



**NATIONAL ENDOWMENT FOR THE ARTS
OFFICE OF INSPECTOR GENERAL**

**FINANCIAL MANAGEMENT SYSTEM &
COMPLIANCE EVALUATION**

OF THE

MUSIC-THEATRE GROUP

NEW YORK, NEW YORK

**REPORT NO. SCE-08-03
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INTRODUCTION

BACKGROUND

Music-Theatre-Group (MTG) was founded in 1970 to nurture, develop, and produce the works of emerging, mid-career, and established artists in order to take productions to diverse communities. It centers its production activities on the following: 1) to recognize and support artists of considerable gifts at any stage in their development, 2) to support long-term commitments to collaboration, and 3) to produce and promote these artists' music-theatre works. MTG is located in New York City.

OBJECTIVE AND SCOPE

The objective of this financial management system and compliance evaluation by the National Endowment for the Arts (NEA) Office of Inspector General (OIG) is to determine whether the organization's financial management system and recordkeeping complies with the requirements established by the Office of Management and Budget (OMB) and NEA's *General Terms and Conditions for Grants and Cooperative Agreements to Organizations (General Terms)*. The evaluation was conducted in accordance with the President's Council on Integrity and Efficiency Quality Standards for Inspections, as applicable.

PRIOR AUDIT COVERAGE

During the past five years, neither the Government Accountability Office (GAO) nor the NEA Office of Inspector General has issued any audit reports on Federal grants awarded to the MTG. As of our September 14, 2007 site visit, the most recent issued independent auditor's report on MTG was for the years ended June 30, 2006 and June 30, 2005. The auditors, Bloom and Street, LLP, rendered an unqualified (clean) opinion on MTG. MTG was not subject to the audit requirements of OMB Circular A-133.

RESULTS OF EVALUATION

Our evaluation concluded that MTG could not support some of the expenditure amounts reported for selected Grant No. 03-2800-5011, and did not have a Section 504 self-evaluation on file. In addition, MTG [REDACTED] [REDACTED] was not in compliance with the repayment terms of its Cash Reserve Fund.

REPORTED EXPENDITURES

For selected Grant No. 03-2800-5011, MTG did not maintain personnel activity (time and effort) reports for all employees whose salaries and fringe benefits are charged, in whole or in part, to either the award or the matching funds if the award is greater than \$25,000 (or \$50,000 or more for grants awarded beginning with fiscal year 2005). This requirement is mandated by OMB and is detailed in NEA's *General Terms*. A sample personnel activity report is also provided in the *General Terms*.

MTG should develop procedures to ensure that individual time sheets are maintained for employees whose salaries are charged, in whole or in part to grant awards that are \$50,000 or more.

In addition, MTG could not justify how it determined the percentage it used to allocate salaries and overhead costs. As a result of these two deficiencies, we are questioning salary and overhead costs totaling \$64,304. Without the questioned costs, MTG does not meet the matching requirements of the grant. Therefore, a potential refund of \$18,626 could be due the NEA (see Appendix 1).

SECTION 504 SELF-EVALUATION

MTG did not have the required Section 504 self-evaluation on file. As noted in NEA's *General Terms*, "A Section 504 self-evaluation must be on file at your organization." A *Section 504 Self-Evaluation Workbook* is now available online at www.arts.gov/about/504Workbook.html.

Subsequent to our evaluation, MTG provided us with a completed *Section 504 Self-Evaluation Workbook*. Therefore, no additional action is required on this finding.

OTHER ISSUES

[REDACTED]

Cash Reserve Fund. MTG previously was awarded a Challenge Grant in 1986. Part of the award was to establish a permanent Cash Reserve Fund, which was to consist of NEA funds of \$135,000 and matching amounts of \$405,000 (total fund \$540,000). According to the terms of the award, all borrowings from this fund shall be repaid in cash according to a repayment schedule to be developed and adhered to by the grantee. MTG indicated that it has not paid back any borrowings to the Fund since the early 1990's. MTG's Combined Statement of Financial Position as of June 30, 2006, showed a Due from Unrestricted Funds of \$543,391 and Unrestricted Operating Assets of a negative \$627,449.

Because of the current financial condition of the organization, it does not appear that MTG will be able to pay the Fund back anytime in the near future. However, MTG has indicated that during the past year they have taken steps to raise new funds through increased Board giving, involvement in the Patron Giving Program and involvement with the Capacity Giving Program. (Hopefully, these new funds if not used for operating expenses can be used to repay the Cash Reserve Fund [REDACTED].)

We recommend that MTG develop a workable plan that would result in MTG coming into full compliance with the requirements of the grant. Failure to come in compliance could result in funds due to the NEA in the amount of \$135,000.

Based on the above findings, we believe that MTG should be placed on the Working Capital Advance (WCA) Method of Funding. The WCA method works like an imprest fund, allowing a grantee to be advanced funds, which must be disbursed upon receipt (the initial request cannot be for the entire amount of the award). After the funds are received and disbursed, the grantee can request another cash advance to replenish the fund. All requests for payments, exclusive of the initial advance, should be supported by adequate documentation. As such, with each new reimbursement request, information is provided that verifies actual expenses incurred and paid from the previous request. If a grant has a matching requirement, expenses will be reimbursed only if required matching costs have also been incurred, paid and documented. The final reimbursement request must indicate that all of the required matching costs under the grant were incurred and paid. MTG should remain under WCA until it can document that it has a stable financial condition and all other report recommendations are cleared.

Accounting Manual. We found that MTG did not have a formalized accounting manual. Although having a manual is not a NEA or OMB requirement, we believe that individual employee's knowledge would be further enhanced and potential systematic problems could be avoided if MTG formalized many of its own policies and procedures, and guidance available on other grants and accounting matters. This formalized accounting handbook could contain policies and procedures relating to financial management, grants management, internal controls, budgeting, etc. An addendum to the handbook could include publications such as the General Terms and Conditions for Grants, the Financial Management Guide for Non-profit Organizations, the OMB Circulars and other publications on Federal and State requirements.

EXIT CONFERENCE

An exit conference was held with MTG personnel on September 14, 2007. A followup conversation on November 16, 2007, also took place with the MTG's producing director. MTG basically concurred with our findings and recommendations, and agreed to take corrective action.

RECOMMENDATIONS

We recommend that MTG:

1. Develop procedures to ensure that personnel activity (time and effort) reports are prepared for employees whose salaries are charged, in whole or in part to grant awards that are \$50,000 or more. (This amount has been increased to \$50,000 or more for grants awarded beginning with fiscal year 2005).
2. Develop procedures to justify the charging of overhead costs. Alternatively, an indirect cost rate may need to be negotiated.
3. Provide information to support the questioned salary and overhead costs of \$64,304 claimed under Grant No. 03-2800-5011. If the documentation submitted is not deemed satisfactory, a refund of up to \$18,626 may be required.
4. [REDACTED]
5. Develop a workable plan that would result in MTG coming in full compliance with the Challenge Grant requirements for a Cash Reserve Fund.

We recommend that NEA:

1. Make MTG ineligible for any future awards and not make any payments to MTG until an agreement is reached [REDACTED] and evidence of such payments being made is provided to NEA.
2. Place MTG on the Working Capital Advance Method of Funding for all current and future grants. All reimbursement requests should be supported by adequate documentation such as cancelled checks, invoices, personnel activity reports or other records; documentation supporting program accomplishments should also be provided.

Calculation of Potential Refund
On Grant No. 03-2800-5011

Total Costs Claimed	\$107,052
Less: Questioned Salary & Fringe	(64,304)
Total Allowable Costs	42,748
Less: NEA Share of Allowable Costs	(21,374)
Matching Amount	<u>21,374</u>
Amount Disbursed	40,000
Less: NEA Share of Allowable Costs	(21,374)
Potential Refund	\$ <u>18,626</u>