. For example, in the case of the subaward to build the public housing facility, the pass-through entity could request reports on the status of the construction, review documentation such as construction workers time sheets or make site visits to ensure the construction is proceeding as required.

The pass-through entity should incorporate the subrecipient's proposed budget for performing the subaward. The budget identifies various costs associated with administering the subaward such as staff salaries, utilities, supplies, materials and fringe benefits. Using both the scope of work and the budget, the pass-through entity can monitor the subrecipient's expenditures against the proposed budget and the specific performance goals or benchmarks described in the scope of work. It can identify any unanticipated spending patterns that may reflect problems that need to be addressed.

Program Authorizing Statute

The pass-through entity generally should include in the subagreement relevant portions or all of the program's authorizing statute. The authorizing statute establishes the program and describes (usually) the program's purpose and objectives, eligibility requirements, matching requirements and other requirements that are important to administering the program. The level of detail provided in authorizing legislation varies, however. Generally pass-through entities want to ensure that subrecipient's activities conform with the program legislation when performing any monitoring activities.

Program Regulations

Program regulations also flow down from the original grant between the federal awarding agency and the pass-through entity to the subaward between the pass-through entity and the subrecipient. In many instances, the program regulations describe the eligibility requirements, the allowable program activities, describe how the subrecipient should treat program income and include other program-related requirements. However, because program regulations generally are extensive, they usually are incorporated by reference into the subaward agreement. For example, a CDBG subaward agreement might state, "The subrecipient agrees to comply with the requirements of Title 24 of the *Code of Federal Regulations*, Part 570 (U.S. Department of Housing and Urban Development CDBG program regulations)." As with the authorizing legislation, the pass-through entity should give the subrecipient a copy of the relevant provisions of the regulations, and the subrecipient should be sure to review them.

In addition to referencing the program regulations, pass-through entities may incorporate certain important requirements directly into the agreement to ensure that subrecipients comply with them. For example, if a subrecipient is administering a subaward such as the TANF program, the pass-through entity may include the specific eligibility requirements in the agreement, perhaps as part of the scope of work, because of the importance of eligibility determinations to the TANF program.

Public Policy Requirements

Primary grantees should incorporate all public policy requirements in their subaward agreements. These requirements are imposed on grant recipients and their subrecipients by executive order of the president, a law enacted by Congress (either a statute that applies to all

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federal grantees, such as the Drug-Free Workplace Act, or a program authorizing statute such as the Elementary and Secondary Education Act), and regulations issued by federal agencies. Still, there are additional public policies that must be complied with, regardless of whether an organization receives federal funding. Examples of these are the Americans With Disabilities Act and the Civil Rights Act.

Examples of Public Policy Requirements

- Title VI of the Civil Rights Act of 1964 (prohibits discrimination based on race, color or national origin)
- Section 504 of the Rehabilitation Act (prohibits discrimination against disabled individuals by recipients of federal financial assistance)
- Age Discrimination Act of 1975
- Freedom of Information Act (grants public access to federal records)
- Title IX of the Education Amendments of 1972 (prohibits gender discrimination in federally assisted education programs)
- Davis-Bacon Act (sets wage rates for laborers and construction workers working on projects funded by federal assistance)
- Work Hours Act of 1962
- Drug-Free Workplace Act of 1988
- Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970
- National Environmental Policy Act
- Safe Drinking Water Act of 1974
- The Clean Air Act and the Federal Water Pollution Control Act
- Wildlife Protection
- The Coastal Zone Management Act of 1972
- Historic Preservation Act
- Affirmative Action Requirements of Executive Order 11246

These are only a few of the many public policy requirements that could flow down to subawards. Pass-through entities preparing a subaward agreement should include all of the applicable public policy requirements identified in program legislation and regulations.

Additionally, there are public policy requirements or mandates that apply to only certain federal assistance programs or certain activities under those programs. For example, the Uniform Relocation Assistance and Real Property Acquisition Policies Act mandates that federally assisted programs or activities that displace or disturb people or buildings (by, for example, obtaining rights-of way to construct a new road or bridge) provide for relocation assistance to displaced persons or organizations.

Regardless of the source or origin of public policy requirements, primary grantees must ensure that they themselves and their subrecipients comply with them. How should primary grantees determine which requirements apply to subrecipients? First, pass-through entities may want to require their subrecipients to submit a statement of assurance with their subgrant applications that they will comply with the public policy requirements. This statement of assurance could mirror the one organizations submit to federal agencies when applying for federal grant funds. Second, pass-through entities should review their grant agreements with federal agencies to determine the applicable public policy requirements to incorporate into their subaward agreements, as most if not all of them "flow down" to the subrecipient level. Third, primary grantees should review the program authorizing statute and

regulations for any other public policy requirements that may apply. Finally, grantees should contact federal program and other grants officials should they have questions about which requirements apply.

Administrative Requirements

The subaward agreement should describe how the subrecipient should administer the federal program. Generally, state agencies should follow state laws and procedures when administering federal subgrants. While state agencies most often are primary grantees, they can receive subawards from other organizations such as nonprofit entities. For example, the American Red Cross may receive disaster relief training funds from the Federal Emergency Management Agency that it subawards to various state emergency management agencies.

Local governments such as cities, towns and Indian tribal governments that receive subawards should follow the administrative requirements in the Office of Management and Budget's (OMB's) grants management common rule, *Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*. Similarly, colleges and universities or nonprofit organizations that are administering federal subawards must follow the administrative requirements in OMB's Circular A-110, *Uniform Administrative Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals and Other Nonprofit Organizations*.

Certain federal programs such as Medicaid, the National School Lunch program and other entitlement programs, block grants authorized by the Omnibus Budget Reconciliation Act of 1981 and certain grants to local educational agencies (LEAs), are exempt from OMB's administrative requirements. Instead, state and local governments administering such subawards must follow the administrative requirements specified in the program legislation or regulations and, in many cases, rely on state administrative requirements for such areas as accounting, budgeting, procurement and treatment of equipment.

Subaward agreements should specifically state which governmentwide grants management policies apply or even include the text of them. Some pass-through entities are content with inserting a provision in the subaward agreement that requires the subrecipient to follow the applicable federal grants management circular. For example, a nonprofit subrecipient may be required to certify that it will comply with the administrative requirements of Circular A-110 as codified by the federal awarding agency. This may be sufficient when the pass-through entity is dealing with an experienced subrecipient that is familiar with OMB's administrative requirements. However, pass-through entities that frequently have new subrecipients should consider enumerating the subrecipient's various administrative responsibilities in the subaward agreement. Subrecipients are more likely to understand and carry out their responsibilities if they are spelled out in the agreement, rather than in a document that is incorporated by reference.

There are several administrative requirements that the pass-through entity should include in the subaward agreement. For instance, the subaward agreement should describe the type of financial management system that a subrecipient should establish. Generally, pass-through entities should require their subrecipients to maintain a financial management system that provides financial information about the federal program being administered that will satisfy the reporting requirements of the subaward. Additionally, subrecipients should maintain records that adequately identify the source of federal funds and how those funds were spent. The subrecipient's financial management system also should ensure adequate

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internal control over cash management, consistent treatment of costs with the applicable cost principles and sufficient source documentation to support the accounting records. An example of a more detailed financial management provision that could be included in a subaward agreement with a college or university follows:

The subrecipient agrees to comply with OMB Circular A-110 and agrees to adhere to the accounting principles and procedures required therein, use adequate internal controls and maintain necessary source documentation for all costs incurred.

The subrecipient must administer its program in conformity with Circular A-21, *Cost Principles for Educational Institutions*. These principles must be applied for all costs incurred whether charged on a direct or indirect basis.

This provision could be modified for a nonprofit organization or a state or local government agency by incorporating the appropriate grants administration circular and cost principles.

By including detailed information in the subaward agreement about financial accounting, the pass-through entity can prevent confusion among subgrantees. The grants management common rule explains that states must expend and account for federal grant funds in accordance with state laws and procedures for expending and accounting for state funds. In contrast, local governments and Indian tribal organizations, which also are subject to OMB's grants management common rule, must follow the financial management standards described in the administrative circular. Pass-through entities that make awards to state and local government agencies should tailor the subaward agreement to prescribe the financial management requirements appropriate to the type of subrecipient receiving the award.

The subaward also should address how the subrecipient will be paid. OMB's grants administration circulars recommend that the pass-through entity should pay the subrecipient in advance. However, there may be instances when an alternative method of payment is appropriate such as if the subrecipient fails to minimize the time between the transfer of funds from the pass-through entity and their disbursement, or if the subrecipient is considered high-risk. The pass-through entity can insert a provision to pay the subrecipient on a cost-reimbursement basis. Also, if the subaward is for a construction contract, the pass-through entity can select a cost-reimbursement payment method. The pass-through entity may require other forms of payment if required by the type of subaward.

Federal Cost Principles Applicable to Grants

Type of Subrecipient	Applicable Cost Principles
State, local or Indian tribal government	Circular A-87, <i>Cost Principles for State, Local and Indian Tribal Governments</i>
Nonprofit organizations	Circular A-122, <i>Cost Principles for Nonprofit Organizations</i>
Colleges and universities	Circular A-21, <i>Cost Principles for Educational Institutions</i>
Hospitals	U.S. Department of Health and Human Services regulations 45 CFR Part 74
For-profit organizations	<i>Federal Acquisition Regulation</i> 48 CFR Part 31

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Pass-through entities may want to spell out in the subaward that failure by the subrecipient to comply with subaward conditions can result in the withholding of payments.

The subaward agreement should explain that the subrecipient can use the subaward money only for charges that are allowed under the applicable federal cost principles. It also should specify the applicable cost principles. For instance, nonprofit organizations are subject to Circular A-122, *Cost Principles for Nonprofit Organizations*.

The pass-through entity also may want to include provisions that address the subrecipient's procurement system. Subrecipients that are states should follow the same procedures that they use for making procurements with nonfederal funds. The state, however, must ensure that every purchase includes any clauses required by federal statutes and regulations. Local governments and Indian tribal subgrantees must use their own procurement procedures that reflect applicable state and local laws and regulations, as well as federal requirements. In addition, they should review the requirements in OMB's grants management common rule for additional guidance. Nonprofit organizations, colleges and universities also must create their own procurement procedures that prevent the purchase of unnecessary items and otherwise follow the standards in Circular A-110.

The subaward should specify the types of reports that the subrecipient must submit to the recipient, including both financial and progress reports. The agreement should specify when the reports are due and the types of information that they should contain because the pass-through entity will rely on these reports to monitor subrecipient activities and ensure their compliance with the subaward agreement and relevant federal laws and regulations.

The agreement should specify the programmatic records that a subrecipient must maintain and how long those records must be retained. For example, a CDBG subaward agreement between a city and a nonprofit subrecipient may require the recipient to maintain the following:

- records providing a full description of each activity undertaken;
- records demonstrating that each activity undertaken meets the national objectives of the CDBG program;
- records required to determine the eligibility of activities;
- records required to document the acquisition, improvement, use or disposition of real property acquired or improved with CDBG assistance;
- records documenting compliance with the fair housing and equal opportunity components of the CDBG program; and
- financial records required by CDBG program regulations and Circular A-110.

Generally, the agreement should specify that a subrecipient should retain records for a period of three years, unless litigation or audit findings require the subrecipient to keep them for a longer period of time. An example of a record retention provision follows:

The subrecipient shall retain all records pertinent to expenditure incurred under this contact for a period of three years after the termination of all activities funded under this agreement. Records for any displaced person must be kept three years after he/she has received final payment. Notwithstanding the above, if there are litigation, claims, audits, negotiations or other actions that involve any of the records cited and that have

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started before the expiration of the three-year period, then such records must be retained until completion of the actions and resolutions of all issues, or the expiration of the three-year period, whichever occurs later.

In addition to describing the reports and records that the subrecipient should maintain, the pass-through entity should require the subrecipient provide access to any program books and records to not only the pass-through entity but also auditors and federal awarding agency officials.

The pass-through entity should specify in the agreement when the subrecipient must obtain prior approval from the pass-through entity to take certain actions. OMB's grants administration circulars require that subrecipients obtain prior approval for certain activities such as when there is a change in the scope or objective of the project or a transfer of training funds to pay for other expenses. While the pass-through entity can waive certain prior approval requirements, they should consider requiring such prior approvals as a method of monitoring their subrecipients. In fact, subrecipients that are considered high-risk could be required to obtain additional prior approvals. OMB's grants management circulars both authorize pass-through entities to require additional prior approvals when awarding funds to high-risk subrecipients.

The pass-through entity should include a provision giving it the right to monitor subrecipient activities. The provision should describe the areas the pass-through entity will monitor, which generally are the subrecipient's provision of required services or benefits and its compliance with applicable laws and regulations referenced in the agreement. The primary recipient may want to specify in the agreement how many monitoring visits will be required and when those visits will take place, or it may negotiate the details during the subaward period. The subaward agreement also should specify that the subrecipient will have a Circular A-133 audit, if necessary. Only subrecipients that spend \$300,000 or more in federal awards in a year are required to have a single audit.

The pass-through entity should include the period of time that the federal money is available for the subrecipient's use.

Often funds are available only for a limited amount of time, and a subrecipient can charge to the subaward only those costs that are incurred during that period of time. Another administrative area that the pass-through entity should address is the subrecipient's responsibility to obtain matching funds from nonfederal sources. Many federal programs require grant recipients and subrecipients to obtain matching funds from state agencies, nonprofit entities or other private sources.

Other areas that the pass-through entity should consider addressing include the subrecipient's

Administrative Requirements Checklist

The subaward agreement should specify the pass-through entity's and subrecipient's responsibilities for the following administrative requirements:

- ✓ Financial management standards
- ✓ Payment
- ✓ Matching
- ✓ Reporting and recordkeeping
- ✓ Cost principles
- ✓ Period of availability
- ✓ Procurement
- ✓ Program income
- ✓ Real property
- ✓ Equipment
- ✓ Supplies
- ✓ Monitoring
- ✓ Audits

treatment of program income, real property and equipment, patents and copyrights, supplies, and the right of either party to terminate the agreement. Not all of these areas may need to be included in the subaward agreement, however. For example, if the subrecipient is performing a research and development project, it probably will not need to purchase, use or dispose of real property.

Pass-Through Entity Requirements

In addition to incorporating certain federal requirements into the subaward agreement, pass-through entities may impose additional state laws and regulations that the subrecipient must fulfill as part of the subaward process. For instance, subrecipients may have to comply with state environmental laws as well as federal requirements. Also, a state may impose a shorter single audit report submission deadline than is required by Circular A-133 to comply with a state law (e.g., many states have enacted their own single audit requirements and dead-

lines). The pass-through entity may address other issues in the subaward, including arbitration of disputes, insurance and indemnification requirements. Pass-through entities also may impose special conditions on select subrecipients. For example, a subrecipient may have had findings in a certain area such as eligibility determinations on previous audits. In response, the pass-through entity may require as a condition of the new subaward that the subrecipient submit additional documentation regarding its eligibility procedures.

Key Provisions of a Subaward Agreement

- ✓ Subaward identification, including CFDA name and number, award year and awarding agency
- ✓ Scope of work and budget
- ✓ Program authorizing statute
- ✓ Program authorizing legislation
- ✓ Administrative requirements
- ✓ Requirements and conditions imposed by the pass-through entity

Structuring the Agreement

Pass-through entities can structure subaward agreements several ways to incorporate the federal program and cross-cutting requirements. Some pass-through entities might choose to reference all of the federal and state laws and regulations directly in the agreement. In such a case, the subaward agreement is the subrecipient's main source of information regarding the laws, regulations and requirements with which it must comply. The subrecipient is responsible for finding, reviewing and complying with the requirements that are incorporated in and apply to its subaward.

Other pass-through entities require their subrecipients to sign a statement certifying that it will comply with applicable federal (and state) laws and regulations such as the Single Audit Act Amendments of 1996 and Circular A-133, the Civil Rights Act of 1964 or the Davis-Bacon Act. The certification statement, not the subaward agreement, identifies the specific laws and regulations that apply to the subaward. The pass-through entity then incorporates by reference the certifications as part of the overall subaward agreement. (For an illustrative certification statement, see Appendix A, Page 76.)

To assist subrecipients with complying with their subgrant agreements, pass-through entities should consider incorporating additional guidance as part of the subaward agreement. Some pass-through entities develop guidance, in the form of either an attachment to the subaward agreement or a separate handbook that is referenced in the agreement, that explains the

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applicable compliance requirements in understandable language. The guidance may also provide recipients with techniques on how to comply, illustrative examples or sample forms that recipients may have to complete. Pass-through entities may find it more effective and less costly to provide added guidance at the beginning of a subaward to help their subrecipients carry out the program requirements rather than providing the advice as follow-up to audits or monitoring reviews that require corrective action by one or more subrecipients.

4 Effective Monitoring Procedures

There are a variety of methods primary grantees can use to oversee their subrecipients' compliance and performance. Many of these tools are already part of the grant award and management process, while others are common (but not so obvious) actions that can be taken to effectively monitor subawards. Pass-through entities need to determine which ones will work best for their subrecipients. However, what will work for one particular organization may not be the best tool for each and every subrecipient or subaward.

Pass-through entities can look at many of the federal grants management and audit policies as a starting point for developing and choosing monitoring tools. For example, OMB's *Circular A-133 Compliance Supplement* suggests that primary grantees can review financial and progress reports submitted by subrecipients or schedule site visits to review records and observe operations (both of which are chargeable to federal awards). Moreover, primary grantees can review subrecipients' single audit reports or arrange for limited-scope audits of certain areas (e.g., eligibility determinations) of subrecipients that are exempt from having single audits.

Still, there are other tools that are not specifically mentioned (or mandated) in federal rules and policies, but are quite effective. By providing training and technical assistance to subrecipients, for example, primary grantees can work with subrecipients to review operations and records, ultimately to identify and correct any problems early on in the grants management process. Training can also help subrecipients expand or increase their services and improve their performance. Evaluations by third-parties (such as consultants) are also valuable monitoring tools because they can provide cost-effective yet targeted reviews of subrecipient activities.

One of the most important facets of the grant/subgrant process is to stay informed. Pass-through entities and subrecipients alike can use such communication tools as telephone interviews and e-mail to stay abreast of activities and changes to programs and policies relevant to a particular award. Critical to a good pass-through-subrecipient relationship and solid grant performance is effective communication (discussed further in Chapter 5). Open communication can help ensure that the subaward runs smoothly. Moreover, pass-through entities can stay informed by monitoring local and national media (newspapers, magazines, radio and television) for news about their subrecipients. Frequently, news stories and features will shed light on the successes or problems of a nonprofit or governmental subrecipient.

Which tools should a pass-through entity use to monitor its subrecipients? Should it use several of them, all of them, or none of them?

Methods for Monitoring Subrecipient Activities

- ✓ Review single audits
- ✓ Arrange for limited-scope audits
- ✓ Schedule site visits
- ✓ Review subrecipient reports
- ✓ Require prior approval for certain activities
- ✓ Require third-party evaluations
- ✓ Provide technical assistance and training
- ✓ Make telephone calls and use other means of communication such as e-mail
- ✓ Follow subrecipient coverage in the news

Chapter 4: Effective Monitoring Procedures

Which practices are best for a particular type of subrecipient (community organization, local government agency, school district, etc.)?

Before selecting the best monitoring tool for a particular subrecipient, there are several factors a pass-through entity should consider. First, the pass-through entity should determine the purpose of the monitoring activity. Then it should consider the risk of noncompliance associated with the subrecipient. Additionally, the pass-through entity should assess its available monitoring resources.

By identifying the purpose and objectives of the monitoring effort, a pass-through entity can select the best monitoring techniques. Most pass-through entities monitor their subrecipients to ensure compliance with program requirements and identify any problems with the administration and performance of the award. But there are other reasons for monitoring such as identifying whether subrecipients need technical assistance. Monitoring also can be used to follow up on findings identified in an earlier monitoring visit, document review or audit to ensure that corrective action has been taken.

Thus, a pass-through entity that wants to monitor a subrecipient's general compliance with the subgrant agreement may require a more comprehensive monitoring plan that involves the review of financial and progress reports, site visits and, in the case of subrecipients spending \$300,000 or more in federal money, a review of the single audit report. In contrast, monitoring a subrecipient for corrective action of an earlier finding may require more limited monitoring such as reviewing a revised report from the subrecipient.

Pass-through entities also may want to monitor the quality of a subrecipient's performance. For instance, monitoring could focus not only on the number of children receiving breakfast under the U.S. Department of Agriculture's School Breakfast program but on the quality and kinds of food provided. Similarly, a pass-through entity might look beyond the number of individuals trained and employed through WIA programs to the kind of training being provided and the quality of the instructors. These are issues pass-through entities may address when monitoring subrecipients that have single audits conducted because an audit generally does not address quality-of-service issues.

Pass-through entities may be looking for success stories that they can share with other subrecipients in the same program. They also can use monitoring tools to determine if they are doing their job as a pass-through entity. Are there problems or gaps in communication that need to be addressed? Or do they have a good working relationship with the subrecipient?

Once a pass-through entity has identified the purpose of its monitoring efforts, it should also consider the risk that a particular subrecipient will not comply with the applicable requirements in the subaward.

When determining risk, the pass-through entity should consider factors such as the size of the subawards administered by subrecipients and the percentage of the pass-through entity's total federal funds awarded to subrecipients. The greater risk generally will be with those subrecipients that receive larger subawards.

For example, if a pass-through entity subawards a large portion (e.g., 75 percent) of federal awards to 10 subrecipients that each spend less than \$300,000 in federal funds annually, then the pass-through should determine the most effective method for monitoring these funds. To do so, it would balance the cost of monitoring the subrecipients against the size of the subawards and the percentage of the pass-through entity's total federal awards that are passed through. If, for example, the pass-through entity provides the majority of these funds

Special Grant Conditions for High-Risk Subgrantees

Both the grants management common rule and Circular A-110 discuss special treatment for subgrantees that have had one or more of the following problems and are considered "high-risk":

- a history of unsatisfactory performance;
- financial instability;
- an inadequate management system that does not meet the standards mandated in OMB's grants management circulars;
- failure to comply with the terms and conditions of previous subawards; or
- is not otherwise responsible.

A pass-through entity that subawards funds to a high-risk subgrantee can incorporate any of the following special conditions or restrictions into the agreement:

- requiring that subrecipients be paid on a reimbursement basis;
- withholding the authority to proceed to the next phase of the project until the pass-through entity receives evidence of acceptable performance;
- requiring additional or more detailed financial reports;
- requiring the subgrantee to obtain technical or management assistance; or
- establishing additional prior approvals.

If a pass-through entity decides to impose additional restrictions on a high-risk subgrantee, it should notify the subgrantee of the following:

- the nature of the additional restrictions;
- the reasons for imposing them;
- the corrective action that the subgrantee must take before the pass-through entity will remove the restrictions; and
- the method by which the subrecipient can request reconsideration of the restrictions.

Pass-through entities may want to cite the applicable grant administration circular as authority for imposing additional restrictions.

to two subrecipients, it might perform more extensive site visits to the two largest subrecipients and review the documentation supporting the requests for reimbursement from the other eight subrecipients. On the other hand, if a pass-through entity subawards only a small percentage of its federal awards to subrecipients, the risk to the pass-through entity will most likely be low. Therefore, the pass-through entity's monitoring procedures could be more limited.

A pass-through entity also should consider the complexity of the compliance requirements. A more complex program usually will require more monitoring because there is a greater chance of noncompliance with at least some of the program requirements. Also, complex programs often involve larger amounts of federal funds, which invite more attention from pass-through entities. For example, state educational agencies (SEAs) subaward Eisenhower Professional Development funds to LEAs to help improve teacher skills. Each LEA can use the money for a variety of activities such as individual training or group training. States, however, must develop methods for tracking the funds and ensuring all of an LEA's activities support the program's goals. This may require detailed reports and site visits.

Another important factor to consider is an organization's experience with administering a federal subaward. A subrecipient that has administered the same program for several years often will require less monitoring than a subrecipient that is administering an award.

for the first time. A first-time subrecipient may have to submit more financial and progress reports and receive more visits from the pass-through entity than a more experienced subrecipient. How much monitoring is conducted will depend on whether the pass-through entity is familiar with the subrecipient, perhaps from another subaward agreement, or has reviewed the subrecipient's prior single audits, if they are available.

If an experienced subrecipient has made changes in program staff, a pass-through entity may monitor their activities more closely because the new staff members may not be as familiar with the subaward requirements.

The subgrantee's prior monitoring results will have a great influence on future monitoring efforts by the pass-through entity. Thus, if a subrecipient has such problems as submitting incomplete or late reports or not having records available for review during an onsite visit, the pass-through entity most likely will slate that subrecipient for additional monitoring.

The type of award will affect the frequency and type of monitoring that a pass-through entity performs. When a pass-through entity awards a single-year subaward, it has to perform all of the monitoring during the year-long award period. In the case of a multiyear subgrant, a pass-through entity can spread its monitoring effort over the life of the agreement

perhaps concentrating its efforts at the beginning when a subrecipient is new to the program and at the end when the subaward is winding up.

Another important factor a pass-through entity must consider in selecting the best techniques for monitoring its subrecipients is the amount of resources a pass-through entity can devote to subrecipient monitoring, including the cost of the monitoring and the staff and time required.

No grantee has unlimited resources, even for subrecipient monitoring.

Therefore, it must determine the most efficient and effective method to allocate its resources while obtaining assurance that its subrecipients are properly administering their subawards and accounting for program funds.

A pass-through entity most likely will devote more resources to monitor the subrecipients that receive the most funds. For example, an SEA may pass through funds from the School Breakfast, National School Lunch and Special Milk programs to local schools. However, if 60 percent of the funds passed through go to five LEAs while the remaining 40 percent of funds are distributed to 15 other LEAs, the state agency may be willing to pay more to monitor the five LEAs than the remaining 15 LEAs. The state agency may make more onsite visits or provide more training and technical assistance to the subrecipients receiving the larger amount of money.

Similarly, a pass-through entity that has limited staff but many subrecipients may choose to rely primarily on desk reviews of progress reports, reimbursement requests and other records. When onsite visits are necessary to adequately monitor subrecipients, the pass-through entity may send staff to subrecipients on a rotating basis rather than trying

Factors To Consider When Assessing A Subrecipient's Risk

- ✓ Size of the subaward administered by a subrecipient
- ✓ Percentage of a pass-through entity's total federal funds awarded to subrecipients
- ✓ Complexity of the subaward requirements
- ✓ Subrecipient's experience with administering a federal subaward
- ✓ Subrecipient's prior monitoring and audit results
- ✓ Type of subaward (single year v. multiyear)

to visit every subrecipient each year. By visiting each subrecipient once every two or three years, the pass-through entity can monitor one-half or one-third of its subrecipient's each year.

Single Audits

For subrecipients that expend at least \$300,000 a year in federal funds, primary recipients have a valuable monitoring tool at their disposal — the subrecipients' Circular A-133 audit. All state and local governments, colleges and universities, and nonprofit organizations, that expend \$300,000 or more of federal awards in a fiscal year must have a single audit. Primary recipients must ensure that such subrecipients have their audits performed.

However, audits of subrecipients spending less than \$300,000 are not required by Circular A-133 and the cost of these and other audits (e.g., financial statement audits) are unallowable. Pass-through entities, therefore, must rely on other methods to monitor these subrecipients or pay for the cost of the audit with nonfederal funds.

The single audit provides the auditor's opinion on the subrecipient's financial statements. Because many federal assistance programs do not require recipients or subrecipients to have a financial statement audit, a subrecipient's single audit report may provide the pass-through entity with information on the subrecipient's financial statements and any related compliance problems that it might not have otherwise. The single audit also includes a report on the subrecipient's internal controls. While the auditor does not give an opinion on internal controls, his or her report should identify reportable conditions and material weaknesses that relate to the subrecipient's administration of federal programs and that the pass-through entity should ensure are corrected. The single audit report provides information on a subrecipient's compliance with program-specific and cross-cutting (e.g., cost principles) regulations, including a list of findings and questioned costs.

The single audit report also includes the subrecipient's corrective action plan, which identifies how the subrecipient will remedy any problems identified by the auditor and prevent them from recurring. Primary recipients should review the plan to make sure the planned corrective action is allowable and will be made in a timely fashion. They also should determine if the subrecipient needs any technical assistance. In addition, they may want to plan additional monitoring to ensure the corrective action is taken.

Once the single audit is complete, it is the subrecipient's responsibility to submit the final single audit report to the pass-through entity if there are findings affecting the pass-through entity. The pass-through entity can review the audit results for any audit findings and the subrecipient's planned corrective action to determine whether the subrecipient is complying with the subaward requirements.

Reviewing a Single Audit Report

A single audit report contains information about a subrecipient's use of federal money and compliance with program objectives. Primary recipients should review the following components of a subrecipient's single audit report as part of its monitoring efforts:

- ✓ the auditor's opinion on the financial statements;
- ✓ the auditor's report on internal control;
- ✓ the auditor's report and opinion on compliance with laws and regulations that could have an effect on major programs;
- ✓ the schedule of findings and questioned costs; and
- ✓ the subrecipient's corrective action plan.

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The single audit has limitations. Auditors only test a subrecipient's compliance with program requirements for "major programs." Major programs include the subrecipient's larger programs and programs which the auditor determines have a higher risk of noncompliance. Smaller programs and low-risk programs are excluded from the audit and may be audited as infrequently as once every three years.

Additionally, the auditor's testing is required to cover only 50 percent of the subrecipient's programs although, in many cases, auditors test closer to 90 percent of the programs. Therefore, there is the potential for many programs to go unaudited. Moreover, subrecipient single audit reports usually are not available until nine months after the end of the subrecipient's fiscal year. If there are problems, the pass-through entity may not be able to correct them before they are repeated.

In most instances, pass-through entities that review single audit reports from their subrecipients still perform additional monitoring such as site visits or document reviews. In fact, if a pass-through entity's only method of monitoring a subrecipient is reviewing its single audit report, it risks a finding in its own single audit report for failure to adequately monitor its subrecipients.

Some pass-through entities choose not to rely on the single audit as a monitoring tool at all, preferring instead to rely on their own additional desk reviews and onsite visits. These pass-through entities can monitor areas of a program that an auditor would not test, such as quality-of-service issues (e.g., appropriateness of the service provided). Additionally, they can look at programs administered by a subrecipient that are not tested as part of the single audit either because they are too small or they are not high-risk. Early identification of problems is another incentive for pass-through entities to do additional monitoring. Rather than waiting nine months to learn that one or more subrecipients have been charging certain costs incorrectly because of poorly written program guidance, the pass-through entity can identify and remedy the problem before it leads to larger unallowable costs that must be recovered from the subrecipient or possibly the pass-through entity.

Other pass-through entities rely on the single audit report to monitor their subrecipients' activities, but also perform supplementary monitoring. If a subrecipient's single audits regularly report no findings affecting its subawards, then the pass-through entity may feel comfortable relying more heavily on the single audit results and less so on its supplementary monitoring activities to ensure compliance. In contrast, if a subrecipient's single audits report findings that affect the pass-through entity's awards, the pass-through entity may increase its monitoring activities — performing additional visits and reviewing additional reports. Pass-through entities can plan their monitoring activities accordingly.

Still other primary grantees scale back their monitoring of subrecipients that must have single audits (organizations spending at least \$300,000 annually). Instead, they concentrate their resources on those small subrecipients that are exempt from Circular A-133's audit requirements. Therefore, it is important that subrecipients let their pass-through entities know what their total federal expenditures will be and thus whether they will have a single audit performed (see Chapter 5).

Limited-Scope Audits

Pass-through entities that award funds to subrecipients that are exempt from single audit requirements should consider arranging for limited-scope audits to monitor those subrecipients. The cost of a limited-scope audit is allowable only if the subrecipient has not

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had a single audit. Primary grantees would have to pay for (using nonfederal funds) limited-scope audits of subrecipients that have single audits performed.

A pass-through entity would hire an auditor to perform the limited-scope audit because such audits only include agreed-upon procedures engagements performed in accordance with either generally accepted auditing standards (GAAS) or attestation standards. They must be paid for and arranged by the pass-through entity and not the subrecipient. Pass-through entities should note that audits are limited to the following types of compliance requirements:

- activities allowed or unallowed;
- allowable costs/cost principles;
- eligibility;
- matching, level of effort and earmarking; and
- reporting.

When a primary grantee hires an auditor to perform a limited-scope audit, the primary grantee must determine the procedures to be used and compliance areas to be reviewed. The pass-through entity will need to base these determinations on its needs, as well as the needs of other audit report users such as federal awarding agencies.

For example, if an auditor performs a limited-scope audit of reports the subrecipient submitted, the pass-through entity would have to specify that the auditor test whether the subrecipient's records support the information included in the reports.

Arranging for an Agreed-Upon Procedures Engagement

GAAS defines an agreed-upon procedures engagement as one in which an accountant is engaged by a client to issue a report of findings based on specific procedures performed on the specific subject matter of specified elements, accounts or items of a financial statement. The client engages the accountant to assist users in evaluating specified elements, accounts or items of a financial statement as a result of the needs of the users of the report. Because users require that findings be independently derived, the services of an accountant are obtained to perform procedures and report his or her findings. The users and the accountant agree upon the procedures to be performed by the accountant that the users believe are appropriate.

Because users' needs may vary widely, the nature, timing and extent of the agreed-upon procedures may vary as well; consequently, the users assume responsibility for the sufficiency of the procedures since they best understand their own needs. In an agreed-upon procedures engagement performed in accordance with GAAS, the accountant does not perform an audit and does not provide an opinion or negative assurance relating to the fair presentation of the specified elements, accounts or items of a financial statement. Instead, the accountant's report on agreed-upon procedures should be in the form of procedures and findings.

Similarly, AICPA's attestation standards state that an agreed-upon procedures engagement is one in which an accountant is engaged by a client to issue a report of findings based on specified procedures performed on the subject matter of an assertion, which is any declaration or set of declarations taken as a whole by a party responsible for it. Under the attestation standards, the client engages the accountant to assist users in evaluating an assertion as a result of the needs of the users of the report.

A limited-scope audit may be a cost-effective technique to monitor a specific area of compliance for a group of subrecipients that are exempt from single audit rules. For instance, a pass-through entity that subawards program funds for which eligibility determinations are very important (e.g., the TANF program) must ensure that subrecipients are complying with the eligibility regulations. A pass-through entity can hire an auditor to perform an agreed-upon procedures engagement of its subrecipients' compliance with eligibility requirements, rather than having to train their own personnel. Using the criteria defined by the pass-through entity, the auditor would perform a targeted evaluation and provide a report for each subrecipient that describes the procedures performed and any findings.

For-Profit Subrecipients

Pass-through entities that subaward funds to for-profit organizations can arrange for these subrecipients to have an agreed-upon procedures engagement. Because for-profit subrecipients are not subject to Circular A-133, the engagement could cover compliance areas other than the five specified in the circular (e.g., eligibility, reporting).

If there are a large number of subrecipients to be monitored, the pass-through entity can enter into one auditing contract (or maybe a few to spread the work) to perform agreed-upon procedures for all subrecipients administering the program in question. The auditing firm can perform the engagements on a cyclical basis. For example, if a pass-

through entity hires the firm to perform procedures on 60 subrecipients spending less than \$300,000, the firm and pass-through entity could agree to a three-year monitoring cycle. The firm would perform procedures on one-third of the subrecipients each year, which would provide the pass-through entity with some assurance about compliance with eligibility determination rules. In addition, the pass-through entity could direct the firm to perform procedures on higher-risk subrecipients (e.g., more incidents of noncompliance) more frequently.

Onsite Visits

Onsite visits can be a useful tool for pass-through entities to ensure that subrecipients are complying with program requirements. During an onsite visit, a pass-through entity can:

- inspect a subrecipient's facilities and operations to ensure they comply with governmentwide and program requirements (e.g., eligibility determinations, Section 504 of the Rehabilitation Act of 1973);
- interview staff to ensure they are informed of and carry out program policy and regulations;
- review documentation and records such as invoices and payrolls that support subrecipient reports;
- view delivery of program services such as training;
- become familiar with subrecipient operations and staff; and
- learn about the subrecipient's progress and problems.

Many subaward agreements include provisions for onsite visits. Based on the type of subaward, a pass-through entity should be able to foresee if site visits will be necessary. The agreement should specify the number of visits that the pass-through will make to enable both

the pass-through and the subrecipient to plan for those visits (see Appendix A, Page 79). The subaward agreement, however, does not have to specify the time or nature of the onsite reviews. Primary grantees and their subrecipients must negotiate the details of when the visits occur once the agreement is signed. Subrecipients should be aware that pass-through entities may make additional visits if they feel it is necessary such as to check on whether the subrecipient corrected a previously identified problem. For example, a monitoring visit may reveal a subrecipient receiving CDBG funds is building a facility that does not comply with the Americans With Disabilities Act. The pass-through entity would most likely schedule a follow-up visit to ensure that the facility has been modified to accommodate disabled individuals.

Planning Onsite Visits

There are several steps to planning an onsite visit. A pass-through entity and subrecipient need to plan when the visit will take place. They also need to schedule the actual visit and develop an agenda for the meeting. Both parties need to review pertinent documents and files that are relevant to the subaward.

Pass-through entities and their subrecipients need to plan when the pass-through entity will make its monitoring visit. The timing of the visit will depend on several factors such as the availability of pass-through entity staff and resources and the areas that the pass-through entity plans to review during its visit (e.g., financial transactions, environmental records).

Exactly when the onsite visit will occur also will depend on the type of subaward. If a subrecipient administers an award that is renewed every year (for example, a school district that receives school breakfast and lunch program funds), the pass-through entity may schedule a regular visit for each recipient. In the case of a school district, the pass-through entity probably would schedule the visit during the school year, so it could review the school's records, conduct interviews with school staff and ensure that only eligible students are receiving the subsidized meals.

In contrast, if a subrecipient has a grant for a one-time project such as building low-income housing a pass-through entity may schedule monitoring visits at different intervals of the subaward period, as time and resources permit. For example, when a subrecipient buys a parcel of land on which it will build low-income housing, the primary grantee may visit to inspect the location. As the building progresses, the pass-through entity might make visits to ensure the construction actually is proceeding, the builder is

When Are Onsite Visits Appropriate?

Onsite visits are more costly than some other types of monitoring because they require staff to prepare for the visit, travel to the subrecipient and review its operations. Many pass-through entities opt for onsite visits for subawards that require closer supervision:

- programs with complex compliance requirements;
- high dollar programs;
- a program newly authorized by Congress;
- programs with prior audit or monitoring findings;
- high profile programs in which the federal awarding agency, Congress or the public have an interest;
- programs administered by inexperienced subrecipients or subrecipients that have inexperienced staff;
- programs where the subrecipient has requested an onsite visit; and
- subrecipient sites that have not been visited recently.

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following the subrecipient's plans, construction is completed and the facility complies with program requirements.

Lastly, pass-through entities may want to consider making unscheduled visits to high-risk subrecipients to ensure they comply with program requirements throughout the term of the subaward.

A pass-through entity and subrecipient may want to establish a schedule that will enable both organizations to prepare for onsite visits. The schedule could list specific dates, particularly if the subaward involves regular activities (e.g., job training) that the pass-through entity can monitor any time. Or the schedule could be linked to specific events such as the benchmarks in a building's construction. If a pass-through entity does establish a schedule for its visits, it should allow for a few changes to accommodate unplanned events. Some pass-through entities and subrecipients, however, may prefer to negotiate the details of each visit as the need arises.

When the time for the monitoring visit draws near, a pass-through entity should schedule the exact time first with a telephone call, followed by a letter of confirmation (see

Georgia Gets a Blue Ribbon for its CDBG Monitoring Program

In the early 1980s, the state of Georgia Department of Community Affairs initiated a monitoring process that involved ongoing reviews of local CDBG recipients through one- or two-day local visits. During these visits, staff reviewed activities such as procurement and financial management practices and inspected construction in progress. Making timely visits and providing advice before the local government proceeds on a particular project has proved to be effective in ensuring compliance with program requirements and also in keeping paperwork to a minimum.

Over the years, Georgia has continued to use this approach, making minor adjustments to make the system more efficient. The key to its success is an experienced staff of program representatives who are continually visiting subrecipients. The staff report findings and help ensure that they are promptly resolved. By doing so, Georgia has kept major instances of noncompliance to a minimum.

Georgia deploys its program representatives in the field and emphasizes frequent one-on-one contacts with representatives of local governments. Written correspondence is kept to a minimum, and the strategy of making several short visits to each local government rather than one comprehensive monitoring visit to review program compliance has proven to be effective. Program representatives are in a position to counsel local government officials at critical stages of the development process. They monitor all activities in all applicable compliance areas and make an immediate verbal report to the locality. Letters are written only to notify the local government of a finding.

The program representatives have worked with the same local governments over several years and have become familiar with each community's needs. They can also advise local government officials about which CDBG activities have the most potential to meet their needs. In some instances, the program representatives have dissolved barriers between state and local governments and have become trusted advisers on community development matters.

As a result of these monitoring practices, Georgia has corrected most of the instances of noncompliance quickly – before they became serious.

Source: U.S. Department of Housing and Urban Development, Blue Ribbon Practices in Community Development, <http://www.hud.gov:80/ptw/docs/ga14.html>.

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Figure 1, below). The letter should contain the following information to help a subrecipient prepare for the visit:

- date of the visit;
- purpose;
- agenda;
- individuals to be interviewed; and
- documents and operations to be reviewed.

Figure 1 Onsite Monitoring Confirmation Letter

To: [insert subrecipient contact name]
From: [insert pass-through entity contact name]
Date: [insert date]
Subject: [Onsite Monitoring Visit for Community Development Block Grant (CDBG) program]

This memorandum is to confirm the CDBG program onsite monitoring visit of the CDBG subaward agreements, [insert agreement numbers], to be conducted [insert date and time of site visit].

I will review, at a minimum, the files indicated below, although I may choose to review any and all CDBG-related documents, if appropriate:

- application and contract;
- financial management;
- procurement and contracting;
- Americans With Disabilities Act/Section 504 of the Rehabilitation Act of 1973;
- construction contracts;
- labor standards;
- environmental review records; and
- civil rights.

Please ensure that all files are available for review during this onsite visit and that all personnel responsible for this contract can meet with me to respond to questions or concerns. Such personnel includes the finance director, the program administrator and any other personnel that deals with the documents identified above.

If possible, I would prefer a room where I can review files before or after the visit to the program site. Prior to the conclusion of the visit, I will discuss any questions and concerns with you and attempt to resolve as many issues as possible.

Should you have any questions please contact me at [insert telephone number].

To better plan their monitoring visits, pass-through entities may want to develop program-specific monitoring policies and checklists for use by their staffs. By using the checklists, the staff can perform more efficient visits, reviewing only relevant administrative and compliance areas, and apply uniform monitoring procedures to its subrecipients. When preparing the checklist, the pass-through entity should include all of the areas it needs to review to get an assurance that the subrecipient is meeting its obligations under the subaward agreement. (Pass-through entities that monitor small awards to only a few subrecipients may not need to develop policies to ensure uniformity.) However, pass-through entities should build some flexibility into their policies to allow for the

unexpected. Areas that a pass-through entity should consider covering in their checklist include:

- accounting and financial management policies and procedures, including internal control systems;
- personnel policies and procedures;
- procurement policies and procedures;
- property records and inventory;
- environmental review record;
- labor policies and procedures;
- Americans With Disabilities Act and Section 504 of the Rehabilitation Act of 1973 compliance;
- eligibility determinations;
- program income records and reports; and
- other program-related compliance areas that are material to the subaward.

By reviewing some or all of these areas, a pass-through entity can verify during an onsite visit that a subrecipient's records support the periodic status reports provided to the pass-through entity and confirm the subrecipient's compliance with program requirements.

To help subrecipients prepare for their onsite visit, pass-through entities may find it more efficient to give the subrecipients a copy of the checklists so they know what the pass-through entity will be reviewing and can adequately prepare for the visit. It also may be less costly to provide the subrecipients with this guidance at the beginning of the subaward process rather than at the end of the process as follow-up advice in a management decision on a finding. Additionally, if there are any forms that the subrecipient may have to complete during the visit, the pass-through entity may want to provide those to the subrecipient in advance. The subrecipient can complete the forms and have them ready at the time of the visit.

Conducting the Onsite Visit

When the visit begins, a pass-through entity and subrecipient should discuss the purpose of the visit, the documents to be reviewed and the people to be interviewed. While all of this information is set out in the monitoring visit letter, the pass-through entity or subrecipient may want to make changes to the agenda. For example, the subrecipient may have identified a problematic area that requires the pass-through entity's technical advice.

During an onsite visit, a primary grantee has an opportunity to review a subrecipient's provision of program services (e.g., providing job training, building housing) on a first-hand basis. The pass-through entity can confirm that the subrecipient is providing the services in compliance with program regulations (e.g., the subrecipient is providing job training only to individuals that meet certain age or income requirements). To do this, the pass-through can interview both beneficiaries and staff. It can also review the documents and records related to the program areas it wants to monitor (e.g., financial and accounting systems, program-specific requirements) using the checklists it developed (see Figure 2, Page 35).

At the completion of the site visit, the pass-through entity should conduct an exit conference to clarify any questions and share its initial findings and recommendations.

Figure 2

Community Development Block Grant Program

Financial Management System

Onsite Monitoring Form

Recipient: _____ Monitoring Date: _____

Agreement Number: _____ Reviewer: _____

A. Pre-Visit File Check

1. Number of requests for payment: _____ 2. Amount requested to date: _____

3. Total disbursed to date: _____ 4. Balance: _____

5. Follow-up needed from prior visits or audits: _____

B. Onsite Visit

Ask for a copy of the revenue and expense ledger for this contract. Expense ledger should be itemized to show each expenditure. Note that this will likely cover two to three fiscal years, and we need ledgers for the entire length of the contract. Ledgers can be requested in the appointment memorandum, so they will be available at the onsite visit. Ledgers should be reviewed before sending the follow-up letter.

	Yes	No	N/A	Comments
1. Internal Controls				
a. Title of person(s) who approves expenditures:				_____
_____				_____
b. Title of person(s) who signs checks:				_____
_____				_____
c. Title of person(s) responsible for general ledger transactions:				_____
_____				_____
2. Disbursements (random sample of two requests for payment)				
a. Request No. Amount:				_____
Date received:				_____
Date deposited:				_____
All funds disbursed within 10 days:	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
b. Request No. Amount:				_____
Date received:				_____
Date deposited:				_____
All funds disbursed within 10 days:	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
c. No improper costs incurred prior to release of funds date	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____

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Figure 2 (continued)

	Yes	No	N/A	Comments
3. Source Documentation				
Files should contain original records, invoices, vouchers and documents – select two items and trace through the system.				
<u>Request for Payment No.</u>				
<u>Amount</u>				
<u>Item</u>				
a. _____				_____
b. _____				_____
c. approval to pay on each	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
4. CDBG Funded Staff				
a. Names/Title				
_____				_____
_____				_____
_____				_____
b. Engaged in activities as in application	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
c. Time records signed by employee and supervisor	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
5. Program Income				
a. Records indicate source, date, amount and deposit account	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
b. Disbursements for eligible activities	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
c. Program income spent prior to additional requests for funds (unless revolving loan fund)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
d. Payments timely	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
6. Property Management				
a. Fixed assets ledger lists all assets acquired with CDBG funds and includes: description, serial identification number, acquisition date, invoice, unit, cost and total cost, location, use, condition, documentation of disposition	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
b. Inventory agrees with subrecipient's application	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
7. Other Items				
a. Indirect cost documentation, if applicable	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
b. Audits: file contains and identifies location of all audits and related correspondence	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____
c. Follow-up actions from prior visits or audits were implemented	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	_____

Follow-Up

The pass-through entity should prepare a written report of its findings and recommendations following the site visit. The report should address each area that the pass-through entity reviewed as part of the monitoring visit (e.g., financial management, environmental policies and procedures, program compliance). The report should be added to the subrecipient's file. In the final monitoring report, the pass-through entity should list all of the monitoring checklists it used during the visit, so when staff prepare for future monitoring efforts (e.g., desk reviews, audits, onsite visits), they can find all of the records pertaining to the subrecipient.

The pass-through entity also should prepare a follow-up letter to the subrecipient that discloses any monitoring findings, makes recommendations to correct those findings, offers technical assistance if necessary and requests a corrective action plan (see Chapter 6). To ensure the subrecipient corrects the problem, the pass-through entity might schedule additional monitoring visits or request certain reports. For example, if a subrecipient built a facility using federal funds, and the facility did not meet federal accessibility standards, the primary recipient's management may need to make a return visit to verify that the subrecipient made changes to the facility.

Document Reviews

Pass-through entities can perform desk reviews of documentation and reports as a method for monitoring subrecipient activities. Desk reviews generally are less expensive than other monitoring methods (e.g., limited-scope audits) because pass-through entity staff do not have to travel or gather data, and they can target specific areas of compliance. By performing document reviews, a pass-through entity can determine whether a subrecipient is complying with financial, environmental, labor and other compliance requirements.

Subaward agreements generally authorize the pass-through entity to perform document reviews. For example, subrecipients must submit all requests for payment to the pass-through entity for approval and often have to include supporting invoices or receipts. Many pass-through entities also require periodic reports (e.g., quarterly or annually) from their subrecipients that include financial information or performance data with respect to the goals and objectives of the federal programs. Additionally, the subaward should contain provisions that give the pass-through entity access to all program-related materials for the purposes of reviews, site visits and audits.

Financial Monitoring

Most pass-through entities should develop some financial monitoring procedures to ensure that subrecipients:

- request the correct amount of federal funds;
- use the funds for program-related purposes;
- ensure only authorized personnel request funds;
- deposit funds in the proper account; and
- otherwise properly account for federal funds spent.

For example, pass-through entities monitoring subrecipient payments can require their subrecipients to identify in advance the official(s) authorized to request federal reimbursement (e.g., providing a signature card for the pass-through entity's files) and the bank or other institution where the pass-through entity will make any deposits. In addition, when any subrecipient makes a reimbursement request, the pass-through may want to require the subrecipient to provide not only a request for the money but an explanation (including supporting documentation such as payroll records) of how funds will be used (e.g., to pay subcontractors). Using this information, the pass-through entity would be able to verify not only that the proper parties requested the funds but also that the funds were being used for allowable program purposes. For example, if a subrecipient requests money to pay a subcontractor, the pass-through entity could verify against the documentation that the subcontractor is not debarred or suspended and that it actually performed the required work.

Monitoring Compliance With Other Requirements

Pass-through entities can perform document reviews to monitor subrecipient compliance with program-specific requirements throughout the subaward period, identifying problems and correcting them early on. Some pass-through entities begin performing desk reviews when a subrecipient submits a grant application, checking whether the subrecipient has included all of the necessary information. When an organization receives a subaward, the pass-through can monitor all facets of the subaward using desk reviews. For example, if a subrecipient receives a Community Development Block Grant (CDBG) subaward for a public housing facility, the pass-through entity can monitor every phase of the construction and completion of the facility. When the subrecipient purchases the land for the facility, the pass-through entity should ensure the subrecipient is complying with environmental regulations and notice requirements. For example, the pass-through entity may review and approve the necessary public notices to ensure they contain the language required by the program regulations and are published within the required time period. When the subrecipient hires construction contractors, the pass-through should consider reviewing the subrecipient's internal procurement procedures, the request for proposal that was issued and the construction agreement. In addition, the pass-through entity may want to review the subcontractor's payroll records to ensure compliance with Davis-Bacon Act requirements. Once the facility is completed and running, the pass-through entity may want regular reports on the facility's maintenance.

Planning Document Reviews

Both pass-through entities and subrecipients can plan for upcoming document reviews to make them more efficient and mitigate problems. Those pass-through entities that administer several federal programs may want to develop a monitoring cycle, performing document reviews of different programs at different times of the year. For example, a pass-through entity that administers the U.S. Department of Agriculture's Summer Food Service Program for Children, which provides meals for low-income children during the summer, might begin desk reviews in the spring when subrecipients are in their planning stages, increase the reviews over the summer as the program is performed and conduct any follow-up during the fall and winter months. At the same time, the pass-through entity may gear up desk review monitoring for other programs such as

the School Breakfast Program, which provides breakfast to low-income children during the school year, when it is finishing up work on the Summer Food Service program subrecipients. By establishing a monitoring cycle, pass-through entities and subrecipients should go through the monitoring process more efficiently. Pass-through entities can allot the necessary resources and staff to perform the desk reviews and any necessary follow-up, and subrecipients can prepare and provide the proper reports and documents to the pass-through entities within established time frames.

Financial and Progress Reports

Beyond looking at a subrecipient's specific transactions (e.g., a request for reimbursement or a request for proposal), many pass-through entities require subrecipients to prepare periodic financial or progress reports.

The financial reports usually provide an overview of the subrecipient's financial status and include information concerning the subrecipient's total expenditures and program income. Some federal agencies require subrecipients to complete certain financial reporting forms such as standard form SF-269, *Financial Status Report*, (see Figure 3, Page 40) or an agency-specific form. However, most federal agencies allow the pass-through entity to develop its own financial reporting form. In many instances, pass-through entities require more detailed information than is called for by SF-269 such as a line item comparison of budgeted and actual expenditures. When developing a financial reporting form, a pass-through entity should consider what information it needs and how it will use the information to evaluate a subrecipient's progress.

A subrecipient's progress report explains the subrecipient's progress toward achieving subaward goals and objectives (see Figure 4, Page 42). (The goals and objectives often are described either in the subaward agreement, reference regulations or the subrecipient's original application, which usually is incorporated into the subaward.) While a few federal agencies have developed program reporting formats for use by subrecipients, most pass-through entities must develop their own. Circular A-110 and the grants management common rule both state that performance reports should include the following information:

- a comparison of actual accomplishments with the goals and objectives established for the period;
- reasons why goals were not met; and
- other pertinent information, including analysis of cost overruns or high unit costs.

When reviewing subrecipient financial reports, the pass-through entity should make sure that the information is accurate and complete. Has the subrecipient provided all of the requested information? Do all of the figures add up? For example, if a subrecipient is paid in advance, the pass-through entity should verify that the amounts drawn down by the subrecipient match with the actual expenditures it reported. The pass-through entity also should compare the subrecipient's actual expenditures to those budgeted. Discrepancies may indicate problems that should be followed up on if the subrecipient is spending money either too quickly or too slowly.

As with the financial reports, the pass-through entity should review subrecipient progress reports to determine if adequate progress is being made toward the subgrant goals and objectives. If there are problems, determine whether any follow-up action is needed.

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Figure 3

FINANCIAL STATUS REPORT (Long Form)

(Follow instructions on the back)

1. Federal Agency and Organizational Element to Which Report is Submitted		2. Federal Grant or Other Identifying Number Assigned By Federal Agency		OMB Approval No 0348-0039	Page of pages
3. Recipient Organization (Name and complete address, including ZIP code)					
4. Employer Identification Number		5. Recipient Account Number or Identifying Number		6. Final Report <input type="checkbox"/> Yes <input type="checkbox"/> No	
7. Basis <input type="checkbox"/> Cash <input type="checkbox"/> Accrual					
8. Funding/Grant Period (See instructions) From: (Month, Day, Year)		To: (Month, Day, Year)		9. Period Covered by this Report From: (Month, Day, Year)	
To: (Month, Day, Year)					
10. Transactions					
		I		II	
		Previously Reported		This Period	
				III	
				Cumulative	
a. Total outlays					
b. Refunds, rebates, etc					
c. Program income used in accordance with the deduction alternative					
d. Net outlays (Line a, less the sum of lines b and c)					
Recipient's share of net outlays, consisting of:					
e. Third party (in-kind) contributions					
f. Other Federal awards authorized to be used to match this award					
g. Program income used in accordance with the matching or cost sharing alternative					
h. All other recipient outlays not shown on lines e, f or g					
i. Total recipient share of net outlays (Sum of lines e, f, g and h)					
j. Federal share of net outlays (line d less line i)					
k. Total unliquidated obligations					
l. Recipient's share of unliquidated obligations					
m. Federal share of unliquidated obligations					
n. Total Federal share (sum of lines j and m)					
o. Total Federal funds authorized for this funding period					
p. Unobligated balance of Federal funds (Line o minus line n)					
Program income, consisting of:					
q. Disbursed program income shown on lines c and/or g above					
r. Disbursed program income using the addition alternative					
s. Undisbursed program income					
t. Total program income realized (Sum of lines q, r and s)					
11. Indirect Expense		a. Type of Rate (Place "X" in appropriate box)			
		<input type="checkbox"/> Provisional		<input type="checkbox"/> Predetermined	
		<input type="checkbox"/> Final		<input type="checkbox"/> Fixed	
		b. Rate	c. Base	d. Total Amount	e. Federal Share
12. Remarks: Attach any explanations deemed necessary or information required by Federal sponsoring agency in compliance with governing legislation.					
13. Certification: I certify to the best of my knowledge and belief that this report is correct and complete and that all outlays and unliquidated obligations are for the purposes set forth in the award documents.					
Typed or Printed Name and Title				Telephone (Area code, number and extension)	
Signature of Authorized Certifying Official				Date Report Submitted	

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269-104

Standard Form 269 (Rev. 7-97)

Prescribed by OMB Circulars A-102 and A-110

200-498 P.O. 139 (Face)

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Figure 3 (continued)

FINANCIAL STATUS REPORT (Long Form)

Public reporting burden for this collection of information is estimated to average 30 minutes per response, including time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding the burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to the Office of Management and Budget, Paperwork Reduction Project (0348-0039), Washington, DC 20503.

PLEASE DO NOT RETURN YOUR COMPLETED FORM TO THE OFFICE OF MANAGEMENT AND BUDGET.

Please type or print legibly. The following general instructions explain how to use the form itself. You may need additional information to complete certain items correctly, or to decide whether a specific item is applicable to this award. Usually, such information will be found in the Federal agency's grant regulations or in the terms and conditions of the award (e.g., how to calculate the Federal share, the permissible uses of program income, the value of in-kind contributions, etc.). You may also contact the Federal agency directly.

Item	Entry	Item	Entry
1, 2 and 3.	Self-explanatory.	10b.	Enter any receipts related to outlays reported on the form that are being treated as a reduction of expenditure rather than income, and were not already netted out of the amount shown as outlays on line 10a.
4.	Enter the Employer Identification Number (EIN) assigned by the U.S. Internal Revenue Service.	10c.	Enter the amount of program income that was used in accordance with the deduction alternative.
5.	Space reserved for an account number or other identifying number assigned by the recipient.	Note:	Program income used in accordance with other alternatives is entered on lines q, r, and s. Recipients reporting on a cash basis should enter the amount of cash income received; on an accrual basis, enter the program income earned. Program income may or may not have been included in an application budget and/or a budget on the award document. If actual income is from a different source or is significantly different in amount, attach an explanation or use the remarks section.
6.	Check <i>yes</i> only if this is the last report for the period shown in item 8.	10d,	e, f, g, h, i and j. Self-explanatory.
7.	Self-explanatory.	10k.	Enter the total amount of unliquidated obligations, including unliquidated obligations to subgrantees and contractors.
8.	Unless you have received other instructions from the awarding agency, enter the beginning and ending dates of the current funding period. If this is a multi-year program, the Federal agency might require cumulative reporting through consecutive funding periods. In that case, enter the beginning and ending dates of the grant period, and in the rest of these instructions, substitute the term "grant period" for "funding period."		Unliquidated obligations on a cash basis are obligations incurred, but not yet paid. On an accrual basis, they are obligations incurred, but for which an outlay has not yet been recorded.
9.	Self-explanatory.		Do not include any amounts on line 10k that have been included on lines 10a and 10j.
10.	The purpose of columns, I, II, and III is to show the effect of this reporting period's transactions on cumulative financial status. The amounts entered in column I will normally be the same as those in column III of the previous report in the same funding period. If this is the first or only report of the funding period, leave columns I and II blank. If you need to adjust amounts entered on previous reports, footnote the column I entry on this report and attach an explanation.		On the final report, line 10k must be zero.
10a.	Enter total gross program outlays. Include disbursements of cash realized as program income if that income will also be shown on lines 10c or 10g. Do not include program income that will be shown on lines 10r or 10s.	10l.	Self-explanatory.
	For reports prepared on a cash basis, outlays are the sum of actual cash disbursements for direct costs for goods and services, the amount of indirect expense charged, the value of in-kind contributions applied, and the amount of cash advances and payments made to subrecipients. For reports prepared on an accrual basis, outlays are the sum of actual cash disbursements for direct charges for goods and services, the amount of indirect expense incurred, the value of in-kind contributions applied, and the net increase or decrease in the amounts owed by the recipient for goods and other property received, for services performed by employees, contractors, subgrantees and other payees, and other amounts becoming owed under programs for which no current services or performances are required, such as annuities, insurance claims, and other benefit payments.	10m.	On the final report, line 10m must also be zero.
		10n.	o, p, q, r, s and t. Self-explanatory.
		11a.	Self-explanatory.
		11b.	Enter the indirect cost rate in effect during the reporting period.
		11c.	Enter the amount of the base against which the rate was applied.
		11d.	Enter the total amount of indirect costs charged during the report period.
		11e.	Enter the Federal share of the amount in 11d.
		Note:	If more than one rate was in effect during the period shown in item 8, attach a schedule showing the bases against which the different rates were applied, the respective rates, the calendar periods they were in effect, amounts of indirect expense charged to the project, and the Federal share of indirect expense charged to the project to date.

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Figure 4
Sample Progress Report

Date _____

Subrecipient Contact Person _____

Subrecipient Name _____

Subaward Number _____

Pass-Through Entity Contact Person _____

Report Number and Period _____

Progress Achieved Toward Project Goals and Objectives _____

Goals	Target	Actual	Unit Costs	*Problems/Resolution
Goal No. 1 (e.g., provide medical care to children under age 5)				
Goal No. 2				
Goal No. 3				
Goal No. 4				

* The subrecipient should indicate the problems encountered, why goals were not met and how it plans to resolve the problems.

When required reports are overdue, the pass-through entity should contact the subrecipient to remind them of the requirement. An informal telephone reminder may be all that is necessary. But if the report fails to appear, the pass-through entity may want to send a formal letter specifying the report that is required, the date it was due and the provisions of the subgrant agreement or program regulations that require the report.

Pass-through entities should try to establish standard monitoring procedures and checklists for performing desk reviews of subrecipient reports. Because most subrecipients perform similar activities and provide similar reports, pass-through entities can re-use these checklists to save time and apply uniform monitoring procedures to subrecipients. Pass-through entities should make part or all of the checklists available to their subrecipients (and if they do not, subrecipients may want to ask for them), so the subrecipients can make sure they are properly carrying out the subaward and preparing the correct reports and documentation. Pass-through entities may find it more efficient and less costly to provide guidance at the beginning of the subaward process rather than at the end of the process as follow-up advice in a management decision on a finding.

Pass-through entities may need to supplement document reviews with onsite monitoring. By visiting the subrecipient, the pass-through entity can review the underlying

documentation (e.g., payroll, applications or receipts) that support subrecipient reports, conduct staff interviews and view the actual site and services being delivered.

If a desk review discloses problems, the pass-through entity is responsible for informing the subrecipient and prescribing corrective action (e.g., repaying funds). In response to the finding, the pass-through may schedule follow-up desk reviews (and onsite visits, if necessary) and require additional reports to ensure the subrecipient has corrected the problem.

Prior Approvals

Circular A-110 and the grants management common rule require most subrecipients to get prior written approval from the pass-through entity for most major changes to the budget or the scope of work once the subaward is finalized. Examples of changes that require prior approval are:

- revisions that would result in the need for additional funding;
- transfer of funds allotted for training;
- revisions in the scope or objectives of the subaward;
- the need to extend the period of availability of funds; and
- changes in key personnel (e.g., the principle investigator of a research project).

In addition, the cost principles require subgrantees to obtain prior written approval from pass-through entities to charge certain costs to their subaward such as travel and special facilities rearrangement and alterations.

By requiring a subrecipient to get prior approval for such expenditures or changes, the pass-through entity can monitor the activities of the subrecipient. If certain costs or changes are not chargeable to the subaward, the pass-through entity can inform the subrecipient before the subrecipient incurs unallowable costs. Similarly, if the subrecipient needs to change a key staff member, this may signal problems with subaward administration. The pass-through entity may need to perform additional monitoring until a new staff person is hired and becomes familiar with the subaward requirements.

Both Circular A-110 and the grants management common rule state that requiring prior approvals is an effective method to monitoring "high-risk" subgrantees. By requiring certain prior approvals, the pass-through entity and subrecipient work closely throughout the subaward period and the pass-through entity stays informed of subrecipient activities.

By the same token, primary grantees have the discretion to waive prior approval requirements for reliable subrecipients to ease their administrative burden.

Third-Party Evaluations

A pass-through entity may require as part of the subaward agreement that subrecipients have an outside consultant specializing in grants administration review their operations. The consultant generally would review the subrecipient's various systems (e.g., financial management, property management, procurement) and prepare a report that identifies any problems and makes recommendations for improvements. Before hiring a consultant, both pass-through entities and subrecipients need to consider who will pay for the evaluation and

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whether the costs are chargeable to the federal award — are they reasonable, allowable and allocable?

There are other types of independent evaluations that pass-through entities should consider reviewing as part of their efforts to monitor subrecipients. Besides paid consultants, pass-through entities and subrecipients should consider having other interested groups evaluate their program such as beneficiaries of the subrecipient's services or community organizations operating in the same community where the subrecipient provides its services. These groups may provide valuable insights about problems with the services or benefits provided or areas where the subrecipient could increase its services.

City Uses Citizens Advisory Committee To Evaluate its CDBG Program

The city of Santa Maria, Calif. sought to manage CDBG programs according to program and statutory requirements. While delivering quality services to beneficiaries, the city must ensure that program funds are expended in a timely manner; that performance reports are complete, timely and accurate; that CDBG-funded programs are eligible activities that benefit low- and moderate-income residents; and that the new consolidated planning requirements are met.

The city's staff works closely with a citizens advisory committee to ensure that programs and activities reflect community needs. In terms of day-to-day administration, performance reports are prepared carefully and completely, and program activities are classified properly. Corrections, when they are required, are submitted in a timely fashion, and responses are prompt to requests for supplemental information.

This practice provides an example of a city combining a strong commitment to citizen participation with an unusual attention to detail in administering its housing and community development programs. City staff have developed particular expertise in administering affordable housing programs. Contractors and subrecipients are informed of their responsibilities under the CDBG program, and they are monitored on a yearly basis. The city has avoided audit or monitoring findings, achieving a high level of performance with program funds.

Source: U.S. Department of Housing and Urban Development, Blue Ribbon Practices in Community Development, <http://www.hud.gov:80/ptw/docs/ca30.html>.

Technical Assistance and Training

Training is an effective means of ensuring that subrecipients, especially new ones, are familiar with the governmentwide and program-specific requirements that apply to their subaward. By providing training, the pass-through entity can answer questions, recommend techniques for carrying out the subaward that have been successful with previous subrecipients and develop a partnership with its subrecipients. Similarly, pass-through entities may want to provide subrecipients with training when there is a major change in program policy and the pass-through entity wants to ensure that all subrecipients understand and correctly implement the change.

Pass-through entities can provide more targeted technical assistance to individual subrecipients. During a desk review or monitoring visit, the pass-through entity may identify a problem that will require technical assistance. For example, a primary grantee may discover that a subrecipient does not have effective internal controls over its financial accounting and cash management systems. This may require the primary grantee's staff to work with the subrecipient to develop a new internal control system. This kind of

targeted assistance can be costly because it requires substantial staff time. However, the long-term benefits of setting up successful internal controls may include fewer overpayments by the pass-through entity, fewer findings and possibly an internal control system that can be shared with other subrecipients.

NJ City Uses Technical Assistance Partnerships To Monitor CDBG Subrecipients

The city of Elizabeth, N.J. wanted to develop a more comprehensive system for ensuring subrecipients' compliance with program requirements and for simultaneously assisting subrecipients to improve performance.

The city's strategy for monitoring and managing subrecipients includes a detailed risk analysis of all the subrecipients, onsite and remote monitoring, and continuous technical assistance and staff interviews.

The city provides each agency with program-specific technical assistance that helps establish effective partnerships with its subrecipients. The city gives personal attention to each agency by providing ongoing technical assistance — both onsite and at its offices. City staff review each subrecipient's past operational and fiscal performance. In addition to examining relevant records and reports, the city meets with subrecipients to discuss problems and issues in order to get an overall sense of how the agency is doing. City staff emphasize a broad perspective in their technical assistance approach: assistance is provided in regulatory compliance, as well as in project delivery, outreach and performance. Finally, the city has designed and is implementing workshops to better acquaint subrecipient agencies with the entire grant process.

As a result of technical assistance provided to a group counseling and therapy provider for survivors of domestic abuse, the subrecipient was able to expand services from approximately 100 clients served per year to 140 clients. More generally, the city's approach to subrecipient monitoring focuses on improving the subrecipients' capacity to serve its clients.

Source: U.S. Department of Housing and Urban Development, Blue Ribbon Practices in Community Development, <http://www.hud.gov:80/ptw/docs/nj10.html>.

Informal Monitoring

Telephone calls and e-mail communication are probably the least costly and time-consuming methods of monitoring available. Such tools provide pass-through entities with the opportunity to ask a subrecipient questions about financial and progress reports and other documents submitted for review. Informal communication enables the pass-through entity to interview subrecipient staff about various subaward issues without having to make an onsite visit. Also, because telephone calls can be made and e-mail can be sent frequently and with less planning (e.g., when to make monitoring visit, what record to review) than other forms of monitoring, these types of procedures can help a pass-through entity develop a closer partnership with its subrecipients.

Like any other monitoring techniques, pass-through entities and subrecipients need to prepare for the telephone interview. The pass-through entity should schedule a time for the interview with the subrecipient, if it is going to involve complex questions, cover several areas or require a large amount of time. Routine questions and advice should be reserved for separate telephone calls.

When scheduling a telephone interview, a pass-through entity should inform a subrecipient of the purpose of the interview, issues that will be addressed during the call, who

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should be present for the call, how long it will take and any other information necessary (e.g., documents that the subrecipient should have on hand).

To prepare for the call, the pass-through entity and subrecipient both should review the relevant subaward provisions and administrative and programmatic regulations. The pass-through entity also should review the subrecipient's file.

The pass-through entity should make the call at the appointed time and identify the parties to the call from both the pass-through entity and the subrecipient. It should review the purpose of the call and follow the agenda, making sure the scheduled issues are covered. At the close of the call, the pass-through entity should summarize the results of the telephone interview, including any findings. The pass-through entity should indicate whether any follow-up will be necessary.

Both the pass-through entity and the subrecipient should take notes during the interview (or get permission to record it on tape). Once the call is complete, both sides should review their notes and make final copies for their files. If either side has any questions about what was said, a follow-up call may be necessary.

The pass-through entity also should prepare a final report to the subrecipient that summarizes the telephone call, identifying the issues addressed, any findings and recommendations for corrective action or improvement. The report should be added to the subrecipient's file. If the subrecipient disagrees with any aspect of the final report, it should contact the pass-through entity immediately. Otherwise, the subrecipient is responsible for taking any required corrective action and informing the pass-through entity when it is completed.

While there are a variety of tools available for subrecipient monitoring, a pass-through entity must choose those that will work best for its subrecipients. In making this choice, it should always keep in mind that its monitoring efforts should ensure that a subrecipient is meeting performance goals and objectives and administering its federal funds in compliance with the subaward requirements.

Regardless of the type of monitoring tool chosen, a pass-through entity should keep a detailed record of monitoring activities and other vital information related to all subawards. Thus, for each monitoring effort, a pass-through entity should prepare for its files a report that lists the monitoring date, the type of monitoring that was performed and the purpose of the monitoring activity. It should also identify any subrecipient staff or beneficiaries who were interviewed. The pass-through entity also should describe the monitoring results and any follow-up that is needed. This will enable the pass-through entity to better assess the subrecipient's compliance, plan future monitoring activities and prepare its own reports and records.

Checklist for Subrecipient Monitoring Results

A pass-through entity should keep a record of monitoring activities and other vital information related to all subawards.

- ✓ Subrecipient name and address
- ✓ Program name
- ✓ Subrecipient contact person
- ✓ Subaward agreement number
- ✓ Date of monitoring
- ✓ Type of monitoring procedure
 - telephone call
 - financial/progress report review
 - onsite visit
 - limited-scope audit (or other agreed-upon procedures engagement)
 - audit review
- ✓ Purpose of the monitoring
 - Review program progress and compliance with subaward requirements
 - Perform follow-up review
 - Other
- ✓ Subrecipient staff contacted/interviewed as part of monitoring
- ✓ Beneficiaries contacted/interviewed as part of monitoring
- ✓ Related reports (e.g., financial status reports)
- ✓ Monitoring results
 - findings
 - recommendations
 - required corrective action (e.g., report, site visit)
 - necessary technical assistance
- ✓ Subrecipient contact person responsible for follow-up
- ✓ Pass-through entity contact person responsible for follow-up
- ✓ Deadline for corrective action



5 Communication Between Pass-Through Entities and Subrecipients

Effective communication between pass-through entities and subrecipients during the subaward agreement period is essential to ensuring that the subrecipient performs the activities or services required by the agreement in compliance with the applicable program laws and regulations.

The pass-through entity needs to convey to the subrecipient the kinds of activities that the subrecipient must perform and any applicable laws and regulations with which the subrecipient must comply. Similarly, in many instances (e.g., performing a research grant), the subrecipient must inform the pass-through entity, usually through its application or proposal to perform the subaward, how it intends to perform the activities or services required in the subaward. For instance, a subrecipient that is performing a research subgrant for a university generally must provide a budget for its work, a list of the personnel that will be working on the subgrant and a list of the equipment needed to do the research. Beyond the terms of the agreement, pass-through entities and subrecipients will need to convey additional information to each other. Pass-through entities may have to inform their subrecipients about changes in program regulations and subrecipients, in turn, may have questions about subaward terms or changes in personnel. Therefore, pass-through entities and subrecipients should maximize the various tools of communication available to them.

Importance of the Subaward Agreement and Other Guidance

Perhaps the most important form of communication between the parties is the subaward agreement. It describes both the pass-through entity's and subrecipient's roles and responsibilities, the activities or services to be performed, and the applicable laws and regulations (see Chapter 3). It is the first document that either party should review when questions arise regarding the subaward.

Many pass-through entities prepare handbooks and other guidance for subrecipients that explain further the program's requirements and include important information such as program laws and regulations and OMB circulars. Such guidance also may describe additional requirements imposed by the pass-through entity. By providing such documents, pass-through entities help ensure that subrecipients, particularly new subrecipients, understand all of the relevant regulations and guidelines. And subrecipients get a more complete picture of what is required of them.

Information for Subrecipients

To help ensure that subrecipients understand all of the relevant laws, regulations and guidelines that apply to the subaward, pass-through entities should consider preparing a package of information that provides the following, as appropriate:

- ✓ program authorizing legislation;
- ✓ excerpts of program regulations;
- ✓ relevant public policy laws (e.g., the Davis-Bacon Act);
- ✓ the *Catalog of Federal Domestic Assistance* program listing;
- ✓ OMB Circulars (e.g., Circular A-110);
- ✓ excerpts of the *Federal Acquisition Regulation*;
- ✓ relevant state laws; and
- ✓ guidelines developed by the pass-through entity.

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Whether a pass-through entity prepares such guidance depends on several factors, including the number of subrecipients the pass-through has to oversee, the size of the subawards it makes, the need for such guidance and whether the benefits outweigh any related costs. For example, some state agencies have developed labor or environmental guidelines that subrecipients must follow when performing housing rehabilitation or other construction activities under the CDBG program. State agencies have developed such guidelines because they subaward a large portion of their CDBG funds to county and city governments and other entities. In many cases, the state making the subaward may include the guidelines by reference in the subaward agreement (see Appendix A, Page 71). If so, the subrecipient must follow them to comply with the agreement's requirements.

Even if guidelines prepared by the pass-through entity are not referenced in the subaward agreement, subrecipients should read the guidelines because they can provide additional information for carrying out the award such as describing the reports that the subrecipient must prepare. For example, the Library of Michigan, which awards subgrants to certain public, private, research, and elementary and secondary libraries under the Library Services and Technology Act (LSTA), has developed the *LSTA Subgrant Program Guidelines*. The guidelines address several areas such as reimbursement policies and procedures, the procurement of property and services, and copyrights. Under the section on reports, it states that "during the grant year, the Library of Michigan will send forms to subgrantees for reporting project progress. These reports request information pertinent to project expenditures, as well as progress on project objectives. This information is required for federal and state reporting and must be submitted in a timely fashion." It also notes that site visits may be conducted on a random basis.

Need for Dialogue Between Pass-Through Entities and Subrecipients

In most cases, the information in the agreement and any additional policy documents is just the beginning of an ongoing dialog between a pass-through entity and its subrecipients. Subrecipients frequently need to ask their pass-through entities questions about the subgrant agreement and its compliance requirements that are not answered in the subaward agreement or other guidance. In fact, many pass-through entities provide question and answer sessions for subrecipients during the application process. At these sessions, the pass-through entity answers questions about various aspects of the subawards such as modifying the scope of work, the applicable compliance requirements and the payment process. The pass-through entity also can explain the policies and procedures (e.g., the accounting or procurement systems) that the subrecipient is expected to have in place.

Subrecipients, especially those that are administering an award for the first time, may have questions for the pass-through entity during the course of the subaward. For example, a subrecipient may have a question about whether a certain cost is allowable. Additionally, a subrecipient may want to ask the pass-through entity if a change in the subaward such as adding personnel or purchasing new equipment needs prior approval from the pass-through entity (see Chapter 4). Pass-through entities should encourage subrecipients to ask questions and try to provide the answers quickly and clearly. If both parties deal with questions as they arise, they can prevent potential problems such as noncompliance or unallowable expenditures, which if not caught can lead to findings during an audit or review and possibly a reduction or complete loss of federal funding.

Most pass-through entities try to keep these type of communications informal, but depending on the nature of the subrecipient's question, a pass-through entity may want to

Chapter 5: Communication Between Pass-Through Entities and Subrecipients

document the answer in writing. Also, if a subrecipient identifies a problem such as a break down of its internal control, it may want to inform the pass-through entity in advance rather than having the pass-through entity discover it through an audit or monitoring visit. A pass-through entity or auditor probably would be more assured if the subrecipient has found a problem, informed the pass-through entity and is working to correct it.

Pass-through entities may need to contact subrecipients about changes in grant requirements. Federal agencies update program regulations frequently, and while subrecipients are responsible for following the most current compliance requirements, pass-through entities also should inform their subrecipients of applicable federal regulations and related changes to ensure that the program is successful. Circular A-133 states that pass-through entities should "advise subrecipients of requirements imposed on them by federal laws, regulations and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity." For instance, pass-through entities that are aware of changes to income guidelines that affect the eligibility of certain beneficiaries of program services should communicate this information to any affected subgrantees. Also, subrecipients should be made aware of other changes such as a new address or contact person for the pass-through entity.

How pass-through entities choose to communicate this information may vary depending on the number of subrecipients they have, the importance of the regulatory changes and the pass-through entity's resources. Some pass-through entities with a large number of subrecipients may send an official letter that explains the changes, while others may telephone if they have only a few subrecipients. Pass-through entities that rely on the telephone may want to keep a record of calls with subrecipients as part of the subgrant file.

Pass-through entities also may want informal updates on the progress from subrecipients without waiting for formal reports or audits. Some pass-through entities schedule regular meetings with subrecipients. The frequency of the meetings depends on the nature of the subaward, how near the subrecipients are to the pass-through entity and how much oversight the pass-through entity wants to exercise. In one case, the program director for a midwestern medical school that subawards U.S. Department of Education funds for health education training to nonprofit organizations attends the subrecipients' board meetings because of their proximity. In this way, the medical school is able to ascertain on a regular basis that the subrecipients are performing the activities set forth in the subaward.

During these informal meetings, subrecipients should discuss any problems they may be having rather than waiting for a formal monitoring visit or progress report and get advice from the pass-through entity on potential remedies. Subrecipients also can use the informal meetings to report program successes such as achieving program goals or reducing administrative costs.

Many pass-through entities, including those that contact their subrecipients on a more informal basis, specify in the subaward agreement that the subrecipient must submit financial or progress reports during the course of the subaward. These reports may be in addition to or in lieu of a Circular A-133 audit, depending on whether the subrecipient's federal expenditures exceed the circular's audit threshold. However, the subaward agreements quite frequently do not fully explain the reporting that subrecipients must provide to the pass-through entities. Pass-through entities may have to further explain to the subrecipients the type of reporting required.

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For example, a disaster funding agreement between the state of Florida and its subgrantees requires the subgrantees to provide quarterly progress reports. The pertinent language in the agreement states:

The first report is due three months after the date of execution of this agreement and quarterly thereafter until the work has been completed and approved through final inspection. All reports shall be provided using the attached quarterly report form. ... The grantee may require additional reports as needed. The subgrantee shall, as soon as possible, provide any additional reports requested by the grantee.

If the pass-through entity needs any additional reports, it should contact the subrecipient as soon as possible to explain what information the report should contain and where and when it should be submitted. Providing the subrecipient with the most information possible about the required report will help ensure the subrecipient submits information the pass-through entity needs to oversee the subaward.

Similarly, pass-through entities should contact their subrecipients to schedule monitoring visits. While most subaward agreements specify that the pass-through entity has the right to visit the subrecipient, they generally don't specify when the visits take place or what the pass-through entity will inspect. An example of subaward monitoring language is as follows: "The subgrantor will schedule two monitoring visits with the provider on the following basis to evaluate the progress and performance of the program and provide technical assistance."

Pass-through entities, therefore, usually must contact subrecipients to schedule their visits. When contacting the subrecipient, pass-through entities may want to let the subrecipients know the areas of the program they want to focus on and the records they want to review during their visit. This should help the visit go smoothly and efficiently. And if the pass-through entity does not volunteer this information, subrecipients should go ahead and ask for it.

Preparing for a Site Visit

When scheduling a visit to a subrecipient's program site, a pass-through entity should consider providing the subrecipient with the following information, so it can prepare for the visit:

- ✓ the visit's purpose;
- ✓ the pass-through entity contact person;
- ✓ records to be reviewed;
- ✓ areas of the program site to be visited or observed;
- ✓ employees to be interviewed; and
- ✓ beneficiaries to be interviewed.

There may be instances when a pass-through entity does not inform a subrecipient of an inspection, preferring instead to "surprise" the subrecipient. While these types of visits are not common, they give subrecipients greater incentive to keep their books and records in order. However, a pass-through entity may want to consider the effect a surprise approach to monitoring might have on its relationship with its subrecipient.

During the monitoring visit, the pass-through entity and subrecipient should maintain an open discussion rather than waiting for the pass-through entity to issue its report on the visit. By talking during the visit, the pass-through entity can alert the subrecipient to problems such as noncompliance with program regulations or accounting errors that it discovers. This gives the subrecipient an opportunity to explain why it is not a problem or possibly correct it before the pass-through entity leaves.

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Once the monitoring visit is over, the pass-through entity should prepare a report of the results that includes any findings and send it to the subrecipient. The report also should contain the pass-through entity's recommendations and technical advice for improvement and how the subrecipient should follow-up. The subrecipient should take the opportunity to comment on the report, indicating where it disagrees with the pass-through entity, and providing a corrective action plan to address any findings and implement the pass-through entity's recommendations. The pass-through entity should indicate in the report whether it will require additional reports or inspections as a result of the monitoring visit. If so, the pass-through entity and subrecipient will have to work together to schedule subsequent visits and reports.

Communication About Subrecipient Single Audits

The amount of monitoring, both document reviews and onsite visits, that a pass-through entity performs depends on whether a subrecipient has a single audit performed in accordance with Circular A-133 (see Chapter 4). When a pass-through entity knows that a subrecipient will have a Circular A-133 audit performed, it may reduce the amount of monitoring it performs because it can rely on the single audit to identify problems with or provide assurance about a subrecipient's compliance with program requirements.

Under Circular A-133, a subrecipient must provide any pass-through entity with a copy of its single audit report when the pass-through entity is affected by findings reported in the schedule of findings and questioned costs or disclosed in the summary schedule of prior audit findings. Otherwise, a subrecipient must send its pass-through entity a letter stating that the subrecipient had a single audit performed and there were no audit findings affecting the pass-through entity's subawards.

Pass-through entities, however, should not wait to receive a subrecipient's single audit report to determine what level of additional monitoring is required. They must determine a subrecipient's federal expenditures early enough in the subaward period to conduct effective monitoring. While a pass-through entity can identify those subrecipients to which it awarded \$300,000 or more in federal funds or that had single audits conducted in previous years, it cannot identify all of its subrecipients that will have a single audit. Therefore, to identify how much monitoring it will have to do, a pass-through entity should require as part of the subaward agreement that subrecipient inform the pass-through entity what their federal expenditures are and whether they are going to have single audit done. Many pass-through entities require their subrecipients to complete a certification letter that provides this information (see Figure 1, Page 54).

Using this information, the pass-through entity can set up a monitoring plan for each subrecipient. To monitor a subrecipient that does not have a single audit, pass-through entities will have to develop a more comprehensive review plan that focuses on such areas as the subrecipient's financial records and program compliance. In contrast, pass-through entities can focus monitoring efforts on areas that are not covered in a single audit such as performance objectives (e.g., qualitative issues that auditors do not test), or they can focus on certain subrecipients that are deemed high-risk because of prior findings, the amount of money they receive, the complexity of the program or other reasons.

Figure 1
Single Audit Certification Letter

Date
Subrecipient Contact Person
Subrecipient Organization Name
Street Address
City, State, Zip

RE: Subrecipient Audit Requirements of OMB Circular A-133
Contract between [insert pass-through entity's name] and [insert subrecipient's name] for the period of [insert date] through [insert date] under [identify subaward by name/CFDA number/ amount of award]

Dear [insert subrecipient contact person]:

[Insert the pass-through entity's name] is subject to the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments and Nonprofit Organizations*. As such, Circular A-133 requires [insert pass-through entity's name] to monitor our subrecipients of federal awards and determine whether they have met the audit requirements of the circular and whether they are in compliance with federal laws and regulations.

Accordingly, we are requesting that you check one of the following, provide all appropriate documentation regarding your organization's compliance with the audit requirements, sign and date the letter and return this letter to me at your earliest convenience.

1. We have completed our Circular A-133 audit for fiscal year ended [enter date]. A copy of the audit report and a schedule of federal programs by major program are enclosed. (If material exceptions were noted, please enclose a copy of the responses and corrective actions taken.)
2. We expect our Circular A-133 audit for fiscal year ended [insert date] to be completed by [insert expected completion date]. A copy of our audit report will be forwarded to [insert pass-through entity's name] within 30 days of receipt of the report. A schedule of federal programs is enclosed.
3. We are not subject to a Circular A-133 audit because:
 We are a for-profit organization.
 We expend less than \$300,000 in federal awards annually.
 Other (please explain) _____

Type or Print Name

Title

Date

Signature

Please address all correspondence to:
Pass-Through Entity Contact Person
Pass-Through Entity Name
Street Address
City, State, Zip

Your prompt attention to this matter is greatly appreciated. If you have any questions please contact me at [insert telephone number for pass-through entity contact person].

Sincerely,
Pass-Through Entity Contact Person

Contacting the Federal Awarding Agency

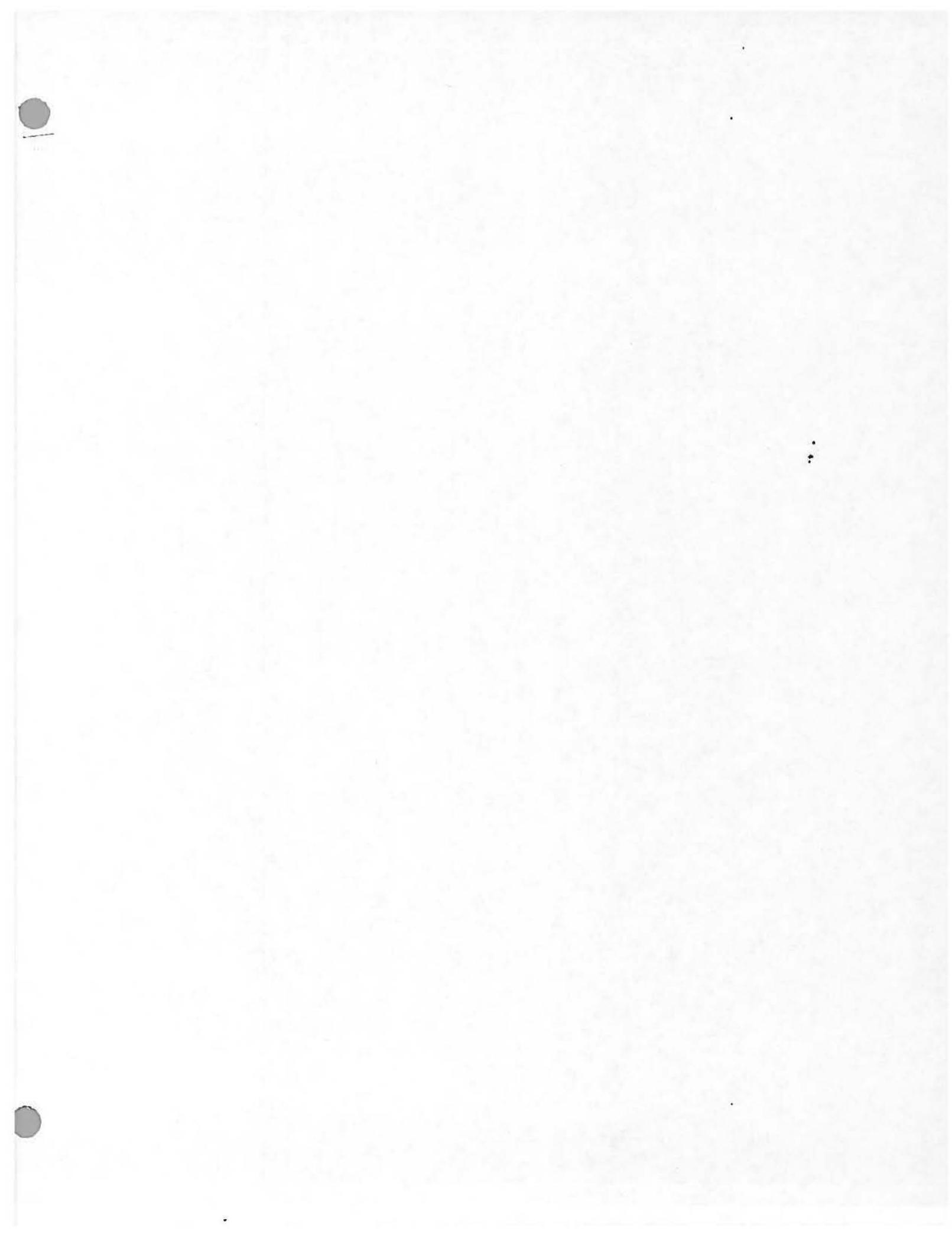
Federal agencies generally are not involved in the management or monitoring of subrecipients. This is because the subrecipients receive their federal funds through agreements with pass-through entities. Therefore, because subrecipients and federal agencies do not have a contractual relationship, they are not directly linked. When preparing any financial or progress reports or having an audit performed, the subrecipient should submit any results to the pass-through entity. Similarly, questions about the subaward also should be directed to the pass-through entity. This is not to say that subrecipients are prohibited from contacting federal agencies.

In fact, a subrecipient may need to contact the federal awarding agency directly when the pass-through entity cannot answer its questions about the subaward. For example, a subrecipient may need to contact the federal awarding agency for the CFDA name and number of a program it administers to complete the *Data Collection Form for Reporting on Audits of States, Local Governments and Nonprofit Organizations* (SF-SAC). The pass-through entity often does not have the CFDA information because it is a subrecipient itself and did not receive the CFDA information from its pass-through entity.

Additionally, under most subaward agreements, subrecipients must make their records available for inspection by not only the pass-through entity but also the federal awarding agency.

While the federal agency is not directly involved in subrecipient management, they want to ensure that subrecipients are spending federal awards in accordance with program requirements and that the pass-through entities are monitoring their subrecipients' activities. Therefore, pass-through entities' monitoring procedures are audited during their single audit. The results of the audit, including any findings regarding subrecipient monitoring, are sent to the federal awarding agency.

Beyond reporting the results of their single audits to their federal awarding agencies, pass-through entities may want to contact program officials or auditors at the federal agency. They may have questions about program regulations or subaward provisions that affect how their subrecipients perform the program activities or about monitoring procedures. For example, a subrecipient may want to purchase a piece of equipment not listed in the approved budget. Before the pass-through entity approves the purchase, it may contact the grantor agency to ensure the piece of equipment is an allowable expense under the federal award. By contacting the federal awarding agency for answers to subrecipient questions, the pass-through entity can help ensure its subrecipient complies with program requirements and properly manages their federal funds. It also is a method for monitoring subrecipient activities.



6 Monitoring Follow-Up

Regardless of whether primary grantees make onsite visits or review documents and audits, the results of these monitoring efforts must be conveyed to the subrecipients. When doing so, problem areas that need to be corrected, as well as examples of successful program administration, should be identified. Recommendations and corrective actions needed should also be noted. For example, a university that finds a nonprofit subrecipient performing biomedical research has inadequate time sheets can provide samples of how time sheets should be prepared when it informs the subrecipient of the finding. In addition to offering subrecipients recommendations for corrective action, the pass-through entity also can provide more specific technical advice and training directed toward the subrecipient's problem.

Once a subrecipient receives its pass-through entity's recommendations, it must take steps to correct any problems found and prevent recurrence of similar problems. If necessary, the subrecipient may need to consult the pass-through entity for additional advice or to make sure that its plan of action is allowable under the federal program. The subrecipient also should keep the pass-through entity informed of its follow-up progress and let the pass-through entity know when the problems have been remedied.

A pass-through entity must ensure that the subrecipient has taken the necessary steps to correct the problems identified. To do so, the pass-through entity may request additional follow-up reports and documentation from the subrecipient, and in some cases, it may make a follow-up visit to the subrecipient. For example, a state housing agency that discovers a contractor is building public housing facilities that do not satisfy Section 504 of the Rehabilitation Act of 1973, which prohibits discrimination against disabled individuals by federal programs, may make a follow-up visit to verify that the facilities now accommodate persons with disabilities.

Pass-Through Entity Responsibilities

When a pass-through entity completes an onsite visit or a document review or receives a copy of an auditor's limited-scope audit report, it must inform the subrecipient of the findings. Even if the pass-through entity has communicated the results of the review to the subrecipient informally (e.g., at the onsite visit or over the phone after a desk review), it should send an official letter confirming those results (see Figure 1, Page 58). The letter should identify:

- specific problems (e.g., misspent funds, problems with internal control, noncompliance with program requirements);
- the type of corrective action required (e.g., repaying federal funds, establishing new policies or procedures);
- whether a corrective action plan is necessary;
- the time frame for the subrecipient to take the corrective action;
- technical assistance that is available from the pass-through entity, if appropriate;

Figure 1
Monitoring Follow-Up Letter

August 2, 1999

Subrecipient Contact Name _____
Subrecipient Name _____
Subrecipient Address _____
Response Due Date _____
Agreement Number _____

Dear [Insert Subrecipient Contact Name]

This letter is a follow up of my monitoring visit on [insert date] of Community Development Block Grant (CDBG) agreement [insert agreement number]. I appreciate the time you took to show me the CDBG files and the completed Waste Water Expansion project. I also enjoyed meeting and talking to [insert names and titles of individuals interviewed].

I reviewed files dealing with financial management and labor standards, and I performed a general overview of all CDBG files. I wish to acknowledge that the files provided were all readily available and well organized.

Following are items of recommendation for future CDBG grants and items that require a response. Please respond to those items in bold by the due date indicated above.

1. The [insert the subrecipient organization name] provided notification to unsuccessful bidders for the Waste Water Expansion project but it did not include the [subrecipient organization name's] protest procedure in either the bid package or the notification. **Please provide a copy of the [insert subrecipient organization's name] protest procedure for bidders wishing to protest an award and ensure that future notifications include such.**
2. I noted that you do not have a complete set of CDBG handbooks and information bulletins. They are a useful tool for CDBG grant administration and may also answer questions that arise during the application process. Please ensure that the [insert the subrecipient organization name] obtains a set of handbooks and bulletins if it plans to apply for future CDBG grants.
3. I was unable to review the [insert the subrecipient organization name] procurement policy and procedures. **Please submit a copy.**
4. A special survey was conducted for the Waste Water Expansion project but the back up documentation was not available for review. **Please provide documentation of that survey, including: tabulation sheets, all completed surveys and how the survey was publicized.**
5. The leverage ledger was incomplete as it documented only \$76,000 rather than the \$82,000 as stated in the application. **Please complete the ledger and send a copy to me.**

Should you have any questions about this or other CDBG related subjects, please feel free to contact me at [insert telephone number].

Sincerely,

[insert pass-through entity's contact name]

CDBG Program

- ❑ any additional reports that the subrecipient may have to provide to the pass-through entity; and
- ❑ any additional monitoring the pass-through entity will perform to verify that the corrective action has taken place (e.g., site visit to view renovated facilities, document review of new policy or revised account ledgers).

Similarly, if the monitoring did not disclose any problems, the pass-through entity should confirm the results in writing to the subrecipient. It may congratulate the subrecipient and encourage it to continue any successful practices.

Subrecipients should ask their primary grantees when they plan to issue a monitoring follow-up letter. Often, a pass-through entity may include such information in its program guidance. The sooner a pass-through entity issues a letter, the sooner a subrecipient can make any needed corrections.

While monitoring follow-up often takes place after the pass-through entity completes its monitoring activity, pass-through entities and their subrecipients can take the opportunity to begin follow-up and corrective action while the monitoring activity is still going on. Pass-through entities performing site visits can inform subrecipients immediately when they discover problems such as misspent funds, internal control deficiencies or inadequate compliance with eligibility, matching or other program requirements. Then pass-through entities and subrecipients can work together to determine what corrective action will be necessary while the pass-through entity is onsite. In some instances, it may be possible for a subrecipient to begin corrective measures during the onsite review. For example, a pass-through entity may determine that certain ineligible beneficiaries have been receiving program services. Before the pass-through entity's staff leaves, the subrecipient may have drafted new policies to properly identify only eligible beneficiaries.

Reviewing a Subrecipient's Single Audit Report

When the pass-through entity receives a copy of a subrecipient's single audit report, it must issue a management decision within six months of receiving the report if that report discloses any findings. In the management decision, the pass-through entity must state whether it sustains the audit findings identified in the auditor's report, the reasons for its decision and the corrective action that the subrecipient must take. If the subrecipient has not completed the necessary corrective action, the pass-through entity should include a timetable for completion. The management decision should also specify any appeals procedures that are available to the subrecipient.

Subrecipients should note that a pass-through entity may request additional information or documentation before it issues a management decision. Also, they should initiate corrective action within six months of receiving their audit report and proceed as quickly as possible.

Pass-through entities should remember that if a subrecipient's single audit disclosed no findings that related to awards provided by the pass-through entity, the subrecipient does not have to send the pass-through entity a copy of its single audit report. Instead, the subrecipient must send a letter to the pass-through stating that the subrecipient had a Circular A-133 audit and that no findings affecting awards provided by the pass-through entity were reported.

After reviewing a subrecipient's single audit report, the pass-through entity should consider whether it is necessary to adjust its own records. As part of the finding-resolution

process, the pass-through entity should estimate the total unallowable costs for each subrecipient finding and consider the need to adjust its financial records and federal expenditure reports. Failure to do so should be considered by the auditor in forming his or her opinion on the primary recipient's major program compliance.

Subrecipient Responsibilities

Once a pass-through entity informs a subrecipient of the monitoring results, the subrecipient should take any corrective action prescribed by the pass-through entity such as repaying the misspent funds or changing its policies or practices to prevent further noncompliance with the subaward requirements. If the pass-through entity provides the monitoring results through a follow-up letter, the subrecipient may want to respond to the pass-through

Figure 2
Subrecipient Monitoring Visit Letter Response

August 28, 1999

Pass-Through Entity Contact Name
CDBG Program
Pass-Through Entity Address

Re: [Insert Contract Number]

Dear [Insert Pass-Through Entity Contact Name]:

This letter is in response to your monitoring visit letter of [insert date]. I will respond to your concerns in the order presented in your letter.

1. Enclosed is a copy of the [insert the subrecipient organization name] protest procedure as addressed in our purchasing policies. We will ensure that future bid documents related to CDBG contracts include the protest procedure.
2. Enclosed is a check for \$60.00. Please send me a copy of all CDBG handbooks and information bulletins that are currently available.
3. Enclosed is a copy of the [insert the subrecipient organization name] procurement policy and procedures.
4. Enclosed are the tabulation sheets and marketing information for our special survey of 1997 pertaining to the Waste Water Expansion project. Because the survey area was very large and we had a high response rate, I did not include all 234 survey responses. I spoke with you on [insert date] regarding this and was instructed to send a sampling of 15 completed responses. Those are enclosed.
5. Enclosed is a copy of the completed ledger documenting the full amount of \$82,000.

Please call me if you have any other questions or concerns.

Sincerely,

[Insert the Subrecipient Contact Name and Title]

encl: Procurement Policies (includes protest procedure)
Check for \$60.00
Special Survey documents

entity with its own letter, explaining how it has already corrected or plans to correct any findings (see Figure 2, Page 60).

A subrecipient must correct the problem in the time period specified by the pass-through entity. To demonstrate its corrective action to the pass-through entity, a subrecipient may have to:

- provide revised documentation or a report for the pass-through entity to review (e.g., revised accounting ledger entry); or
- undergo a follow-up visit by the pass-through entity (e.g., to review a change in operations).

If a subrecipient disagrees with a finding disclosed during monitoring, it should negotiate with the pass-through whether it must take corrective action. In some instances, pass-through entities have established appeal procedures.

To ensure the subrecipient corrects the problem, the pass-through entity might schedule additional monitoring visits or request certain reports. For example, if a nonprofit performing job training has been charging the same costs inconsistently, as both direct and indirect costs, the state agency that subawarded the money should require the nonprofit to submit revised reimbursement requests that treat the costs consistently.

Importance of Follow-Up

Failure by either the pass-through entity or the subrecipient to carry out their follow-up responsibilities could have serious consequences. If monitoring is performed and problems are identified, but neither party ensures corrective action is taken, the problems could be compounded, leading to more serious findings. For example, a monitoring visit may reveal that a subrecipient is determining program or benefit eligibility incorrectly. However, if the subrecipient does not correct its eligibility determination process and the pass-through entity just lets it go, the subrecipient's unallowable costs for providing benefits to ineligible persons will continue to grow, potentially costing the federal government hundreds of thousands of dollars. Remember, both the subrecipient and the pass-through entity are liable for misspent federal funds.

Furthermore, an auditor performing a pass-through entity's single audit may determine that the pass-through entity does not

Monitoring Follow-Up: Looking at the Big Picture

Pass-through entities should look at the overall results of their monitoring to identify:

- recurring problems unique to one program of which the federal awarding agency should be informed;
- opportunities to better monitor funds they subaward; and
- recurring problems with individual subrecipients.

Like the pass-through entity, the subrecipient should look at the overall monitoring results to identify:

- recurring problems that affect several programs (e.g., an inadequate financial accounting system) and need to be corrected;
- effective methods to administer subawards and comply with program requirements that can be applied to other subawards; and
- program-specific problems that may require a change in the way the pass-through or federal agency administers the program.

have an adequate subrecipient monitoring system because of the pass-through entity's failure to follow-up on identified findings. The auditor most likely would identify a reportable condition and possibly a compliance finding in the pass-through entity's single audit report. If the lack of adequate subrecipient monitoring was material to a major program, it also could affect the auditor's opinion on whether the pass-through entity complied with laws, regulations and the provisions of its grant agreement that could have a direct and material affect on major programs. For example, an auditor could modify its opinion if a pass-through entity that subawarded 90 percent of its federal funds did not perform adequate subrecipient monitoring follow-up and, therefore, did not have an adequate subrecipient monitoring system.

As discussed above, a subrecipient that fails to correct monitoring findings risks incurring additional unallowable costs. It also could suffer additional sanctions, such as the pass-through entity withholding program funds or suspending the subaward until the necessary corrective action is taken. More stringent sanctions might include termination of the subaward, denial of refunding and debarment and suspension.

In many instances, the subaward may specifically address the need for parties to follow-up on monitoring and the potential sanctions that could result if they do not. An example of such a provision is as follows:

The grantor will monitor the performance of the subrecipient against goals and performance standards required herein. Substandard performance as determined by the grantor will constitute noncompliance with this agreement. If action to correct such substandard performance is not taken by the subrecipient within a reasonable period of time after being notified by the grantor, subaward suspension or termination procedures will be initiated.

7 Auditor Review of Monitoring Activities

Organizations that pass through funds to subgrantees need to provide assurance to their federal awarding agencies that they are properly monitoring their subrecipients' use of federal funds and following up on any problems that are identified as a result of the monitoring. Therefore, OMB included guidance in its *Circular A-133 Compliance Supplement* for auditors on reviewing grantees' procedures for monitoring subrecipients as part of performing a single audit. Auditors will review the pass-through entities policies and records to verify that pass-through entities have internal controls in place to ensure monitoring is carried out and that they actually monitor their subrecipients. Additionally, auditors will look at whether the procedures ensure that federal funds are used by subrecipients for authorized purposes in compliance with applicable laws and regulations and that program performance goals are achieved.

How Auditors Test Subrecipient Monitoring

When selecting and performing activities to monitor subrecipients, primary grantees should keep in mind that OMB's guidance requires an auditor to test only a pass-through entity's programs that are large or otherwise at-risk for noncompliance with program requirements — "major programs." Once the auditor has selected the pass-through entity's major programs, he or she should inquire whether the entity provided program funds to subrecipients. Thus, if the pass-through entity made no awards to subrecipients from a major program, the auditor would not perform any tests for monitoring.

In contrast, when awards were made to subrecipients, the auditor must determine whether the amount of subawarded funds was material to the major program involved. The auditor uses his or her judgment to determine if it is material. Pass-through entities should note that certain federal programs contain requirements that generally will make their subawards material to a major program. For example, a state must subaward at least 90 percent of its CDBG funds. When such a large percentage of funds is passed through to subrecipients, the auditor would test a state's procedures for monitoring subrecipients administering CDBG subawards.

When the amount of subawarded federal funds is material in relation to a major program, the auditor reviews the pass-through entity's subrecipient monitoring activities. The auditor would develop audit procedures for testing the pass-through entity's subrecipient monitoring procedures by reviewing the number, size, and complexity of subawards provided.

Pass-through entities should note that auditors will look at both subrecipient and vendor relationships (see Chapter 2, Page 6). An auditor may determine that a pass-through entity's relationship with a vendor is, in substance, a subaward to a subrecipient and, therefore, is subject to monitoring. If the pass-through entity has not monitored these entities sufficiently, the auditor most likely will issue a finding. Pass-through entities must look closely at the substance of the relationship when determining whether they should issue a contract to a vendor or a subaward to a subgrantee.

As part of the single audit, an auditor must review the subrecipient monitoring controls a pass-through entity has in place. A pass-through entity's controls should provide reasonable assurance that federal award information and compliance requirements are clearly conveyed to subrecipients, subrecipient activities are monitored and the impact of any subrecipient noncompliance on the pass-through entity is evaluated. Also, grantees must ensure that subrecipients have required audits, and must take appropriate follow-up action on audit findings.

If an auditor determines that a primary grantee does not have effective internal controls in place, the auditor would include a reportable condition in the grantee's single audit report. (A reportable condition indicates there are sufficient deficiencies in the internal controls over compliance requirements, including subrecipient monitoring, that could affect a pass-through entity's ability to administer the federal program in accordance with applicable program requirements.) Then the auditor would do additional testing to determine the overall extent of the pass-through entity's noncompliance with subrecipient monitoring requirements. In contrast, if the entity's controls appear to be effective in detecting material noncompliance in subrecipient monitoring, then the auditor would identify those key controls the entity had in place and test that the controls were operating as designed.

Therefore, in anticipation of its single audit, a pass-through entity should assess whether it has adequate subrecipient monitoring controls in place. Questions that a primary

Internal Control Assessment Checklist

A pass-through entity must ensure it has internal controls in place to support its subrecipient monitoring objectives. Therefore, it may want to ask itself several of the following questions:

- ✓ Does the "tone at the top" demonstrate management's commitment to monitoring subrecipients?
- ✓ Is management intolerant of overriding established procedures to monitor subrecipients?
- ✓ Are sufficient resources dedicated to subrecipient monitoring?
- ✓ Do individuals performing subrecipient monitoring possess the necessary knowledge, skills and abilities required?
- ✓ Are subrecipients willing and able to comply with the requirements of the subaward?
- ✓ Do subrecipients have accounting systems, including the use of applicable cost principles, and internal control systems adequate to administer the subaward?
- ✓ Are appropriate sanctions taken for subrecipient noncompliance?
- ✓ Do key managers understand the subrecipient's environment, systems and controls sufficiently to identify the level and methods of monitoring required?
- ✓ Do mechanisms exist to identify risks arising from external sources affecting subrecipients such as economic conditions, political conditions, regulatory changes and unreliable information?
- ✓ Do mechanisms exist to identify and react to changes in subrecipients such as financial problems that could lead to diversion of grant funds; loss of license or accreditation to operate the program; rapid growth; new activities, products or services; and organizational restructuring?
- ✓ Does an official written policy exist establishing:
 - ❑ communication of federal award requirements to subrecipients;
 - ❑ responsibilities for monitoring subrecipients;
 - ❑ process and procedures for monitoring;
 - ❑ methodology for resolving findings of subrecipients' noncompliance or weakness in internal control; and
 - ❑ requirements for and processing of subrecipient audits, including appropriate adjustment of pass-through entity's accounts?

Internal Control Assessment Checklist (continued)

- ✓ Describe how subrecipients' compliance with audit requirements is monitored. The techniques that may be used include the following:
 - determining by inquiry and discussion whether the subrecipient met thresholds requiring an audit under Circular A-133;
 - if an audit is required, assuring that the subrecipient submits the report, reporting package or the documents required by the latest circular or primary recipient's requirements;
 - following-up on reported deficiencies related to programs funded by the primary recipient; and
 - if a subrecipient was required to have a Circular A-133 audit but did not do so, following-up with the subrecipient until the audit is completed and taking appropriate actions such as withholding further funding until the subrecipient meets the audit requirements.
- ✓ Describe the follow-up system used to track reported subrecipient deficiencies and resolution actions.
- ✓ Describe how subrecipients' compliance with federal program requirements is monitored. The following techniques may be used:
 - issue timely management decisions for audit and monitoring findings to inform the subrecipient whether the corrective action planned is acceptable;
 - maintain a system to track and follow-up on reported deficiencies related to programs funded by the recipient and ensure that timely corrective action is taken;
 - contact subrecipients regularly and make appropriate inquiries concerning the federal program;
 - review subrecipient reports and follow-up on areas of concern;
 - monitor subrecipient budgets;
 - perform site visits to subrecipients to review financial and programmatic records and observe operations; and
 - offer subrecipients technical assistance when needed.
- ✓ Are the federal award information (e.g., *Catalog of Federal Domestic Assistance* (CFDA) title and number, award name, name of federal agency, amount of award) and applicable compliance requirements provided to subrecipients?
- ✓ Do agreements with subrecipients include the compliance requirements applicable to the federal program, including the audit requirements of Circular A-133?
- ✓ Do standard award documents used by the nonfederal entity contain:
 - a listing of federal requirements that the subrecipient must follow (items can be specifically listed in the award document, attached as an exhibit to the document or incorporated by reference to specific criteria);
 - the description and program number for each program as stated in the CFDA (if the program funds include pass-through funds from another recipient, the pass-through program information should also be identified); and
 - a statement signed by an official of the subrecipient, stating that the subrecipient was informed of, understands and agrees to comply with the applicable compliance requirements?
- ✓ Is there a record-keeping system in place to ensure that documentation is retained for the time period required by the recipient (applies to subrecipients only)?
- ✓ Are procedures in place to provide channels for subrecipients to communicate concerns to the pass-through entity?
- ✓ Has a tracking system been established to ensure timely submission of required financial reports, performance reports, audit reports, onsite monitoring reviews of subrecipients and timely resolution of audit findings?
- ✓ Are supervisory reviews performed to determine the adequacy of subrecipient monitoring?

grantee should ask include whether the primary recipient's management supports subrecipient monitoring objectives, whether there are written policies that explain its subrecipient monitoring policies and whether there are sufficient records of its monitoring efforts.

As part of the audit, pass-through entities can expect an auditor to test award documents to ascertain if they made subrecipients aware of award information, specifically CFDA information, award name and federal awarding agency, and requirements imposed by laws, regulations, and the provisions of contract or grant agreements pertaining to the program. The auditor also would review the subaward agreement to verify that the activities approved in it were allowable. The auditor would review the grantee's documentation supporting its monitoring activities aimed at ensuring federal funds were used for authorized purposes.

This review would also include procedures to verify that the pass-through entity monitors activities of subrecipients exempt from Circular A-133, using such techniques as a limited-scope audit or document review. Additionally, an auditor would verify that a pass-through entity required its subrecipients subject to Circular A-133 to have the required audits.

When subrecipients are required to have an audit in accordance with Circular A-133, an auditor would verify that a pass-through entity received a copy of the audit reports, as necessary. (Circular A-133 does not require a subrecipient to provide a pass-through entity with a copy of the audit report when there are no findings that affect that pass-through entity.) Pass-through entities should be aware that review of a subrecipient's single audit report generally should be only one element of an adequate monitoring system. Document reviews and other procedures should also be performed.

Additionally, an auditor would verify that a pass-through entity issues management decisions on a timely basis for any audit or monitoring findings disclosed and require subrecipients to take timely corrective action on deficiencies identified. If there were disallowances for subrecipient questioned costs, the auditor would determine whether credits were properly reflected in the pass-through entity's records.

Auditors also will look at whether a pass-through entity identified the total amount of federal awards provided to subrecipients from each program in its schedule of expenditures of federal awards for the single audit. Circular A-133 requires pass-through entities to prepare the schedule, which lists all of its federal expenditures for the year by federal agency and program, and include the amount of subawards made, if practical. A pass-through entity that cannot identify the federal money it gave to subrecipients should raise a red flag for auditors. This would indicate that the pass-through entity is not tracking its subawards adequately.

The primary recipient may have to adjust its financial records and its federal expenditure reports to reflect certain costs incurred by the subrecipient that were identified as unallowable during an audit or review. Failure by the primary recipient to make the necessary adjustments to its records and reports would be considered by the auditor when preparing its final single audit report.

Potential Audit Findings and Their Effect

Primary recipients should be aware of the kinds of findings they may receive from an auditor if they do not have an adequate subrecipient monitoring system. If a primary recipient's monitoring system is not sufficient to ensure a subrecipient's compliance with the subaward and applicable laws and regulations, an auditor would note a reportable condition. The auditor also might report a material weakness if the primary recipient's internal controls over subrecipient monitoring for a program do not reduce the risk that noncompliance with

Chapter 7: Auditor Review of Monitoring Activities

applicable federal and program requirements may occur without detection. In addition, the auditor would consider whether the insufficient monitoring system should be reported as a finding of noncompliance. Should a primary recipient receive any such findings, it would have to correct them and take steps to prevent their recurrence.

A pass-through entity also could receive a qualified opinion as part of its single audit report, depending on the nature of the findings reported by the auditor. The auditor would draw an overall conclusion on whether the pass-through entity is in material compliance with subrecipient monitoring requirements. That conclusion would help the auditor to determine whether he or she can give an opinion on compliance for major programs. (Circular A-133 requires an auditor to give an opinion on whether an auditee complied with laws and regulations that could have a direct and material effect on major programs.) An auditor generally would modify his or her opinion on compliance if a primary recipient's lack of subrecipient monitoring was pervasive, and compliance with subrecipient monitoring requirements was material to the program. For example, if the pass-through entity did not perform adequate monitoring procedures and 90 percent of the program was subawarded, the auditor most likely would modify its opinion on compliance.

An auditor also would consider the effect of inadequate subrecipient monitoring on his or her opinion on the auditee's financial statements. If amounts passed through to subrecipients are considered material to the pass-through entity's financial statements, the auditor may need to alter his or her opinion on the financial statements. In making this determination the auditor should review evidence of whether its subrecipients administered the subawards in compliance with laws and regulations. The auditor can accomplish this by, for example, reviewing the results of limited-scope audits.

When reviewing a pass-through entity's subrecipient monitoring system, auditors want to see if the organization has a monitoring system in place. Many primary recipients that rely on single audits to monitor their subrecipients have no other form of monitoring in place. With the increased audit threshold, many of these subrecipients no longer have single audits. As a result, primary grantees need to use new methods for reviewing subrecipient activities. They must set up procedures to ensure that they provide their subrecipients with the required compliance information. They need to identify the areas they want to monitor, the reports and other documentation that subrecipient must provide and the staff that will oversee the monitoring effort.

Auditors also will look for monitoring activities that ensure subrecipient compliance with certain program-related requirements. Auditors generally will test the areas of allowable costs and activities, matching requirements, eligibility requirements and reporting. Are subrecipients performing allowable activities under the subaward? Are they only charging allowable costs to the federal program? Have they complied with any requirement to obtain matching funds from nonfederal sources? Are they providing benefits and services to eligible individuals only? Have they complied with all applicable financial and performance reporting requirements?

Pass-through entities may want to monitor subrecipient compliance with certain requirements that are unique to the award or the program. Auditors will look for and review the procedures used to monitor those areas. For example, a state that passes through job training funds to a nonprofit organization may request performance reports that describe number of individuals trained and other services provided by the subrecipient. It also may request financial reports, as well as invoices and other documentation to monitor allowability of

Chapter 7: Auditor Review of Monitoring Activities

the nonprofit entity's expenses. In another example, a medical school awarded federal funds to a nonprofit to provide training services. All of the nonprofit entity's grant-related bills are paid by the medical school, so it can review the subrecipient's activities and expenses to ensure they are allowable.

A common problem among pass-through entities is a lack of documentation of monitoring activities. Therefore, entities should maintain files for each subrecipient that contain any financial and progress reports that the subrecipient submits, the single audit report, and other documentation provided by the subrecipient. A pass-through entity should keep any completed checklists its staff may have used to perform onsite or desk reviews of subrecipient activities. Other documents to file include copies of any notes or follow-up letters sent in response to onsite visits or telephone interviews. Finally, a pass-through entity may want to maintain a record of each monitoring activity performed for a subrecipient. The record would include information such as the name of the subrecipient and subaward agreement number. It would identify the type and amount of federal program funds passed through. It would describe briefly the type of monitoring activity performed (e.g., document review, telephone monitoring), the date of the activity, the persons contacted, the activities and records reviewed and the results of the review.

Appendix A: Sample Subaward Agreements

<input type="checkbox"/> Figure 1 — Community Development Block Grant Agreement Between State of ABC Department of Commerce and XYZ County	71
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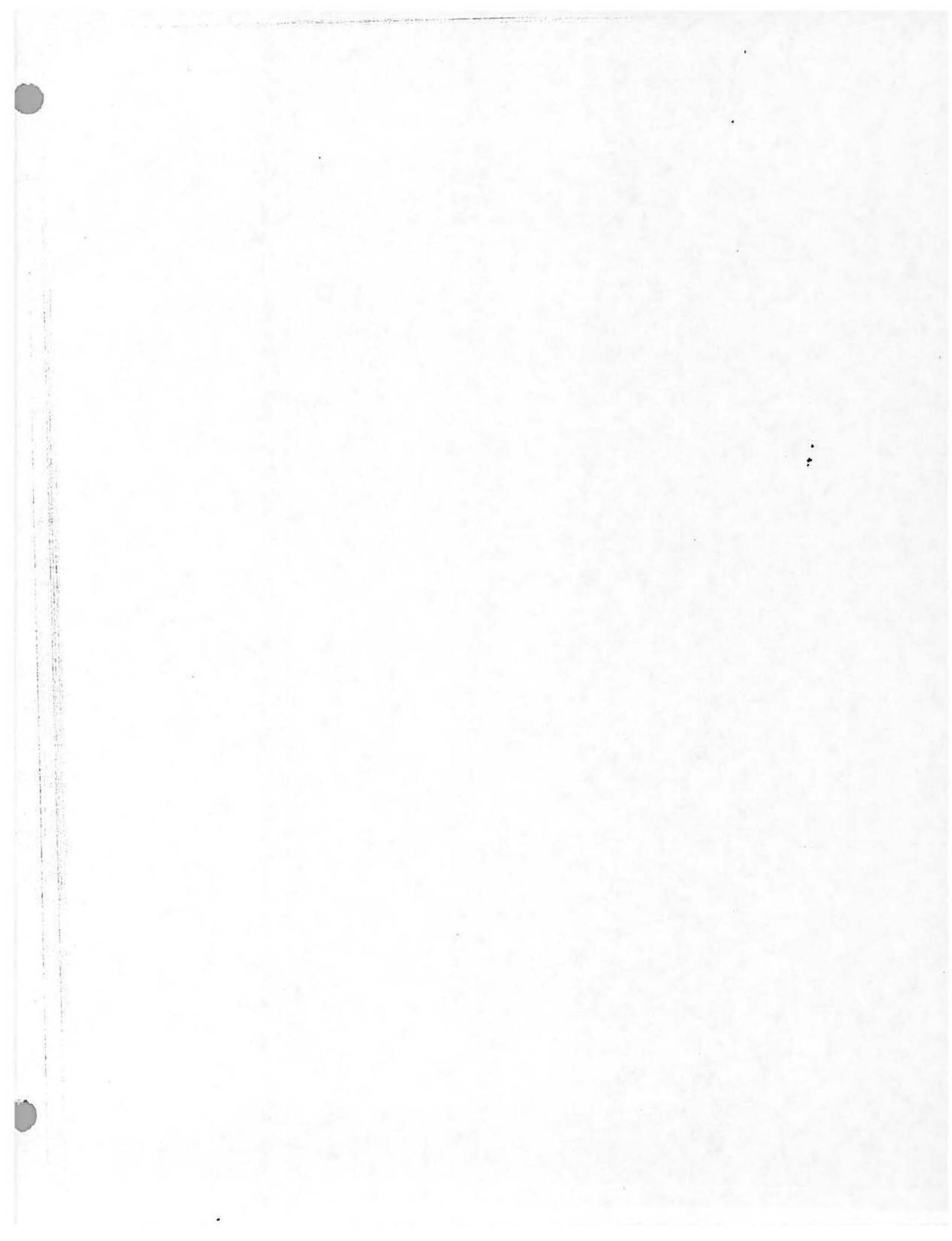


Figure 1

Agreement #: _____
Effective Date: _____
Expiration Date: _____

**COMMUNITY DEVELOPMENT BLOCK GRANT AGREEMENT
BETWEEN
STATE OF ABC
DEPARTMENT OF COMMERCE
AND
XYZ COUNTY**

This Community Development Block Grant (CDBG) agreement is made by and between the STATE OF ABC, DEPARTMENT OF COMMERCE (COMMERCE), located at [address], acting pursuant to [authorizing state code section] and XYZ COUNTY, (the RECIPIENT), acting pursuant to [authorizing state code section] and Title I of the Housing and Community Development Act of 1974, as amended. The RECIPIENT'S certifications relating to Title I assistance and the provisions contained in the *Consolidated Plan, Application Handbook, Labor Standards Handbook, Environmental Handbook, Procurement and Contracting Handbook and Information Bulletins* are hereby incorporated by reference, together with the resolution authorizing RECIPIENT'S actions attached, and made a part of this agreement.

In consideration of the mutual representations and obligations hereunder, COMMERCE and the RECIPIENT agree as follows:

SECTION 1. GRANT AMOUNT:

SECTION 2. PROJECTS FOR WHICH THIS FUNDING IS PROVIDED:

Activity No. 1. Administration: _____

Activity No. 2. Housing Rehabilitation: _____

Total FY 1997 regional account award amount: _____

SECTION 3. SCOPE OF WORK

See page ____ [Page 75]

SECTION 4. SPECIAL CONDITIONS

See page ____ [Page 75]

SECTION 5. REVISIONS BETWEEN AGREEMENTS

The RECIPIENT agrees that if more than one agreement is issued to it, funded from the FY 1997 regional account, all will be considered as if they were one agreement for purposes of revisions in amounts between activities. Thus, the RECIPIENT may increase or decrease funds between said agreements as long as the total of all activities does not exceed the amount indicated above as the total funds awarded to the RECIPIENT from the FY 1997 regional account. All revisions will be subject to the requirements relative to amendments and communication letter changes (CLC).

SECTION 6. ADMINISTRATION FUNDS

The RECIPIENT agrees that it may expend Activity No. 1 Administration funds on behalf of any agreement funded with FY 1997 regional account funds, if more than one is awarded. However, all administration funds will appear in and be paid from only one regional account agreement.

Figure 1 (continued)

SECTION 7. PROFESSIONAL SERVICES AGREEMENT: DIRECT PAYMENT TO A COUNCIL OF GOVERNMENT (COG)

The RECIPIENT agrees that if COMMERCE has a signed professional services agreement with the applicable COG, the following shall apply: COMMERCE shall directly pay the COG for technical assistance and application preparation (TAAP) services provided by the COG to the RECIPIENT relating to its FY 1997 regional account applications upon presentation by a bill from the COG to COMMERCE. A copy of this bill shall also be provided to the RECIPIENT. Such funds shall be subtracted from the total amount of funds identified in Activity No. 1 Administration in this or other FY 1997 regional account agreement.

SECTION 8. DURATION

The agreement shall become effective on the date indicated on Page 71. It shall remain in force until the first of the following: 1) for twenty-four (24) months from the effective date which is the expiration date shown on Page 71, 2) full completion of the scope of work, or 3) termination pursuant to the terms of this agreement.

SECTION 9. ENVIRONMENTAL REVIEW CONDITIONS

The funding assistance authorized hereunder shall not be obligated or utilized for any activities requiring a release of funds by the state of ABC under the environmental review procedures for the CDBG program until the applicable requirements contained in the *Environmental Handbook* have been satisfied.

SECTION 10. APPLICATION AND OTHER PRE-AWARD COSTS

In accordance with federal procedures, the RECIPIENT may use CDBG funds to reimburse itself and/or the COG for costs incurred in preparing the application. In no event shall such compensation exceed 18 percent of the total FY 1997 regional account grant amount as shown on Page 71. In addition, the RECIPIENT may use CDBG funds to reimburse itself for other pre-award costs previously approved, in writing, by COMMERCE.

SECTION 11. RECORDS RETENTION

Pursuant to [state code section], the RECIPIENT shall retain and shall require all of its subcontractors to retain, for inspection and audit by the state of ABC, all books, accounts, reports, files and other records relating to the bidding and performance of this agreement for a period of five (5) years after its completion. Upon request by COMMERCE, the RECIPIENT shall produce a legible copy of all such records at the administrative office of COMMERCE or at the office of the auditor general. The original of all such records shall be available and produced for inspection and audit when required by COMMERCE or the auditor general.

SECTION 12. REVISIONS

The RECIPIENT may request revisions to this agreement compliant with the requirements of Chapter 2 of the *Commerce CDBG Administration Handbook*.

SECTION 13. CANCELLATION

The provisions of [state code section] relating to cancellation of agreements are acknowledged and are incorporated by reference.

SECTION 14. TERMINATION FOR CAUSE

COMMERCE may terminate this agreement in whole or in part at any time whenever it determines that the RECIPIENT has failed to comply with the conditions hereof. If COMMERCE so determines, it shall notify the RECIPIENT in writing by certified mail, return receipt requested, of such termination for cause with such notification to include the reason(s) for the termination and the effective date of the termination.

Figure 1 (continued)

SECTION 15. TERMINATION FOR CONVENIENCE

COMMERCE or the RECIPIENT may terminate this agreement in whole or in part (one or more activities) if either party believes that continuation would not produce beneficial results. In that event, COMMERCE shall allow the RECIPIENT full credit for the CDBG share of the obligations properly incurred by the RECIPIENT prior to termination, as long as those obligations were incurred in full compliance with this agreement and with applicable laws and regulations.

SECTION 16. OBLIGATION OF STATE GENERAL APPROPRIATIONS FUNDS

Nothing herein shall be construed as obligating state general appropriation funds for payment of any debt or liability of any nature arising hereunder. The parties expressly recognize that all payments to be made by COMMERCE are solely from federal funds made available to COMMERCE for this purpose.

SECTION 17. AVAILABILITY OF FEDERAL FUNDS

Payments under this agreement are subject to the availability of the federal funds provided to the state of ABC, Department of COMMERCE for the CDBG program.

SECTION 18. ARBITRATION

This agreement is subject to arbitration only to the extent required by [state code section].

SECTION 19. INDEMNIFICATION

The RECIPIENT shall indemnify COMMERCE and the state of ABC and shall hold them, their officers, agents and employees harmless against any and all liability, loss, damages sustained by any person or property by virtue of the RECIPIENT and its subcontractor's performance under this agreement.

SECTION 20. FEDERAL GOVERNMENT LIABILITY

It is agreed by all parties that neither the federal government nor the U.S. Department of Housing and Urban Development are parties to this agreement, and that no legal liability on the part of the federal government is inferred or implied under the terms of this agreement.

SECTION 21. AUDIT EXCEPTIONS

If federal or state audit exceptions are made relating to this agreement, the RECIPIENT shall reimburse all costs incurred by the state of ABC and COMMERCE associated with defending against the audit exception or performing an audit or follow-up audit, including but not limited to: audit fees, court costs, attorneys' fees based upon a reasonable hourly amount for attorneys in the community, travel costs, penalty assessments and all other costs of whatever nature. Immediately upon notification from COMMERCE, the RECIPIENT shall reimburse the amount of the audit exception and any other related costs directly to COMMERCE as specified by COMMERCE in the notification.

SECTION 22. UNALLOWABLE USE OF FUNDS

The RECIPIENT, its officers, employees and agents, shall not utilize any federal funds provided under this agreement to solicit or influence, or attempt to solicit or influence, directly or indirectly, any member of Congress regarding pending or prospective legislation.

SECTION 23. INTEREST OF MEMBERS OF DEPARTMENT OF COMMERCE AND OTHERS

No officer or employee of COMMERCE and no public official, employee or member of the governing body of the RECIPIENT who exercises any functions or responsibilities in review or approval of the undertaking or carrying out of the agreement shall participate in any decision relating to this agreement which affects their personal interest or the interest of any corporation, partnership or association in which they are directly or indirectly interested, or have any interest, direct or indirect, in this agreement or its proceeds.

Figure 1 (continued)

SECTION 24. ACCESS TO RECORDS, PARTICIPANTS AND STAFF

The RECIPIENT agrees to provide COMMERCE and its representatives access at any reasonable time to all participants and staff involved in this agreement and to all records and reports involving this agreement.

SECTION 25. IDENTIFICATION OF DOCUMENTS

All reports, maps and other documents completed as a part of this agreement, other than documents exclusively for internal use by COMMERCE, shall carry the following notation on the front cover or title page, together with the date (month and year) the document was prepared:

"Preparation of this (report, map, document, etc.) was aided through a Community Development Block Grant from the state of ABC, Department of COMMERCE and as such is not copyrightable. It may be reprinted with customary crediting of the source.

However, any opinions, findings, conclusions or recommendations expressed are those of the authors and do not necessarily reflect the views of the Department of COMMERCE."

All reports, maps, and other documents not completed as a part of this agreement but utilizing the results of this agreement shall carry due and proper acknowledgment of support from the COMMERCE CDBG program.

SECTION 26. COPYRIGHT

No reports, maps or other documents produced in whole or in part under this agreement shall be the subject of any application for copyright or copyright registration by or on behalf of the RECIPIENT or by any employee or subcontractor of the RECIPIENT.

The RECIPIENT shall advise COMMERCE or its designee at the time of delivery of any copyrighted or copyrightable work furnished under this agreement, or any adversely held copyrighted or copyrightable material incorporated in any such work and of any invasion of the right of privacy therein contained.

SECTION 27. RIGHTS IN DATA

COMMERCE may duplicate, use and disclose in any manner and for any purpose whatsoever, within the limits established by federal and state laws and regulations, all information relating to this agreement.

SECTION 28. FUNDING CONDITIONS

COMMERCE will make the funding assistance available to the RECIPIENT upon execution of this agreement by the parties. The obligation and utilization of the funding assistance provided through this agreement are subject to the proper observation of the requirements incorporated by reference. The RECIPIENT shall require any subrecipient entities to observe and follow all provisions of this agreement.

SECTION 29. NONDISCRIMINATION

The contractor shall comply with Executive Order 75-5, which mandates that all persons, regardless of race, color, religion, sex, age, national origin or political affiliation, shall have equal access to employment opportunities, and all other applicable state and federal employment laws, rules and regulations, including the Americans With Disabilities Act. The contractor shall take affirmative action to ensure that applicants for employment and employees are not discriminated against due to race, creed, color, religion, sex, age, national origin or disability.

Appendix A: Sample Subaward Agreements

Figure 1 (continued)

IN WITNESS WHEREOF, COMMERCE and the RECIPIENT have executed this agreement.

THE STATE OF ABC,
DEPARTMENT OF COMMERCE

BY: _____

TITLE: _____

DATE: _____

RECIPIENT/GRANTEE

BY: _____

TITLE: _____

DATE: _____

SECTION 3. SCOPE OF WORK

Activity No. 1. Administration: _____ CDBG funds

Activity No. 2. Housing Rehabilitation: _____ CDBG funds

To provide approximately 13 grants of approximately _____ each for housing rehabilitation to approximately 13 owner-occupied households in XYZ County. The county will also perform housing rehab services. This activity will meet the housing low- and moderate-income benefit national objective and serve approximately 37 persons of whom 100 percent will be low to moderate income.

SECTION 4. SPECIAL CONDITIONS

Prior to approval of the first request for payment, RECIPIENT shall have submitted and obtained CDBG program approval for its Housing Rehab Guidelines.

Figure 2
(Accompanies Figure 1, Page 71)

APPLICANT CERTIFICATIONS FOR FY 1998

The applicant hereby assures and certifies that:

1. It possesses legal authority to apply for Community Development Block Grant (CDBG) funds, and to execute the proposed program.
2. Prior to the submission of the application, the applicant's governing body has duly adopted or passed as an official act a resolution authorizing the submission of the application, including all understandings, assurances, statutes, regulations and orders contained therein, and directing and authorizing the person identified as the official representative of the applicant to act in connection with the application and to provide such additional information as may be required.
3. Its chief executive officer or other officer of the applicant approved by the state:
 - a. Consents to assume the status of a responsible federal official under the National Environmental Policy Act of 1969 (NEPA) and other provisions of federal law, as specified at 24 CFR §58.1 (a)(3) and (a)(4), which further the purposes of NEPA insofar as the provisions of such federal law apply to this program.
 - b. Is authorized and consents on behalf of the applicant and him(her)self to accept the jurisdiction of the federal and state courts for the purpose of enforcement of his/her responsibilities as such an official.
4. It will comply with the provisions of Executive Order 11990, relating to evaluation of flood hazards and Executive Order 11288 relating to the prevention, control and abatement of water pollution.
5. It will, in connection with its performance of environmental assessments under the NEPA, comply with Section 106 of the National Historic Preservation Act of 1966 (16 U.S.C. §470), Executive Order 11593 and the Preservation of Archeological and Historical Data Act of 1966, P.L. 93-291 (16 U.S.C. §469a-1, *et. seq.*).
6. It will administer and enforce the labor standard requirements of the Davis-Bacon Act, as amended at 40 U.S.C. §§276a-276a-5, and the Contract Work Hours and Safety Standards Act at 40 U.S.C. §§327-333.
7. It will comply with the provisions of 24 CFR Part 24 relating to the employment, engagement of services, awarding of contracts or funding of any contractors or subcontractors during any period of debarment, suspension or placement in ineligibility status.
8. It shall comply with the requirements of the Lead Based Paint Poisoning Prevention Act, 42 U.S.C. §§4821-4846 and implementing regulations at 24 CFR Part 35.
9. It will comply with the provisions of 24 CFR Part 58, "Uniform Grant Administrative Requirements" and OMB Circular A-87.
10. It will comply with the Americans With Disabilities Act and Section 504 of the Rehabilitation Act, as amended.
11. It will comply with:
 - a. Title VI of the Civil Rights Act of 1964 (P.L. 88-352), and the regulations issued pursuant thereto (24 CFR Part 1).
 - b. Title VIII of the Civil Rights Act of 1968 (P.L. 90-284), as amended.

Appendix A: Sample Subaward Agreements

Figure 2 (continued)

- c. Section 109 of the Housing and Community Development Act of 1974.
 - d. Executive Order 11063 pertaining to equal opportunity in housing and nondiscrimination in the sale or rental of housing built with federal assistance.
 - e. Executive Order 11246, and the regulations issued pursuant thereto (24 CFR Part 130 and 41 CFR Chapter 60).
 - f. Section 3 of the Housing and Urban Development Act of 1968, as amended.
 - g. Federal Fair Housing Act of 1988, P.L. 100-430.
 - h. The prohibitions against discrimination on the basis of age under the Age Discrimination Act of 1973, 42 U.S.C. §§6101-07, and the prohibitions against discrimination against persons with handicaps under Section 504 of the Rehabilitation Act of 1973, (P.L. 93-112), as amended, and the regulations at 24 CFR Part 8.
 - i. The requirements of the Architectural Barriers Act of 1966 at 42 U.S.C. §§4151-415.
12. It will comply with the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 and implementing regulations.
 13. It will comply with applicable conflict of interest provisions, incorporate such in all contracts and establish safeguards to prohibit employees from using positions for a purpose that is or gives the appearance of being motivated by a desire for private gain for themselves or others, particularly those with whom they have family, business or other ties.
 14. It will comply with the provisions of the Hatch Act, which limit the political activity of employees.
 15. It will give representatives of the state, the secretary of HUD, the inspector general, and the General Accounting Office access to all books, accounts, records, reports, files and other papers, things or property belonging to it or in use by it pertaining to the administration of state CDBG assistance.
 16. It will ensure that the facilities under its ownership, lease or supervision which shall be utilized in the accomplishment of the program are not listed in the Environmental Protection Agency's (EPA) list of violating facilities and that it will notify the state of the receipt of any communication from director of the EPA Office of Federal Activities indicating that a facility to be used in the project is under consideration for listing by the EPA.
 17. It will comply with the flood insurance purchase requirements of Section 102(a) of the Flood Disaster Protection Act of 1973, P.L. 93-234, 87 Stat. 975, approved Dec. 31, 1973, Section 103(a) required on and after March 2, 1974.
 18. It has and will comply with the provisions of the state of ABC citizen participation plan for the state of ABC CDBG program.
 19. It has developed plans to minimize displacement of persons as a result of activities assisted in whole or in part with CDBG funds and to assist persons actually displaced as a result of such activities, and has provided information about such plans to the public.
 20. It will not recover any capital costs of public improvements assisted in whole or in part with CDBG funds by assessing any amount against properties owned and occupied by persons of low or moderate income, including any fee charged or assessment made as a condition of obtaining access to such public improvements unless:
 - a. The CDBG funds are used to pay the proportion of the fee or assessment that is financed from other revenue sources; or

Figure 2 (continued)

- b. It will certify to the state in writing that it lacks sufficient CDBG funds to comply with (a.) but that it will not assess properties owned by very low income persons.
- 21. It will provide all other funds/resources identified in the application, or any additional funds/resources necessary to complete the project as described in the application as submitted, or as may be later amended.
- 22. It will comply with the requirements of the Single Audit Act Amendments of 1996 and OMB Circular A-133, and if the grant is closed out prior to all funds having been audited, it shall refund to Commerce any costs disallowed as a result of an audit conducted after the date of grant closeout.
- 23. It hereby adopts and will enforce a policy prohibiting the use of excessive force by law enforcement agencies within its jurisdiction against any individuals engaged in nonviolent civil rights demonstrations; and will enforce applicable state and local laws against physically barring entrance to or exit from a facility or location which is the subject of such nonviolent civil rights demonstrations within its jurisdiction.
- 24. It will ensure that, to the best of the knowledge and belief of the undersigned:
 - a. No federal appropriated funds have been paid or will be paid, by or on behalf of the undersigned, to any person for influencing or attempting to influence an officer or employee of any agency, a member of Congress, an officer or employee of Congress, or an employee of a member of Congress in connection with the awarding of any federal contract, the making of any federal grant, the making of any federal loan, the entering into of any cooperative agreement, and the extension, continuation, renewal, amendment or modification of any federal contract, grant, loan or cooperative agreement.
 - b. If any funds other than federal appropriated funds have been paid or will be paid to any person for influencing or attempting to influence an officer or employee of any agency, a member of Congress, and officer or employee of Congress, or an employee of a member of Congress in connection with this federal contract, grant, loan, or cooperative agreement, the undersigned shall complete and submit Standard Form-LLL, "Disclosure Form to Report Lobbying," in accordance with its instructions.
 - c. The undersigned shall require that the language of this certification be included in the award documents for all subawards at all tiers (including subcontracts, subgrants and contracts under grants, loans and cooperative agreements) and that all subrecipients shall certify and disclose accordingly.

This certification is a material representation of fact on which reliance was placed when this transaction was made or entered into. Submission of this certification is a prerequisite for making or entering into this transaction imposed by Section 1352, Title 31, U.S. Code. Any person who fails to file the required certification shall be subject to a civil penalty of not less than \$10,000 and not more than \$100,000 for each such failure.
- 25. It shall comply with the provisions of Section 102 of the HUD Reform Act of 1989.

CERTIFIED BY:

Signature of Authorized Officer of the Applicant

Typed Name and Title of Authorized Officer of the Applicant

Figure 3
Illustrative Subaward Agreement

COMMUNITY DEVELOPMENT BLOCK GRANT AGREEMENT
BETWEEN THE CITY OF ABC AND THE XYZ CENTER

This agreement made and entered into this ___ day of _____, 19__ by and between the city of ABC, a municipal corporation, hereinafter referred to as Subgrantor, and the XYZ Center, hereinafter referred to as Provider;

Whereas, the city of ABC has received a grant from the U.S. Department of Housing and Urban Development as part of its Community Development Block Grant Program for the period _____, 19__ to _____, 19__ (hereinafter the "contract period"); and

Whereas, the primary objective of the Community Development Block Grant Program is the development of viable urban communities, including decent housing and a suitable living environment and expanding economic opportunities principally for persons of low and moderate income, and

Now, therefore, in consideration of the mutual benefits contained herein the Subgrantor and Provider do agree as follows:

1. **Contract Documents:** Contract documents shall consist of this agreement and four (4) attachments, all of which are incorporated by reference into this agreement. Attachment I contains a description of the service and goals offered by the Provider (see Page 83). Attachment II is a line item budget (see Page 84). Attachment III outlines financial management procedures for use with Community Development Block Grant funds (see Page 85). Attachment IV contains all applicable federal regulations (see Page 86).
2. **Services:** The Provider agrees to perform those services outlined in Attachment I and II.
3. **Contract Amount:** The Subgrantor agrees to make available \$_____ for use by the Provider for the contract period.
4. **Alterations:** Any alterations in the work program or the budget shall be submitted to and approved in writing by the Subgrantor.
5. **Quarterly Reports:** The Provider agrees to submit quarterly program progress reports on the 15th of October, the 15th of January, the 15th of April and the 15th of July to the director of Community Development. The Provider also agrees to submit on the 15th of July a comprehensive report covering the agreed-upon objectives, activities and expenditures for the entire contract period. Such shall include performance data, including data on client feedback, with respect to the goals and objectives outlined in Attachment I.
6. **Monitoring:** The Subgrantor will schedule two (2) monitoring visits with the Provider to evaluate the progress and performance of the program and provide technical assistance.
The subgrantor shall be provided access to all program-related records and materials at these times.
7. **City Residents Only:** The Provider agrees that Community Development Block Grant Funds shall only be used to provide services to residents of the city of ABC.
8. **Subcontract:** No part of this agreement may be assigned or subcontracted without the prior written approval of the Subgrantor.
9. **Disputes:** Except as otherwise provided in this contract, any dispute concerning a question of fact arising under this contract which is not disposed of by agreement shall be decided by the director of Planning and Community Development, who shall reduce his decision in writing and furnish a

Figure 3 (continued)

copy thereof to the city manager and the Provider. The decision of the director of Planning and Community Development shall be final and conclusive unless, within ten (10) days from the date of receipt of such copy, the Provider furnishes a written appeal to the city manager. The decision of the city manager or his duly authorized representative for the determination of such appeals shall be promptly hand delivered or sent by certified mail to the Provider and such decision shall be final and conclusive unless appealed to a court of competent jurisdiction within thirty (30) days of receipt of the city manager's decision, and determined by that court to have been fraudulent, capricious or arbitrary, or so grossly erroneous as necessarily to imply bad faith, or not supported by substantial evidence. In connection with any appeal proceeding under this clause, the Provider shall be afforded an opportunity to be heard, to be represented by counsel at its own expense, if it so desires, and to offer evidence in support of its appeal. Pending final decision of a dispute hereunder, the Provider shall proceed diligently with the performance of the contract and in accordance with the decision of the contracting officer.

10. **Term:** This agreement shall remain in effect through the contract period with the understanding that at the end of the first fiscal year the ABC city council has the authority to reappropriate any remaining funds.
11. **Termination of Contract for Cause:** If, through any cause, the Provider shall fail to fulfill in a timely and proper manner its obligations under the contract, or if the Provider shall violate any of the covenants, agreements or stipulations of this contract, the Subgrantor shall thereupon have the right to terminate this contract by giving written notice to the Provider of such termination and specifying the effective date thereof at least 30 days before the effective date of such termination. In that event, all finished or unfinished documents, data, studies, surveys, drawings, maps, models, photographs and reports prepared by the Provider shall become the property of the Subgrantor.

Notwithstanding the above, the Provider shall not be relieved of liability to the Subgrantor for damages sustained by the Subgrantor by virtue of any breach of the contract by the Provider and the Subgrantor may withhold any payments to the Provider for the purpose of setoff until such time as the exact amount of damages due to the Subgrantor from the Provider is determined.
12. **Termination for Convenience of the Subgrantor:** The Subgrantor may terminate this contract at any time giving written notice to the Provider of such termination and specifying the effective date thereof, at least 30 days before the effective date of such termination. In that event, all finished or unfinished documents and other materials shall become the property of the Subgrantor. If the contract is terminated by the Subgrantor as provided herein, the Provider will be paid an amount representative of the time the Provider has actually performed under this contract.
13. **Equal Employment Opportunities:** The Provider shall comply with equal employment opportunities as stated in Executive Order 11246, entitled "Equal Employment Opportunity" as amended by Executive Order 11375, and as supplemented in Department of Labor regulations.
14. **Program Income:** Any "Program Income" (as such term is defined under applicable federal regulations) gained from any activity of the Provider, funded by CDBG funds shall be returned to the City.
15. **Religious Organizations or Owned Property:** CDBG funds may be used by religious organizations or on property owned by religious organizations only with prior written approval from the city and only in accordance with requirements set in 24 CFR §570.200(j).
16. **Reversion of Assets:** Within 30 days of the expiration of this agreement, the Provider shall transfer to the city any CDBG funds on hand at the time of expiration and any accounts receivable attributable to the use of CDBG funds. Any real property under the Provider's control that was

Figure 3 (continued)

acquired or improved in whole or in part with CDBG funds in excess of \$25,000 shall be used or disposed of in accordance with 24 CFR §570.503 (A)(8).

17. **Conformity to HUD Regulations:** The Provider agrees to abide by guidelines set forth by the U.S. Department of Housing and Urban Development for the administration and implementation of the Community Development Block Grant Program, including applicable Uniform Administrative Requirements set forth in 24 CFR §570.502, and applicable federal laws and regulations in 24 §CFR 570.600, *et. seq.*

In this regard, the Provider agrees that duly authorized representatives of the U.S. Department of Housing and Urban Development shall have access to any books, documents, papers and records of the Provider that are directly pertinent to this agreement for the purpose of making audits, examinations, excerpts and transcriptions.

18. **Examination of Records:**

- (A) The Provider agrees to make available books, records, documents and other evidence pertaining to the costs and expenses of this contract (hereinafter collectively called the "records") to the extent of such detail as will properly reflect all net costs, direct and indirect labor, materials, equipment, supplies and services, and other costs and expenses of whatever nature for which reimbursement is claimed under the provisions of this contract.
- (B) The Provider agrees to make available at the office of the Provider at all reasonable times during the period of this contract any books, documents, papers or records of the Provider that directly pertain to, and involve transactions relating to this contract or subcontract hereunder for inspection, audit or reproduction by an authorized representative of the Subgrantor or the Department of Housing and Urban Development.
- (C) The Provider shall preserve and make available its records until expiration of three years after final payment under this contract or for such longer period, if any, as is required by applicable statute, by any other clause of this contract, or by (1) or (2) below.
- (1) If this contract is completely or partially terminated, the records relating to the work terminated shall be preserved and made available until expiration of three years from the date of the resulting final settlement.
- (2) Records that related to (i) appeals under the "Disputes" clause of this contract, (ii) litigation or the settlement of claims arising out of the performance of this contract, (iii) cost and expenses of this contract as to which exception has been taken by the auditor of the Department of Housing and Urban Development or any of its duly authorized representatives, shall be retained by the Provider under such appeals, litigation, claims, or exceptions have been disposed of.
- (D) The Provider further agrees to include in each of its subcontracts hereunder, a provision to the effect that the subcontractor agrees that the auditor of the Department of Housing and Urban Development or any of its duly authorized representatives shall, until the expiration of three years after final payment under the contract, have right to examine any books, documents, papers, and records of such subcontractor that directly pertain to, and involve transactions relating to the subcontract. The term "subcontractor", as used in his paragraph only excludes (i) purchase orders not exceeding \$2,500 and (ii) subcontracts or purchase of public utility services with rates established for uniform applicability to the general public.

19. **Insurance to be Provided by Provider:** The Provider must, prior to the contract, file with the Subgrantor certificates or policies of workers' compensation, public liability, automobile liability (including non-ownership and hired vehicles) and property damage insurance satisfactory to the

Appendix A: Sample Subaward Agreements

Figure 3 (continued)

Subgrantor and in compliance with the law, and in form and amount sufficient to protect the Subgrantor. Each certificate or policy shall carry the provision that the insurance shall not be canceled or reduced without prior notice to the Subgrantor. All insurance required by this paragraph of the contract shall be and remain in full force and effect for the entire contract period, and the Subgrantor shall be named as an additional insured under such insurance contracts, which shall contain a stipulation that the insurance provided shall not terminate, lapse or otherwise expire, prior to thirty (30) days written notice to that effect, given by the insurance carrier to the Subgrantor, and that the insurance carrier will not invoke the defense of performance of a governmental function by the Provider in performing this contract.

The minimum limits of liability coverage shall be as follows:

- (A) Comprehensive general liability, including premises and operations; elevator liability; providers protective liability; products liability including completed operations coverage; and contractual liability for this contract.

Limits: \$1,000,000/2,000,000
(per occurrence/annual aggregate)

- (B) Comprehensive automobile liability, including all owned automobiles; non-owned automobiles; hired car coverage.

Limits: \$500,000/1,000,000
(per occurrence/annual aggregate)

- (C) Workers' compensation, including employer's liability.

Limits: Statutory
Employer's Liability \$100,000

This agreement, shall be binding upon all parties hereto and their respective heirs, executors, administrators, successors and assigns.

In witness thereof, the parties hereto leave executed or caused to be executed by their duly authorized officials, this agreement in five (5) copies, each of which shall be deemed an original on the date first above written.

CITY OF ABC

City Manager

SIGNATURE

FUNDS AVAILABLE

DIRECTOR OF FINANCE

APPROVED AS TO FORM:

CITY ATTORNEY

PROVIDER AGENCY

TYPED NAME AND TITLE

Figure 3 (continued)

CDBG CONTRACT

_____, 19__ - _____, 19__

Attachment I

Program Services and Goals

DESCRIPTION OF PROGRAM

PROGRAM GOAL

Appendix A: Sample Subaward Agreements

Figure 3 (continued)

CDBG Contract

_____, 19__ - _____, 19__

**Attachment II
Budget**

Block Grant Budget for 19__ - __ Contract
Contract Amount \$

	Average Cost Per Unit		Total
Materials:	\$ _____	x	_____
Program Support:			
Crew Labor	_____		_____
Warehouse	_____		_____
Tools/Equipment	_____		_____
Vehicle Expense	_____		_____
Non-Crew Labor	_____		_____
Total Materials & Program Support:	_____		_____
Administration:	_____		_____
Indirect Costs:	_____		_____
Totals:	_____		_____

Figure 3 (continued)

Attachment III
Guidelines for Financial Management of CDBG-Funded Activities

To comply with federal regulations, each program must have a financial management system that provides accurate, current and complete disclosure of the financial status of the activity. This means the financial system must be capable of generating regular financial status reports which indicate the dollar amount allocated for each activity (including any budget revisions), amount obligated (i.e., for which contract exists), and the amount expended for each activity. The system must permit the comparison of actual expenditures and revenues against budgeted amounts. The city must be able to isolate and to trace every CDBG dollar received and prove where it went and for what it was used.

Accounting records must be supported by source documentation. Invoices, bills of lading, purchase vouchers, payrolls and the like must be secured and retained for four years in order to show for what purpose funds were spent. Payments should not be made without invoices and vouchers physically in hand. All vouchers/invoices should be on vendors' letterhead.

All employees paid in whole or in part from CDBG funds should prepare a time sheet indicating the hours worked on CDBG projects for each pay period. Based on these time sheets and the hourly payroll costs for each employee, a voucher statement indicating the distribution of payroll charges should be prepared and placed in the appropriate files.

The city is responsible for reviewing and certifying the financial management of any operating agency which is not a city department or bureau, in order to determine whether or not it meets all of the above requirements. If the agency's system does not meet these requirements and modifications are not possible, the city must administer the CDBG funds for the operating agency.

Financial records are to be retained for a period of four years, with access guaranteed to HUD or Treasury officials or their representative.

One copy of the vendors' audited financial statement shall be submitted to the city immediately following the end of the vendors' fiscal year(s) during which CDBG funds are received.

Payment to providers will be on a reimbursement basis to be submitted to:

Grants Coordinator

Street Address

City, State, Zip

Requests are to be submitted on Provider's letterhead in a format consistent with the budget attachment, including an analysis of expenses to budget. A cash advance may be available upon special request.

Figure 3 (continued)

Attachment IV
Applicable Federal Regulations

Compliance with Section 109 of the Housing and Community Development Act of 1974

The work to be performed under this contract is subject to the requirements of Section 109 of the Housing and Community Development Act of 1974, which states that:

"No person in the United States shall, on the ground of race, color, national origin, sex or handicap, be excluded from participation in, be denied the benefits of or be subjected to discrimination under any program or activity funded in whole or in part with funds available under this title."

Compliance with the Equal Opportunity Provisions of Executive Order No. 11246

In carrying out the contract, the contractor shall not discriminate against any employee or applicant for employment because of race, color, religion, sex, handicap or national origin. The contractor shall take affirmative action to insure that applicants for employment are employed, and that employees are treated during employment, without regard to their race, color, religion, sex, handicap or national origin. Such action shall include, but not be limited to, the following: employment, upgrading, demotion or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The contractor shall post in conspicuous places, available to employees and applicants for employment, notices to be provided by the government setting forth the provisions of this nondiscrimination clause. The contractor shall state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex, handicap or national origin.

Compliance with Section 3 of the Housing and Urban Development Act of 1968

During the performance of this contract the contractor agrees as follows:

- A. The work to be performed under this contract is on a project assisted under a program providing direct federal financial assistance from the Department of Housing and Urban Development and is subject to the requirements of Section 3 of the Housing and Urban Development Act of 1968, as amended, 12 U.S.C. 1701u. Section 3 requires that, to the greatest extent feasible, opportunities for training and employment be given lower income residents of the project area and contracts for work in connection with the project be awarded to business concerns which are located in, or owned in substantial part, by persons in the area of the project.
- B. The parties to this contract will comply with the provisions of said Section 3 and the regulations issued pursuant thereto by the Secretary of Housing and Urban Development set forth in 24 CFR, and all applicable rules and orders of the Department issued thereunder prior to the execution of this contract. The parties to this contract certify and agree that they are under no contractual or other disability which would prevent them from complying with these requirements.
- C. The contractor will send to each labor organization or representative of workers with which he has a collective bargaining agreement or other contract or understanding, if any, a notice advising the said labor organization or workers representative of his commitments under this Section 3 clause and shall post copies of the notice in conspicuous places available to employees and applicants for employment or training.
- D. The contractor will include this Section 3 clause in every subcontract for work in connection with the project and will, at the direction of the applicant for, or recipient of federal financial assistance, take appropriate action pursuant to the subcontract upon a finding that the subcontractor is in violation of regulations issued by the secretary of Housing and Urban Development, 24 CFR. The contractor will not subcontract with any subcontractor where it has notice or knowledge that the latter has been found in violation of regulations under 24 CFR and will not let any subcontract

Figure 3 (continued)

unless the subcontractor has first provided it with a preliminary statements of ability to comply with the requirements of these regulations.

- E. Compliance with the provisions of section 3, the regulations set forth in 24 CFR, and all applicable rules and orders of the department issued thereunder prior to the execution of the contract, shall be a condition of the federal financial assistance provided to the project, binding upon the applicant or recipient of such assistance, its successors and assigns. Failure to fulfill these requirements shall subject the applicant or recipient for such assistance, its successors and assigns to those sanctions specified by the grant or loan agreement or contract through which federal assistance is provided, and to such sanctions as are specified by 24 CFR Part 135.

Conflict of Interest

No member of the governing body, or employee of the City of ABC or its designees or agents, and no other public official of such locality who exercises any functions or responsibilities with respect to the Community Development Block Grant Program, during his tenure or for one year thereafter, shall have any interest, direct or indirect, in this contract, or any subcontracts or the proceeds thereof.

Compliance with Lead-Based Paint Regulations

All construction, rehabilitation, or modernization of residential structures provided under this contract shall comply with the provisions of the Lead-Based Paint Poisoning Prevention Act (84 Stat. 2080; 42 USC 4841(3)) and the regulations thereunder (24 CFR Part 35).

Compliance with Section 504 of the Rehabilitation Act of 1973, as amended

The work to be performed under this contract is subject to the requirement of Section 504 of the Rehabilitation Act of 1973, as amended, which states that: "No otherwise qualified handicapped individual in the United States . . . shall, solely by reason of his handicap, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal financial assistance or under any program or activity conducted by any executive agency."

Figure 4

PROTOTYPE OF A FEDERAL SUBAWARD AGREEMENT

University of California, Berkeley
UCB Agreement Number _____

This Agreement is entered into by and between The Regents of the University of California, for the Berkeley campus "California" and "Institution." This agreement is for the performance of a portion of the work originally awarded to California from "Granting Agency" "grant _____" under the direction of Principal Investigator "P.I.'s Name," the parties agree to the following terms and conditions:

ARTICLE I. STATEMENT OF WORK: "Institution" shall exercise its best efforts to carry out the program indicated in Exhibit A, which is incorporated herein and made a part of this agreement.

ARTICLE II. PERIOD OF PERFORMANCE: The period of performance shall be from "begin date" to "end date." These dates are subject to "Granting Agency's" continued support of California.

ARTICLE III. CONSIDERATION: California will reimburse "Institution" actual costs for the performance of work under this agreement in the amount not to exceed \$ _____ which is based on the budget incorporated into this agreement as Exhibit B.

ARTICLE IV. PAYMENTS: California will reimburse "Institution" upon receipt of monthly invoices provided by "Institution." Invoices shall identify expenditures by major budget categories (i.e., salaries, fringe benefits, equipment, travel, supplies, etc.) as provided in Exhibit B. Invoices shall be dated, numbered, make reference to UCB Agreement Number _____ and be mailed to:

"Administrator's Name," "Administering Unit," "Address," University of California

ARTICLE V. PROJECT MANAGEMENT: For technical matters: California's principal investigator "P.I. name" is responsible for the overall conduct of the project. PI is responsible for technical monitoring and guidance.

"Institution's" "P.I. name" is responsible for "Institution's" portion of the project. No substitution may be made of "Institution" principal investigator without prior written approval from California.

For Business Matters:

- For California: "Senior Research Administrator," Sponsored Projects Office, UCB
- For "Institution": "Institution," Authorized Official

ARTICLE VI. REPORTS: "Institution" shall furnish California technical progress reports as required by California's P.I. Final technical report shall be submitted to California within 60 days of the project end date or within 60 days of the termination date whichever comes first. Reports are to be submitted to:

"Principal Investigator's Name," "Address"

ARTICLE VII. COPYRIGHT/PATENT: "Institution" may assert copyright on materials that it produces in the performance of the work of this agreement. California and "Agency" shall have the right to a non-transferable, irrevocable, worldwide, royalty-free, non-exclusive license to use, reproduce, publish or re-publish, or otherwise disseminate such copyrighted materials.

The standard patent rights clause found at [insert applicable federal agency regulation citation] is incorporated herein by reference.

Source: University of California, Berkeley, http://www.spo.berkeley.edu/Forms/model_agree/subgrant.html.

Figure 4 (continued)

ARTICLE VIII. RECORD RETENTION: Financial record, supporting documents and other record pertaining to this agreement shall be maintained and retained by "Institution" for a period of three years from the termination date of this agreement.

ARTICLE IX. PUBLICATIONS: "Institution" agrees that all publications that result from work under this agreement will acknowledge that the project was supported by "Grant No. XXX" under a grant from "Granting Agency."

ARTICLE X. SUSPENSION/TERMINATION: In the event the "Granting Agency" suspends its grant to California, California shall suspend this agreement to "Institution." Notification of suspension shall be in writing from California. California will be unable to reimburse any expenses under suspension unless and until "Granting Agency" reimburses California for such costs.

Either party may terminate this agreement upon thirty days advance written notice to the other party. However, in the event that the "Granting Agency" terminates the grant to California prior to the project's end date as stated in Article II, this agreement will be immediately terminated. In the event of any form of termination, California will reimburse "Institution" for all expenses incurred through the date of termination.

ARTICLE XI. GENERAL PROVISIONS AND CERTIFICATIONS: All terms and conditions set forth in "Granting Agency's" policies "X,Y,Z" shall apply to this agreement and are incorporated herein by reference.

In addition "Institution" certifies that:

1. It is not delinquent on the repayment of any federal debt.
2. It is presently not debarred, suspended, proposed for debarment, declared ineligible, nor voluntarily excluded from covered transactions by any federal department or agency.
3. It is in compliance with the Drug-Free Work Place Act of 1988.
4. It is in compliance with P.L. 101-122, Section 1352 which covers restrictions regarding lobbying.
5. It has filed the assurances required under PHS final rule entitled "Responsibilities of Awardee and Applicant Institution for Dealing with and Reporting Possible Misconduct in Science."
6. It is in compliance with the federal financial disclosure requirements (PHS/NSF only).

ARTICLE XII. CHANGES: This agreement constitutes the entire agreement between the parties regarding the subject matter herein. Any modification to this agreement shall be made in writing and must be signed by the authorized representatives of both parties.

FOR INSTITUTION

By: _____ (signature) _____ (title)
_____ (typed name) _____ (date signed)

FOR THE REGENTS OF THE UNIVERSITY OF CALIFORNIA

By: _____ (signature) _____ (title)
_____ (typed name) _____ (date signed)

Figure 4 (continued)

**Exhibit A
Scope of Work**

[Insert approved scope of work proposed by "Institution"]

Figure 4 (continued)

**Exhibit B
Budget**

[Insert approved budget]

Figure 5

SAMPLE SUBAGREEMENT BETWEEN A UNIVERSITY AND A SUBAWARDEE

When the University has received a federal contract or grant and needs to assign work to a commercial collaborator/participant, and arrange for payment of their costs under the grant, it should use this subagreement.

This is intended as a starting draft. Not all clauses, definitions, etc. will be applicable to any specific transaction. This document MUST be tailored to the specific transaction through extensive consultation with the campus requester and interactive negotiation and understandings between the subawardee, research administrator and principle investigator.

SUBAGREEMENT NO.

between

THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, BERKELEY

and

[INSERT SUBAWARDEE NAME]

THIS SUBAGREEMENT is made and entered into this _____ 1997, by and between THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, BERKELEY ("California") and ("Subawardee").

WHEREAS, California has received funding from the ("Sponsor"), under (grant/contract) number _____ and _____

WHEREAS, California's effort requires the participation of Subawardee as set forth in the proposal which resulted in the above award;

NOW THEREFORE, in consideration of the mutual promises set forth below, California and Subawardee agree as follows:

ARTICLE I. STATEMENT OF WORK

- A. INTRODUCTION: Subawardee shall exercise its best efforts to carry out the program of research described in Exhibit A, which is incorporated herein and made a part of this agreement.
- B. DELIVERABLES:

ARTICLE II. PERIOD OF PERFORMANCE

The authorized period of performance of this subagreement is from _____ through _____.

Add, if appropriate: It is anticipated that this subagreement will be amended annually/periodically to add additional performance/budget periods with an ultimate end date of _____.

ARTICLE III. COST, BILLING, AND PAYMENT

- A. (i) This subagreement provides for payment on a cost-reimbursement basis. The total estimated cost shall be in general accordance with the budget attached as Exhibit B.

Source: University of California, Berkeley, [http://www.spo.berkeley.edu/Forms/model agree/industry.html](http://www.spo.berkeley.edu/Forms/model_agree/industry.html).

Figure 5 (continued)

(ii) The amount authorized for expenditure (under this allotment) is \$ _____. This amount shall not be exceeded unless this subagreement is amended to add additional funds.

Add, if appropriate:

(iii) The (award under which this subagreement is written is expected to have a duration longer than that authorized in Article II above, and the) total award amount authorized is expected to be increased in accordance with the proposal and Exhibit B. Subawardee is not obligated to continue work in excess of the amount reflected in Paragraph A-ii above, and California is not obligated to reimburse costs in excess of that amount unless this subagreement is amended to increase the amount of Paragraph A-ii.

- B. Subawardee may bill California monthly for reimbursement of actual costs incurred in the performance of this Subagreement. Invoices shall be numbered, dated, cite this subagreement number, show cost incurred by budget category (i.e., salaries, fringe benefits, equipment, travel, supplies, etc.) for the billing period and cumulative to date, and be submitted to: [insert address]
- C. California will make provisional payment on all invoices submitted in accordance with the terms of this agreement. The final invoice, clearly marked "Final," must be submitted within 90 days after the expiration date of this agreement. The final invoice shall include the following certification: "Payment of this final invoice shall constitute complete satisfaction of all of California's obligations under this agreement and Subawardee releases and discharges California from all further claims and obligations upon payment hereof."

ARTICLE IV. RECORDS AND AUDITS

Subawardee shall maintain accurate records of all costs incurred in the performance of this work and agrees to allow representatives of California and Sponsor reasonable access to its records to verify the validity of expenses reimbursed under this subagreement. Subawardee hereby warrants that it conducts audits as required by OMB Circulars, federal cost principles, or cost accounting standards applicable to its performance as a recipient of U.S. government funds and that such audit has revealed no material findings. Subawardee shall maintain financial records, supporting documents and other records pertaining to this agreement for a period of five years from the termination date of this agreement.

ARTICLE V. PUBLICITY AND PUBLICATION

Subawardee shall not, without the prior written consent of California, issue any press releases or in any manner advertise the fact that Subawardee has entered into this subagreement. All publications resulting from the work under this agreement will acknowledge that the project was supported by the federal award identified in the recitals of this subagreement.

ARTICLE VI. SUBCONTRACTING AND ASSIGNMENT

Subawardee shall perform the work contemplated with resources available within its own organization and no portion of the work shall be subcontracted, nor shall this subagreement be assigned, without the prior written authorization of California. Nothing contained in this subagreement shall create any contractual or agency relationship between a lower tier subawardee or assignee and California.

ARTICLE VII. KEY PERSONNEL

- A. California's principal investigator is Professor _____, who is responsible for the overall conduct of the project, technical monitoring, and guidance.
- B. Subawardee's principal investigator is _____. No substitution may be made by Subawardee without the written consent of California.

ARTICLE VIII. TERMINATION

- A. Either party may terminate this subagreement upon thirty (30) days written notice to the other party. In the event of termination, Subawardee shall be entitled to reimbursement for all costs incurred to

Figure 5 (continued)

the date of termination and for all uncancellable obligations. In no event, however, shall the termination settlement cause the total amount paid to Subawardee to exceed the estimated cost set forth in Paragraph A of Article III above.

- B. Within 60 days of the effective date of termination, Subawardee shall submit to California a final report, a final financial report and final invoice.

ARTICLE IX. CHANGES

California, within the general scope of this subagreement, may, at any time, by written notice to Subawardee, issue additional instructions, require additional services or direct the omission of services covered by this subagreement. In such event, there will be made an equitable adjustment in price and time of performance, but any claim for such an adjustment must be made within thirty (30) days of the receipt of said written notice.

ARTICLE X. INDEMNIFICATION

- A. California shall defend, indemnify and hold Subawardee, its officers, employees and agents harmless from and against any and all liability, loss, expense (including reasonable attorneys' fees) or claims for injury or damages arising out of the performance of this subagreement but only in proportion to and to the extent such liability, loss, expense, attorneys' fees or claims for injury or damages are caused by or result from the negligent or intentional acts or omissions of California, its officers, agents or employees.
- B. Subawardee shall defend, indemnify and hold California, its officers, employees and agents harmless from and against any and all liability, loss, expense (including reasonable attorneys' fees), or claims for injury or damages arising out of the performance of this subagreement but only in proportion to and to the extent such liability, loss, expense, attorneys' fees or claims for injury or damages are caused by or result from the negligent or intentional acts or omissions of Subawardee, its officers, agents or employees.

ARTICLE XI. DATA RIGHTS

Subawardee holds all rights, title, and interest in the data and works it creates in the performance of this subagreement. Subawardee hereby grants to California, a royalty-free non-exclusive, irrevocable license to reproduce, translate, publish, use and dispose of, and to authorize others to do so, all data collected. As used in this clause, data collected means the original records of scientific and technical data collected during the performance of the work by the principal investigator or the project personnel. Data collected includes, but is not limited to, notebooks, drawings, lists, specifications and computations, in written, pictorial, graphic or machine form.

ARTICLE XII. PATENT RIGHTS

This subagreement is funded by an award from the U.S. Government. Subawardee is therefore granted patent rights in accordance with 37 CFR Part 401 or FAR §52.227-11, or in accordance with FAR §52.227-12 if it is a commercial entity and the prime federal sponsor is the U.S. Department of Defense or National Aeronautics and Space Administration.

ARTICLE XIII. CONFIDENTIALITY

It is expected that the work of this subagreement can be carried out without any of the parties disclosing confidential information to the other parties. However, should it become necessary to disclose confidential information, the parties will notify each other in advance of the disclosure and will negotiate in good faith with respect to protecting such confidential information.

Figure 5 (continued)

ARTICLE XIV. DISPUTES

Any dispute arising under this subagreement which is not settled by subagreement of the parties may be settled by mediation, arbitration, or other appropriate legal proceedings. Pending any decision, appeal or judgment in such proceedings or the settlement of any dispute arising under this subagreement, Subawardee shall proceed diligently with the performance of this subagreement in accordance with the decision of California.

ARTICLE XV. INDEPENDENT CONTRACTOR

Subawardee and its employees, consultants, agents or independent contractors will perform all services under this agreement as independent contractors. Nothing in this agreement will be deemed to create an employer-employee or principal-agent relationship between California and Subawardee's employees, consultants, agents or independent contractors. Subawardee and its employees, consultants, agents and lower tier subawardees will not, by virtue of any services provided under this agreement, be entitled to participate, as an employee or otherwise, in or under any employee benefit plan of California or any other employment right or benefit available to or enjoyed by employees of California.

ARTICLE XVI. GENERAL PROVISIONS AND CERTIFICATIONS

If this subagreement is a Subaward under a federal grant or cooperative agreement, Subawardee certifies that:

1. It is not delinquent on the repayment of any federal debt.
2. It is presently not debarred, suspended, proposed for debarment, declared ineligible nor voluntarily excluded from covered transactions by any federal department or agency.
3. It is in compliance with the Drug-Free Work Place Act of 1988.
4. It is in compliance with P.L. 101-122, Section 1352, which covers restrictions regarding lobbying.
5. It has filed the assurances required under PHS final rule entitled "Responsibilities of Awardee and Applicant Institution for Dealing with and Reporting Possible Misconduct in Science."
6. It is in compliance with the federal financial disclosure requirements (PHS/NSF only).

ARTICLE XVII. PRIME AWARD PROVISIONS AND ATTACHMENTS

The following provisions of the prime award to California are incorporated by attachment, and are applicable to Subawardee and Subawardee's lower tier subagreements:

If this is written under a contract, you can use the list prepared by OP, located at (<http://www.ucop.edu/matmgt/matmgt/supp5.html>) and add any additional provisions from the prime award under which this is written. If using the OP list, delete FAR §52.215-26 and FAR §52.222-1 (pursuant to FAC 90-43).

ARTICLE XVIII. INTEGRATION

This subagreement states the entire contact between the parties in respect to the subject matter of the subagreement and supersedes any previous written or oral representations, statements, negotiations, or agreements. This subagreement may be modified only by written agreement executed by authorized representatives of both parties.

Appendix A: Sample Subaward Agreements

Figure 5 (continued)

IN WITNESS WHEREOF, the parties hereto have caused this subagreement to be executed by their duly authorized representatives.

FOR

("Subawardee")

THE REGENTS OF THE UNIVERSITY
OF CALIFORNIA, BERKELEY
("California")

By: _____

By: _____

Name: _____

Name: _____

Title: _____

Title: _____

Date: _____

Date: _____

Figure 5 (continued)

**Exhibit A
Scope of Work**

[Insert approved scope of work]

Figure 5 (continued)

**Exhibit B
Budget**

[Insert approved budget]

Appendix B: Excerpts from OMB Circulars

The following are excerpts of OMB circulars that are particularly relevant to subrecipient monitoring issues. They address the pass-through entity's responsibility to monitor subrecipients, prior approval provisions and related-audit requirements. There may be other provisions that affect individual subawards. Readers, therefore, may find it useful to review the circulars in their entirety. The circulars are available on the Internet at OMB's home page, <http://www.whitehouse.gov/OMB/grants/index.html>, or from the Government Printing Office, (202) 512-1800.

OMB Circular A-110, *Uniform Administrative Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals and Other Nonprofit Organizations*

General

§__.5 Subawards.

Unless sections of this circular specifically exclude subrecipients from coverage, the provisions of this circular shall be applied to subrecipients performing work under awards if such subrecipients are institutions of higher education, hospitals or other nonprofit organizations. State and local government subrecipients are subject to the provisions of regulations implementing the grants management common rule, "Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments," published at 53 FR 8034 (March 11, 1988).

§__.13 Debarment and suspension.

Federal awarding agencies and recipients shall comply with the nonprocurement debarment and suspension common rule implementing Executive Orders 12549 and 12689, "Debarment and Suspension." This common rule restricts subawards and contracts with certain parties that are debarred, suspended or otherwise excluded from or ineligible for participation in federal assistance programs or activities.

§__.51 Monitoring and reporting program performance.

(a) Recipients are responsible for managing and monitoring each project, program, subaward, function or activity supported by the award. Recipients shall monitor subawards to ensure subrecipients have met the audit requirements as delineated in §__.26.

Special Conditions

§__.14 Special award conditions.

If an applicant or recipient: (a) has a history of poor performance, (b) is not financially stable, (c) has a management system that does not meet the standards prescribed in this circular, (d) has not conformed to the terms and conditions of a previous award, or (e) is not otherwise responsible, Federal awarding agencies may impose additional requirements as needed, provided that such applicant or recipient is notified in writing as to: the nature of the additional requirements, the reason why the additional requirements are being imposed, the nature of the corrective action needed, the time allowed for completing the corrective actions, and the method for requesting reconsideration of the additional requirements imposed. Any special conditions shall be promptly removed once the conditions that prompted them have been corrected.

Prior Approvals

§__.25 Revision of budget and program plans.

(a) The budget plan is the financial expression of the project or program as approved during the award process. It may include either the federal and nonfederal share, or only the federal share, depending

Appendix B: Excerpts from OMB Circulars

upon federal awarding agency requirements. It shall be related to performance for program evaluation purposes whenever appropriate.

(b) Recipients are required to report deviations from budget and program plans, and request prior approvals for budget and program plan revisions, in accordance with this section.

(c) For nonconstruction awards, recipients shall request prior approvals from federal awarding agencies for one or more of the following program or budget related reasons.

(1) Change in the scope or the objective of the project or program (even if there is no associated budget revision requiring prior written approval).

(2) Change in a key person specified in the application or award document.

(3) The absence for more than three months, or a 25 percent reduction in time devoted to the project, by the approved project director or principal investigator.

(4) The need for additional federal funding.

(5) The transfer of amounts budgeted for indirect costs to absorb increases in direct costs, or vice versa, if approval is required by the federal awarding agency.

(6) The inclusion, unless waived by the federal awarding agency, of costs that require prior approval in accordance with OMB Circular A-21, "Cost Principles for Institutions of Higher Education," OMB Circular A-122, "Cost Principles for Nonprofit Organizations," or 45 CFR Part 74 Appendix E, "Principles for Determining Costs Applicable to Research and Development under Grants and Contracts with Hospitals," or 48 CFR Part 31, "Contract Cost Principles and Procedures," as applicable.

(7) The transfer of funds allotted for training allowances (direct payment to trainees) to other categories of expense.

(8) Unless described in the application and funded in the approved awards, the subaward, transfer or contracting out of any work under an award. This provision does not apply to the purchase of supplies, material, equipment or general support services.

(d) No other prior approval requirements for specific items may be imposed unless a deviation has been approved by OMB.

(e) Except for requirements listed in paragraphs (c)(1) and (c)(4) of this section, federal awarding agencies are authorized, at their option, to waive cost-related and administrative prior written approvals required by this circular and OMB Circulars A-21 and A-122. Such waivers may include authorizing recipients to do any one or more of the following.

(1) Incur pre-award costs 90 calendar days prior to award or more than 90 calendar days with the prior approval of the federal awarding agency. All pre-award costs are incurred at the recipient's risk (i.e., the federal awarding agency is under no obligation to reimburse such costs if for any reason the recipient does not receive an award or if the award is less than anticipated and inadequate to cover such costs).

(2) Initiate a one-time extension of the expiration date of the award of up to 12 months unless one or more of the following conditions apply. For one-time extensions, the recipient must notify the federal awarding agency in writing with the supporting reasons and revised expiration date at least 10 days before the expiration date specified in the award. This one-time extension may not be exercised merely for the purpose of using unobligated balances.

(i) The terms and conditions of award prohibit the extension.

(ii) The extension requires additional federal funds.

(iii) The extension involves any change in the approved objectives or scope of the project.

Appendix B: Excerpts from OMB Circulars

(3) Carry forward unobligated balances to subsequent funding periods.

(4) For awards that support research, unless the federal awarding agency provides otherwise in the award or in the agency's regulations, the prior approval requirements described in paragraph (e) are automatically waived (i.e., recipients need not obtain such prior approvals) unless one of the conditions included in paragraph (e)(2) applies.

(f) The federal awarding agency may, at its option, restrict the transfer of funds among direct cost categories or programs, functions and activities for awards in which the federal share of the project exceeds \$100,000 and the cumulative amount of such transfers exceeds or is expected to exceed 10 percent of the total budget as last approved by the federal awarding agency. No federal awarding agency shall permit a transfer that would cause any federal appropriation or part thereof to be used for purposes other than those consistent with the original intent of the appropriation.

(g) All other changes to nonconstruction budgets, except for the changes described in paragraph (j), do not require prior approval.

(h) For construction awards, recipients shall request prior written approval promptly from federal awarding agencies for budget revisions whenever (1), (2) or (3) apply.

(1) The revision results from changes in the scope or the objective of the project or program.

(2) The need arises for additional federal funds to complete the project.

(3) A revision is desired which involves specific costs for which prior written approval requirements may be imposed consistent with applicable OMB cost principles listed in §__.27.

(i) No other prior approval requirements for specific items may be imposed unless a deviation has been approved by OMB.

(j) When a federal awarding agency makes an award that provides support for both construction and nonconstruction work, the federal awarding agency may require the recipient to request prior approval from the federal awarding agency before making any fund or budget transfers between the two types of work supported.

(k) For both construction and nonconstruction awards, federal awarding agencies shall require recipients to notify the federal awarding agency in writing promptly whenever the amount of federal authorized funds is expected to exceed the needs of the recipient for the project period by more than \$5,000 or five percent of the federal award, whichever is greater. This notification shall not be required if an application for additional funding is submitted for a continuation award.

(l) When requesting approval for budget revisions, recipients shall use the budget forms that were used in the application unless the federal awarding agency indicates a letter of request suffices.

(m) Within 30 calendar days from the date of receipt of the request for budget revisions, federal awarding agencies shall review the request and notify the recipient whether the budget revisions have been approved. If the revision is still under consideration at the end of 30 calendar days, the federal awarding agency shall inform the recipient in writing of the date when the recipient may expect the decision.

Audits

§__.26 Nonfederal audits.

(a) Recipients and subrecipients that are institutions of higher education or other nonprofit organizations (including hospitals) shall be subject to the audit requirements contained in the Single Audit Act Amendments of 1996 (31 U.S.C. §§7501-7507) and revised OMB Circular A-133, "Audits of States, Local Governments, and Nonprofit Organizations."

Appendix B: Excerpts from OMB Circulars

(b) State and local governments shall be subject to the audit requirements contained in the Single Audit Act Amendments of 1996 (31 U.S.C. §§7501-7507) and revised OMB Circular A-133, "Audits of States, Local Governments, and Nonprofit Organizations."

(c) For-profit hospitals not covered by the audit provisions of revised OMB Circular A-133 shall be subject to the audit requirements of the federal awarding agencies.

(d) Commercial organizations shall be subject to the audit requirements of the federal awarding agency or the prime recipient as incorporated into the award document.

Grants Management Common Rule, Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments

General

§ ____.35 Subawards to debarred and suspended parties.

Grantees and subgrantees must not make any award or permit any award (subgrant or contract) at any tier to any party which is debarred or suspended or is otherwise excluded from or ineligible for participation in federal assistance programs under Executive Order 12549, "Debarment and Suspension."

§ ____.37 Subgrants.

(a) *States.* States shall follow state law and procedures when awarding and administering subgrants (whether on a cost reimbursement or fixed amount basis) of financial assistance to local and Indian tribal governments. States shall:

- (1) Ensure that every subgrant includes any clauses required by federal statute and executive orders and their implementing regulations;
- (2) Ensure that subgrantees are aware of requirements imposed upon them by federal statute and regulation;
- (3) Ensure that a provision for compliance with Section ____.42 is placed in every cost reimbursement subgrant; and
- (4) Conform any advances of grant funds to subgrantees substantially to the same standards of timing and amount that apply to cash advances by federal agencies.

(b) *All other grantees.* All other grantees shall follow the provisions of this part which are applicable to awarding agencies when awarding and administering subgrants (whether on a cost reimbursement or fixed amount basis) of financial assistance to local and Indian tribal governments. Grantees shall:

- (1) Ensure that every subgrant includes a provision for compliance with this part;
- (2) Ensure that every subgrant includes any clauses required by federal statute and executive orders and their implementing regulations; and
- (3) Ensure that subgrantees are aware of requirements imposed upon them by federal statutes and regulations.

(c) *Exceptions.* By their own terms, certain provisions of this part do not apply to the award and administration of subgrants:

- (1) Section ____.10;
- (2) Section ____.11;
- (3) The letter-of-credit procedures specified in Treasury regulations at 31 CFR Part 205, cited in § ____.21; and
- (4) Section ____.50.

§ ____.40 Monitoring and reporting program performance.

(a) *Monitoring by grantees.* Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity.

Special Conditions

§ ____ .12 Special grant or subgrant conditions for "high-risk" grantees.

(a) A grantee or subgrantee may be considered "high risk" if an awarding agency determines that a grantee or subgrantee:

- (1) Has a history of unsatisfactory performance;
- (2) Is not financially stable;
- (3) Has a management system which does not meet the management standards set forth in this part;
- (4) Has not conformed to terms and conditions of previous awards; or
- (5) Is otherwise not responsible; and if the awarding agency determines that an award will be made, special conditions and/or restrictions shall correspond to the high risk condition and shall be included in the award.

(b) Special conditions or restrictions may include:

- (1) Payment on a reimbursement basis;
- (2) Withholding authority to proceed to the next phase until receipt of evidence of acceptable performance within a given funding period;
- (3) Requiring additional, more detailed financial reports;
- (4) Additional project monitoring;
- (5) Requiring the grantee or subgrantee to obtain technical or management assistance; or
- (6) Establishing additional prior approvals.

(c) If an awarding agency decides to impose such conditions, the awarding official will notify the grantee or subgrantee as early as possible, in writing, of:

- (1) The nature of the special conditions/restrictions;
- (2) The reason(s) for imposing them;
- (3) The corrective actions which must be taken before they will be removed and the time allowed for completing the corrective actions; and
- (4) The method of requesting reconsideration of the conditions/restrictions imposed.

Prior Approvals

§ ____ .30 Changes.

(a) *General.* Grantees and subgrantees are permitted to rebudget within the approved direct cost budget to meet unanticipated requirements and may make limited program changes to the approved project. However, unless waived by the awarding agency, certain types of post-award changes in budgets and projects shall require the prior written approval of the awarding agency.

(b) *Relation to cost principles.* The applicable cost principles (see § ____ .22) contain requirements for prior approval of certain types of costs. Except where waived, those requirements apply to all grants and subgrants even if paragraphs (c) through (f) of this section do not.

(c) *Budget changes.* (1) *Nonconstruction projects.* Except as stated in other regulations or an award document, grantees or subgrantees shall obtain the prior approval of the awarding agency whenever any of the following changes is anticipated under a nonconstruction award:

- (i) Any revision which would result in the need for additional funding.

(ii) Unless waived by the awarding agency, cumulative transfers among direct cost categories, or, if applicable, among separately budgeted programs, projects, functions, or activities which exceed or are expected to exceed ten percent of the current total approved budget, whenever the awarding agency's share exceeds \$100,000.

(iii) Transfer of funds allotted for training allowances (i.e., from direct payments to trainees to other expense categories).

(2) Construction projects. Grantees and subgrantees shall obtain prior written approval for any budget revision which would result in the need for additional funds.

(3) Combined construction and nonconstruction projects. When a grant or subgrant provides funding for both construction and nonconstruction activities, the grantee or subgrantee must obtain prior written approval from the awarding agency before making any fund or budget transfer from nonconstruction to construction or vice versa.

(d) *Programmatic changes.* Grantees or subgrantees must obtain the prior approval of the awarding agency whenever any of the following actions is anticipated:

(1) Any revision of the scope or objectives of the project (regardless of whether there is an associated budget revision requiring prior approval).

(2) Need to extend the period of availability of funds.

(3) Changes in key persons in cases where specified in an application or a grant award. In research projects, a change in the project director or principal investigator shall always require approval unless waived by the awarding agency.

(4) Under nonconstruction projects, contracting out, subgranting (if authorized by law) or otherwise obtaining the services of a third party to perform activities which are central to the purposes of the award. This approval requirement is in addition to the approval requirements of § ____.36 but does not apply to the procurement of equipment, supplies, and general support services.

(e) *Additional prior approval requirements.* The awarding agency may not require prior approval for any budget revision which is not described in paragraph (c) of this section.

(f) *Requesting prior approval.* (1) A request for prior approval of any budget revision will be in the same budget form the grantee used in its application and shall be accompanied by a narrative justification for the proposed revision.

(2) A request for a prior approval under the applicable federal cost principles (see § ____.22) may be made by letter.

(3) A request by a subgrantee for prior approval will be addressed in writing to the grantee. The grantee will promptly review such request and shall approve or disapprove the request in writing. A grantee will not approve any budget or project revision which is inconsistent with the purpose or terms and conditions of the federal grant to the grantee. If the revision, requested by the subgrantee would result in a change to the grantee's approved project which requires federal prior approval, the grantee will obtain the federal agency's approval before approving the subgrantee's request.

Audits

§ ____.26 Nonfederal audit.

(a) *Basic Rule.* Grantees and subgrantees are responsible for obtaining audits in accordance with the Single Audit Act Amendments of 1996 (31 U.S.C. §§7501-7507) and revised OMB Circular A-133, "Audits of States, Local Governments, and Nonprofit Organizations." The audits shall be made by an independent auditor in accordance with generally accepted government auditing standards covering financial audits.

(b) *Subgrantees.* State or local governments, as those terms are defined for purposes of the Single Audit Act Amendments of 1996, that provide federal awards to a subgrantee, which expends \$300,000 or more (or other amount as specified by OMB) in federal awards in a fiscal year, shall:

(1) Determine whether state or local subgrantees have met the audit requirements of the act and whether subgrantees covered by OMB Circular A-110, "Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Nonprofit Organizations," have met the audit requirements of the act. Commercial contractors (private for-profit and private and governmental organizations) providing goods and services to state and local governments are not required to have a single audit performed. State and local governments should use their own procedures to ensure that the contractors has complied with laws and regulations affecting the expenditure of federal funds;

(2) Determine whether the subgrantee spent federal assistance funds provided in accordance with applicable laws and regulations. This may be accomplished by reviewing an audit of the subgrantee made in accordance with the act, Circular A-110, or through other means (e.g., program reviews) if the subgrantee has not had such an audit;

(3) Ensure that appropriate corrective action is taken within six months after receipt of the audit report in instance of noncompliance with federal laws and regulations;

(4) Consider whether subgrantee audits necessitate adjustment of the grantee's own records; and

(5) Require each subgrantee to permit independent auditors to have access to the records and financial statements.

(c) *Auditor selection.* In arranging for audit services, §____.36 shall be followed.

Recordkeeping

§____.42 Retention and access requirements for records.

(a) Applicability.

(1) This section applies to all financial and programmatic records, supporting documents, statistical records, and other records of grantees or subgrantees which are:

- (i) Required to be maintained by the terms of this part, program regulations or the grant agreement, or
- (ii) Otherwise reasonably considered as pertinent to program regulations or the grant agreement.

(2) This section does not apply to records maintained by contractors or subcontractors. For a requirement to place a provision concerning records in certain kinds of contracts, see §____.36(i)(10).

(b) Length of retention period.

(1) Except as otherwise provided, records must be retained for three years from the starting date specified in paragraph (c) of this section.

OMB Circular A-133, Audits of States, Local Governments and Nonprofit Organizations

General

§ ____.200 Audit requirements.

(a) *Audit required.* Nonfederal entities that expend \$300,000 or more in a year in federal awards shall have a single or program-specific audit conducted for that year in accordance with the provisions of this part. Guidance on determining federal awards expended is provided in § ____.205.

(b) *Single audit.* Nonfederal entities that expend \$300,000 or more in a year in federal awards shall have a single audit conducted in accordance with § ____.500 except when they elect to have a program-specific audit conducted in accordance with paragraph (c) of this section.

(c) *Program-specific audit election.* When an auditee expends federal awards under only one federal program (excluding research and development (R&D)) and the federal program's laws, regulations, or grant agreements do not require a financial statement audit of the auditee, the auditee may elect to have a program-specific audit conducted in accordance with § ____.235. A program-specific audit may not be elected for R&D unless all of the federal awards expended were received from the same federal agency, or the same federal agency and the same pass-through entity, and that federal agency, or pass-through entity in the case of a subrecipient, approves in advance a program-specific audit.

(d) *Exemption when federal awards expended are less than \$300,000.* Nonfederal entities that expend less than \$300,000 a year in federal awards are exempt from federal audit requirements for that year, except as noted in § ____.215(a), but records must be available for review or audit by appropriate officials of the federal agency, pass-through entity and General Accounting Office (GAO).

Pass-Through and Subrecipient Responsibilities

§ ____.210 Subrecipient and vendor determinations.

(a) *General.* An auditee may be a recipient, a subrecipient, and a vendor. Federal awards expended as a recipient or a subrecipient would be subject to audit under this part. The payments received for goods or services provided as a vendor would not be considered federal awards. The guidance in paragraphs (b) and (c) of this section should be considered in determining whether payments constitute a federal award or a payment for goods and services.

(b) *Federal award.* Characteristics indicative of a federal award received by a subrecipient are when the organization:

- (1) Determines who is eligible to receive what federal financial assistance;
- (2) Has its performance measured against whether the objectives of the federal program are met;
- (3) Has responsibility for programmatic decision making;
- (4) Has responsibility for adherence to applicable federal program compliance requirements; and
- (5) Uses the federal funds to carry out a program of the organization as compared to providing goods or services for a program of the pass-through entity.

(c) *Payment for goods and services.* Characteristics indicative of a payment for goods and services received by a vendor are when the organization:

- (1) Provides the goods and services within normal business operations;
- (2) Provides similar goods or services to many different purchasers;
- (3) Operates in a competitive environment;
- (4) Provides goods or services that are ancillary to the operation of the federal program; and
- (5) Is not subject to compliance requirements of the federal program.

(d) *Use of judgment in making determination.* There may be unusual circumstances or exceptions to the listed characteristics. In making the determination of whether a subrecipient or vendor relationship exists, the substance of the relationship is more important than the form of the agreement. It is not expected that all of the characteristics will be present and judgment should be used in determining whether an entity is a subrecipient or vendor.

(e) *For-profit subrecipient.* Since this part does not apply to for-profit subrecipients, the pass-through entity is responsible for establishing requirements, as necessary, to ensure compliance by for-profit subrecipients. The contract with the for-profit subrecipient should describe applicable compliance requirements and the for-profit subrecipient's compliance responsibility. Methods to ensure compliance for federal awards made to for-profit subrecipients may include pre-award audits, monitoring during the contract and post-award audits.

(f) *Compliance responsibility for vendors.* In most cases, the auditee's compliance responsibility for vendors is only to ensure that the procurement, receipt and payment for goods and services comply with laws, regulations and the provisions of contracts or grant agreements. Program compliance requirements normally do not pass through to vendors. However, the auditee is responsible for ensuring compliance for vendor transactions which are structured such that the vendor is responsible for program compliance or the vendor's records must be reviewed to determine program compliance. Also, when these vendor transactions relate to a major program, the scope of the audit shall include determining whether these transactions are in compliance with laws, regulations and the provisions of contracts or grant agreements.

§ 400 Responsibilities.

* * * * *

(c) *Federal awarding agency responsibilities.* The federal awarding agency shall perform the following for the federal awards it makes:

- (1) Identify federal awards made by informing each recipient of the CFDA title and number, award name and number, award year and if the award is for R&D. When some of this information is not available, the federal agency shall provide information necessary to clearly describe the federal award.
- (2) Advise recipients of requirements imposed on them by federal laws, regulations, and the provisions of contracts or grant agreements.
- (3) Ensure that audits are completed and reports are received in a timely manner and in accordance with the requirements of this part.
- (4) Provide technical advice and counsel to auditees and auditors as requested.
- (5) Issue a management decision on audit findings within six months after receipt of the audit report and ensure that the recipient takes appropriate and timely corrective action.
- (6) Assign a person responsible for providing annual updates of the compliance supplement to OMB.

(d) *Pass-through entity responsibilities.* A pass-through entity shall perform the following for the federal awards it makes:

- (1) Identify federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is R&D, and name of federal agency. When some of this information is not available, the pass-through entity shall provide the best information available to describe the federal award.
- (2) Advise subrecipients of requirements imposed on them by federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.
- (3) Monitor the activities of subrecipients as necessary to ensure that federal awards are used for authorized purposes in compliance with laws, regulations and the provisions of contracts or grant agreements and that performance goals are achieved.

Appendix B: Excerpts from OMB Circulars

- (4) Ensure that subrecipients expending \$300,000 or more in federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
- (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.
- (6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.
- (7) Require each subrecipient to permit the pass-through entity and auditors to have access to the records and financial statements as necessary for the pass-through entity to comply with this part.

§ ____ .405 Management decision.

(a) *General.* The management decision shall clearly state whether or not the audit finding is sustained, the reasons for the decision and the expected auditee action to repay disallowed costs, make financial adjustments or take other action. If the auditee has not completed corrective action, a timetable for follow-up should be given. Prior to issuing the management decision, the federal agency or pass-through entity may request additional information or documentation from the auditee, including a request for auditor assurance related to the documentation, as a way of mitigating disallowed costs. The management decision should describe any appeal process available to the auditee.

(b) *Federal agency.* As provided in § ____ .400(a)(7), the cognizant agency for audit shall be responsible for coordinating a management decision for audit findings that affect the programs of more than one federal agency. As provided in § ____ .400(c)(5), a federal awarding agency is responsible for issuing a management decision for findings that relate to federal awards it makes to recipients. Alternate arrangements may be made on a case-by-case basis by agreement among the federal agencies concerned.

(c) *Pass-through entity.* As provided in § ____ .400(d)(5), the pass-through entity shall be responsible for making the management decision for audit findings that relate to federal awards it makes to subrecipients.

Costs

§ ____ .230 Audit costs.

(a) *Allowable costs.* Unless prohibited by law, the cost of audits made in accordance with the provisions of this part are allowable charges to federal awards. The charges may be considered a direct cost or an allocated indirect cost, as determined in accordance with the provisions of applicable OMB cost principles circulars, the *Federal Acquisition Regulation (FAR)* (48 CFR Parts 30 and 31) or other applicable cost principles or regulations.

(b) *Unallowable costs.* A nonfederal entity shall not charge the following to a federal award:

- (1) The cost of any audit under the Single Audit Act Amendments of 1996 (31 U.S.C. §7501 *et seq.*) not conducted in accordance with this part.
- (2) The cost of auditing a nonfederal entity which has federal awards expended of less than \$300,000 per year and is thereby exempted under § ____ .200(d) from having an audit conducted under this part. However, this does not prohibit a pass-through entity from charging federal awards for the cost of limited scope audits to monitor its subrecipients in accordance with § ____ .400(d)(3), provided the subrecipient does not have a single audit. For purposes of this part, limited scope audits only include agreed-upon procedures engagements conducted in accordance with either the AICPA's generally accepted auditing standards or attestation standards, that are paid for and arranged by a pass-through entity and address only one or more of the following types of compliance requirements: activities allowed or unallowed; allowable costs/cost principles; eligibility; matching, level of effort and earmarking; and reporting.

Reporting

§ ____ .320 Report submission.

* * * * *

(e) *Additional submission by subrecipients.* (1) In addition to the requirements discussed in paragraph (d) of this section, auditees that are also subrecipients shall submit to each pass-through entity one copy of the reporting package described in paragraph (c) of this section for each pass-through entity when the schedule of findings and questioned costs disclosed audit findings relating to federal awards that the pass-through entity provided or the summary schedule of prior audit findings reported the status of any audit findings relating to federal awards that the pass-through entity provided.

(2) Instead of submitting the reporting package to a pass-through entity, when a subrecipient is not required to submit a reporting package to a pass-through entity pursuant to paragraph (e)(1) of this section, the subrecipient shall provide written notification to the pass-through entity that: an audit of the subrecipient was conducted in accordance with this part (including the period covered by the audit and the name, amount, and CFDA number of the federal award(s) provided by the pass-through entity); the schedule of findings and questioned costs disclosed no audit findings relating to the federal award(s) that the pass-through entity provided; and the summary schedule of prior audit findings did not report on the status of any audit findings relating to the federal award(s) that the pass-through entity provided. A subrecipient may submit a copy of the reporting package described in paragraph (c) of this section to a pass-through entity to comply with this notification requirement.

Appendix C: Excerpt from OMB Circular A-133 Compliance Supplement

The OMB *Circular A-133 Compliance Supplement* provides auditor's performing single audits of pass-through entities that spend at least \$300,000 in federal funds each year with guidance for auditing their subrecipient monitoring systems. It identifies the aspects of subrecipient monitoring that auditors should test and the procedures they should use. Pass-through entities that have single audits performed should be aware that the compliance supplement provides audit guidance for other compliance areas in addition to subrecipient monitoring, such as allowable costs or eligibility. Therefore, they may want to review the compliance supplement in its entirety, which is available online at: <http://www.whitehouse.gov/OMB/grants/index.html>.

Subrecipient Monitoring

Compliance Requirements

A pass-through entity is responsible for:

- Identifying to the subrecipient the federal award information (e.g., CFDA title and number, award name, name of federal agency) and applicable compliance requirements.
- Monitoring the subrecipient's activities to provide reasonable assurance that the subrecipient administers federal awards in compliance with federal requirements.
- Ensuring required audits are performed and requiring the subrecipient to take prompt corrective action on any audit findings.
- Evaluating the impact of subrecipient activities on the pass-through entity's ability to comply with applicable federal regulations.

Factors such as the size of awards, percentage of the total program's funds awarded to subrecipients, and the complexity of the compliance requirements may influence the extent of monitoring procedures.

Monitoring activities may take various forms, such as reviewing reports submitted by the subrecipient, performing site visits to the subrecipient to review financial and programmatic records and observe operations, arranging for agreed-upon procedures engagements for certain aspects of subrecipient activities, such as eligibility determinations, reviewing the subrecipient's single audit or program-specific audit results, and evaluating audit findings and the subrecipient's corrective action plan.

The requirements for subrecipient monitoring are contained in the A-102 Common Rule (§__.37 and §__.40(a)), OMB Circular A-110 (§__.50(a)), federal awarding agency program regulations, and the terms and conditions of the award.

Audit Objectives

Determine whether the pass-through entity:

1. Identified federal award information and compliance requirements to the subrecipient, and approved only allowable activities in the award documents.
2. Monitored subrecipient activities to provide reasonable assurance that the subrecipient administers federal awards in compliance with federal requirements.
3. Ensured required audits are performed and requires appropriate corrective action on monitoring and audit findings.
4. Evaluates the impact of subrecipient activities on the pass-through entity.

Suggested Audit Procedures

(Note: The auditor may consider coordinating the tests related to subrecipients performed as part of cash management (tests of cash reports submitted by subrecipients), eligibility (tests that subawards were

Appendix C: Excerpt from OMB Circular A-133 Compliance Supplement

made only to eligible subrecipients), and procurement (tests of suspension and debarment certifications) with the testing of subrecipient monitoring.)

1. Discuss subrecipient monitoring with the pass-through entity's staff to gain an understanding of the scope of monitoring activities, including the number, size and complexity of awards to subrecipients.
2. Test award documents and/or approved agreements to ascertain if the pass-through entity made subrecipients aware of the award information (e.g., CFDA title and number, award name, name of federal agency) and requirements imposed by laws, regulations and the provisions of contract or grant agreements, and to verify that the activities approved in the award documents were allowable. This testing should include procedures to verify that the pass-through entity required subrecipients expending \$300,000 or more in federal awards during the subrecipient's fiscal year to have audits made in accordance with OMB Circular A-133.
3. Review the pass-through entity's documentation of subrecipient monitoring to ascertain if the pass-through entity monitored that subrecipients used federal funds for authorized purposes and takes actions in response to monitoring findings. This review should include procedures to verify that the pass-through entity monitored the activities of subrecipients not subject to OMB Circular A-133, using techniques such as those discussed in the compliance requirements provisions of this section.
4. Verify that the pass-through entity receives audit reports from subrecipients required to have an audit in accordance with OMB Circular A-133, issues timely management decisions on audit and monitoring findings, and requires subrecipients to take timely corrective action on deficiencies identified in audits and subrecipient monitoring.
5. Verify that the effects of subrecipient noncompliance are properly reflected in the pass-through entity's records.

Appendix D: Glossary

These definitions are drawn from several sources including circulars A-110 and A-133, the grants management common rule and the *Webster's New World Dictionary, Second College Edition*.

Administrative requirements — areas common to grants in general, such as financial management, types and frequency of reports, and retention of records. These are distinguished from programmatic requirements, which are unique to each program or grant, such as activities that can be supported by grants under a particular program.

Auditor — an auditor, that is a public accountant or a federal, state or local government audit organization, which meets the general standards specified in *Government Auditing Standards*. The term does not include internal auditors of nonprofit organizations.

Award — financial assistance that provides support to accomplish a public purpose. Awards include grants and other agreements in the form of money, or property in lieu of money, to an eligible recipient. The term does not include: technical assistance, loans, loan guarantees, interest subsidies, insurance and direct payments to individuals. The term excludes contracts entered into and administered under procurement laws and regulations. See "Grant."

Awarding agency — a federal agency (with respect to a grant) or a pass-through entity (with respect to a subgrant). See "Federal awarding agency."

CFDA number — the number assigned to a federal program in the *Catalog of Federal Domestic Assistance* (CFDA).

Contract — a procurement contract under an award or subaward, and a procurement

subcontract under a recipient's or subrecipient's contract.

Corrective action — action taken by the auditee that corrects identified deficiencies, produces recommended improvements or demonstrates that audit findings are either invalid or do not warrant auditee action.

Federal award — federal financial assistance and federal cost-reimbursement contracts that nonfederal entities receive directly from federal awarding agencies or indirectly from pass-through entities. It does not include procurement contracts (under grants or contracts) used to buy goods or services from vendors. Any audits of such vendors shall be covered by the terms and conditions of the contract.

Federal awarding agency — the federal agency that provides an award to the recipient. See "Awarding agency."

Federal financial assistance — assistance that nonfederal entities receive or administer in the form of grants, loans, loan guarantees, property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations and other assistance. The term does not include amounts received as reimbursement for services rendered to individuals under Medicare and Medicaid.

Federal program — a federal agency function, activity, service or project that is created to implement a public policy or initiative and authorized by statute, regulation or other legal authority.

- Grant** — an award of financial assistance (including cooperative agreements) in the form of money, or property in lieu of money, provided to an eligible grantee. The term does not include technical assistance, loans, loan guarantees, interest subsidies, insurance or direct appropriations. Also, the term does not include grants to individuals, such as fellowships or other lump sum awards. See "Award."
- Grantee** — a state or local government, nonprofit organization, college, or university to which a grant is awarded and which is accountable for the use of the funds provided. The grantee is the entire legal entity even if only a particular component of the entity is designated in the grant award document. See "Recipient."
- Indian tribe** — any Indian tribe, band, nation or other organized group or community, including any Alaskan Native village or regional or village corporation (as defined in, or established under, the Alaskan Native Claims Settlement Act), that is recognized by the United States as eligible for the special programs and services provided by the United States to Indians because of their status as Indians.
- Internal control** — a process designed to provide reasonable assurance that the objectives in the following categories are achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations.
- Local government** — any unit of local government within a state, including a county, borough, municipality, city, town, township, parish, local public authority, special district, school district, intrastate district, council of governments and any other instrumentality of local government.
- Management decision** — the evaluation by the federal awarding agency or pass-through entity of the audit findings and corrective action plan and the issuance of a written decision as to what corrective action is necessary.
- Monitor** — to check or regulate the performance of.
- Nonfederal entity** — a state, local government or nonprofit organization.
- Nonprofit organization** — any corporation, trust, association, cooperative, or other organization that is operated primarily for scientific, educational, service, charitable or similar purposes in the public interest; is not organized primarily for profit; and uses its net proceeds to maintain, improve or expand its operations. The term nonprofit organization includes nonprofit institutions of higher education and hospitals.
- OMB** — the U.S. Office of Management and Budget.
- Pass-through entity** — a nonfederal entity that provides a federal award to a subrecipient to carry out a federal program.
- Prime recipient.** See "Pass-through entity."
- Prior approval** — written approval by an authorized official evidencing prior consent.
- Recipient** — a nonfederal entity that expends federal awards received directly from a federal awarding agency to carry out a federal program.
- State** — any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, Guam, American Samoa, the Commonwealth of the Northern Mariana Islands, and the Trust Territory of the Pacific Islands, any instrumentality thereof, any

Appendix D: Glossary

multistate, regional, or interstate entity that has governmental functions, and any Indian tribe.

Subaward — an award of financial assistance in the form of money, or property, made under an award by a recipient to an eligible subrecipient or by a subrecipient to a lower tier subrecipient. The term includes financial assistance when provided by any legal agreement, even if the agreement is called a contract, but does not include procurement of goods and services or any form of assistance that is excluded from the definition of award.

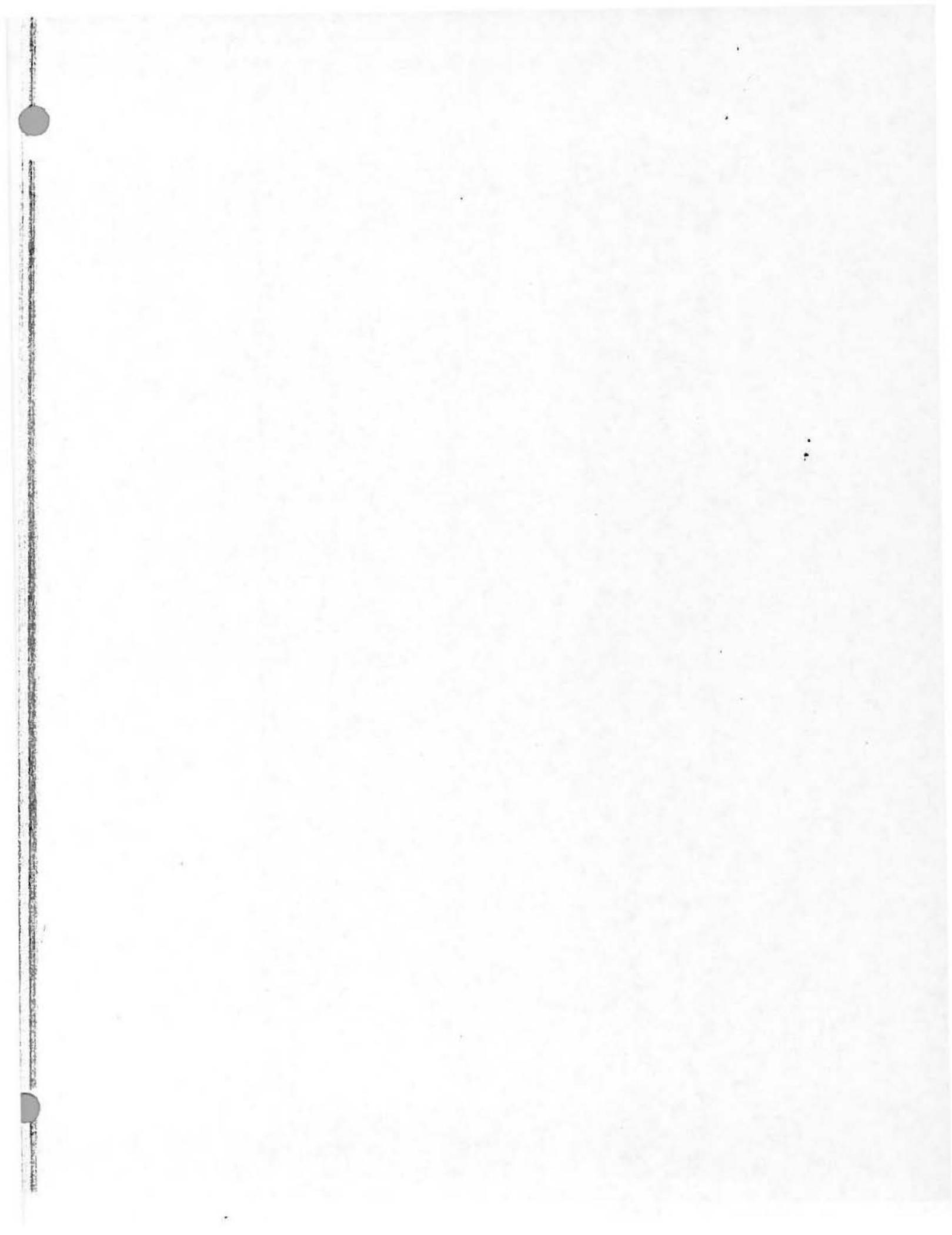
Subgrant. See “Subaward.”

Subgrantee. See “Subrecipient.”

Subrecipient — a nonfederal entity that expends federal awards received from a

pass-through entity to carry out a federal program. It does not include an individual that is a beneficiary of such a program. A subrecipient may also be a recipient of other federal awards directly from a federal awarding agency. Guidance on distinguishing between a subrecipient and a vendor is provided on Page 6.

Vendor — a dealer, distributor, merchant or other provider of goods or services that are needed to administer a federal program. These goods or services may be for an organization’s own use or for the use of beneficiaries of the federal program. Guidance on distinguishing between a subrecipient and a vendor is provided on Page 6.



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Corrective Action Plan of Single Audit for year ended June, 2003.

Its my understanding that part of a single audit and when ever possible the independent auditor should when possible allow for reasonable time to take corrective action with the intention of correcting the findings prior the the final report and once corrected under federal guidelines should not appear in the final report.

Over the past three years the Department of Federal Affairs has not been given reasonable time (at least a couple of weeks to a month) to correct any finding prior to the final report which is due March 31 of each year.

The Director has discussed this important issue with the Mayor, the Finance Director and our internal Auditor and recently with the independent auditor. The following recommendations and changes to the independent auditor (CPA) contract will be studied and recommended to the mayor for approval.

1. The auditor will audit the Department of Federal Affairs first.
2. All findings will be reported to the Director of Federal Affairs within 90 days of the commencement of the contract and no later than 90 days from the due date. (March 31 of each year).
3. Any finding that is corrected and within federal compliance should not appear in the final report.
4. The final draft will be available for review no later than 60 days from the final report.

With these recommendations and changes the independent auditor will greatly enhance the Department of Federal Affairs ability to aggressively comply with OMB- Circular A-133.

It is the Mayors intention to take the necessary steps and changes in enhancing our methods to fully comply and exceed OMB- Circular A-133. The Mayor always strives to be the best in everything the federal government requests. We understand that with these changes we will start steering our auditing methods in a positive direction to excellence.

**Schedule of findings Award finding and Questioned Cost
Year Ending June 30, 2003**

Section III- Finding Reference 03-01 Page 47

Corrective Action Taken:

During the audit for Federal Cash Transaction Report (SF 272) in areas "A+B" this finding was produced in the process of generation the necessary signatures with the purchase component. We have recommended to the Department of Federal Affairs accountant and the finance director to possible color code this component alerting both parties the importance of acquiring the necessary signatures on a timely basis. This finding we understand is rear and we feel should not happen again.

In area "C" of the finding I have instructed our accountant in the Department of Federal Affairs to implement the following suggestion and avoid this finding in the future.

1. Develop a calendar with quarterly date indicating when quarterly reports are due and refer to this calendar on a regular basis.
2. To use and develop a software program which Microsoft Office so that when the computer is turned on it will indicate to the accountant when quarterly reports are due via the computer automatically.

Schedule of findings Award finding and Questioned Cost Corrective Action Response

Finding Reference 03-02 Page 48

Corrective action taken:

Before, during and after the Single Audit the Department of Federal Affairs was conducting periodic visits to all three sub-recipients, the purpose of these visits were to confirm Municipal funding was being spent as stated in each proposal and under federal guidelines.

All three sub-recipients were following requested guidelines and regulations. They all supplied complete documentation photos for all three projects. All three are complying with federal rules governing sub-recipients, checks and balances are confirmed.

The Department of Federal Affairs was in the process of gathering the necessary documentation when the single audit was taking place. The CPA firm conducting the audit only allowed for a few days to take corrective action prior to the final report. As we stated in our cover letter; if the CPA firm conducting the single audit allowed for reasonable time to take corrective action this finding and most if not all of the findings for fiscal year 2002-2003 would not have appeared in the final report and we would have been granted an excellent performance rating which will be the direction we will take for fiscal year audit 2003-2004.

As additional corrective action pertaining to sub recipients in the future the Municipal Government of Cidra will implement the following changes to sub-recipient grants.

1. The municipality will establish bank accounts for each sub-recipient.
2. The municipality will no longer grant donation in the form of a check.
3. The municipality will disburse funds only when the sub-recipient demonstrates that the work projected in the proposal was carried out.
4. Each sub-recipient will turn in as part of their file photos, canceled checks and any documentation that we understand is necessary to justify any disbursement of funds.
5. Each sub-recipient will be required to submit a quaterly progress report.
6. The municipality will conduct a closeout monitoring visit to each sub-recipient.

7. The municipality will use the manual titled "Techniques for Monitoring Federal Sub-award as a guide". Copy attached as attachment 1.

Section III- Finding Reference program 03-03 Page 49.

Special Test- Housing Rehabilitation

The Mayor has hired a new program coordinator, Rehabilitation Inspector and a secretary. The program is now fully staffed with four employees. A new administrative manual has been developed and submitted and approved by our CPD representative Lourdes Moreno. We have implemented all recommendations from HUD during and after the audit. It's our understanding that the office of Housing Rehabilitation has made mayor improvements on the administration of the program. On April, 2004 we received a communication in letter format from Carmen R. Cabrera (see Attachment 2) indicating we can commence to reopen the program with three additional suggestions. These suggestions are being and/or have been incorporated into the programs administration manual. We understand that all findings have been corrected with our desire to comply with all federal requirements pertaining to the program and with the new staff we are now headed in that direction.

**MINUTES OF CITIZEN PARTICIPATION
COMMUNITY BLOCK DEVELOPMENT GRANT
FUNDING FISCAL YEAR 2004**

The municipal government of Cidra held four (4) public hearing for the purpose of receiving community input on how and where these funds should be spent.

The four (4) public hearings were held on separate dates and times with the purpose of offering the general public various options to attend.

Unfortunately no one appeared at the four (4) hearings. An additional hearing was held during the Section 8 public hearing. At this hearing, where over 150 people attended, we took advantage of the hearing and discussed the CDBG funding for fiscal year 2004. Only a few who attended mainly requested infrastructure improvement in the wards (street re-pavement). Others requested illumination and water improvement in their wards.

Attachment II



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
CARIBBEAN OFFICE, CPD DIVISION
EDIFICIO ADMINISTRACION DE TERRENOS
171 Carlos Chardon Avenue - Suite 301
San Juan, Puerto Rico 00918-0903
<http://www.hud.gov>

APR 15 2004

Honorable Angel L. Malavé-Zayas
Mayor
Attention: Mr. George Pereira-Collazo
Municipality of Cidra
PO Box 729
Cidra, PR 00739

Dear Honorable Malavé-Zayas:

SUBJECT: Housing Rehabilitation Activity
Single Audit Period Ending: June 30, 2002
Community Development and Block Grant (CDBG)

This is in response to Mr. George Pereira's letter dated March 19, 2004 regarding subject matter. We also acknowledge receipt of a draft copy of the Housing Rehabilitation Program Operational Manual to be implemented by your Municipality.

Our review of the guidelines was conducted in view that the City wants to implement procedures to ensure compliance with program requirements and to improve its performance. The review of the document submitted is part of the ongoing effort to provide technical assistance to the City and does not constitute an approval of such document. Entitlement cities have full discretion to design and implement their programs and activities based on their local needs and priorities identified in their Consolidated Plans, and as long as they meet program objectives and requirements.

The guidelines that the City finally adapts must be consistent with the method described in the Action Plan. The City needs to describe in its Action Plan how it selects communities when the activity is citywide or describe in general terms the procedures on how families will be selected to participate in the housing rehabilitation program. It is important that citizen clearly understand what procedures have been established to maximize participation under the program and provide fair equitable distribution of funds.

The following are suggestions that we consider may improve the City's guidelines:

1. The guidelines should define as per 24 CFR 570.3 low-income household and moderate-income household in the event that the house is rehabilitated for rental purposes. In addition, the term of years that the rehabilitated house will be available for low-income persons after rehabilitation should be established.

2. According to the guidelines, program participants have thirty days (30) to start construction otherwise; the City will recover from the participants the construction materials. This area is of great concern, since the guidelines do not show what controls will be in place to ensure that construction materials are not sold or are not just laying around because the program participant has not been able to find who will do the work. This area needs to be further addressed in the guidelines. Poor controls in this area may result in the loss of construction materials and in mismanagement of grant funds.
3. The guidelines should describe how the work would be performed. Will the work be contracted out, will it be through force account, or are the participants performing the work? If the participants are performing the work, what skills will be required from the participants to ensure the quality of the work and that it meets specifications. If the work is contracted out, a description of the process, the number of quotations needed from qualified contractors, etc.

Therefore, in view of the Municipality's efforts to substantially improve the single-family housing rehabilitation activity, you are hereby authorized to re-initiate the use of CDBG funds for the activity to benefit low and moderate-income families.

Please be advised that a follow up visit will be scheduled during the year to verify compliance with program requirements. Any funds improperly expended will be disallowed.

If there are any questions, please contact Ms. Lourdes del Carmen Moreno, CPD Representative, at (787) 766-5400, extension 2009.

Sincerely,



Carmen R. Cabrera
Director
Community Planning
and Development

cc: Michael A. Colón, Esq.
Field Office Director