

National Endowment for the Arts
Office of Inspector General

Improper Payments Risk Assessment
FINAL REPORT
July 30, 2020



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Objective

To conduct an improper payments risk assessment for the National Endowment for the Arts (Arts Endowment) in compliance with the Improper Payments Elimination and Recovery Act (IPERA).

Engagement Scope

The scope for the Improper Payments Risk Assessment is to identify potential areas of risk based on an assessment of fiscal year (FY) 2019 payments.

Methodology

RMA Associates, LLC (RMA) requested from Arts Endowment the population of disbursement activity for non-intragovernmental transactions for FY 2019. RMA identified the grants program, to include direct grantmaking and partnerships, as the process where disbursements accounted for approximately 75 percent of Arts Endowment's annual no-year appropriations.¹

RMA subsequently performed a risk assessment to determine if Arts Endowment's grants program is susceptible to improper payments. IPERA defines *significant* as improper payments that exceed \$10 million and 2.5 percent of the program's total expenditures or \$100 million regardless of the proportion to the program's total expenditures.

In performing our assessment, RMA only assessed inherent risk. The potential areas of risk identified in this report are based solely on the population data assessed and does not include an examination of the controls in place to address such risks. The recommendations associated with each potential risk area are not indicative of a current lack of controls but reflect minimum controls which should be in place given the potential areas of risk.

Risk Assessment

RMA used Benford's Law Analysis in identifying potential areas of risk in Arts Endowment's grants program. Benford's Law Analysis helps to identify irregularities in the distribution of numerical data, in this case the total amount of non-intragovernmental transactions. This analysis is based on a premise that it is more likely a number will begin with a smaller digit than a larger digit helping to detect:

1. Excessive number of payments at specific dollar amounts (price fixing or duplicate purchases);
2. Employees making too many payments near-limit to circumvent rules (split purchases);
and

¹ Arts Endowment receives \$150-\$160 million in annual no-year fund appropriations. Of this, approximately \$120 million is obligated for grant programs.

- Dollar amounts that have been delivered and manipulated for contract avoidance (contract amount versus paid amount).

This analysis identifies non-conformity between Benford’s Law and the distribution of amounts in the population in a graphical or tabular form.

Based on the population data, the graph (Figure 1) shows irregularities in the payment amount because of the higher distribution of smaller digits, meaning large number of payments for the same amount, perhaps duplicate payments, price fixing, or near-payment authority limit.

Figure 1: Benford’s Law Analysis of Arts Endowment’s Non-Intragovernmental Transactions



Potential Areas of Risk

RMA used its proprietary Data Extraction and Analysis Procedures system (DEAPs) to extract the data and stratify the population into homogenous groups. Based on the data received, we identified several potential areas of risk.

- Manual Invoice Entries:** \$7,347,375 (9 percent) of the population of transactions are sourced from manual invoice entries:

Source	Count	Amount
WEBADI [Web Applications Desktop Integrator]	2,910	\$75,018,263
Manual Invoice Entry	281	\$7,347,375
Total	3,191	\$82,365,638

Manual invoice entries in the system may result in unauthorized entry, change, or override of invoice amounts and transactions.

According to the Payment Integrity Improvement Analysis FY 2019² report developed by the Arts Endowment Finance Office; Arts Endowment identified approximately \$180,000 in improper payment, which was the result of a keypunch error where a manual payment submission was used. Arts Endowment identified this incident to be isolated, as grants awarded in FY 2017 and prior required paper submission of requests for reimbursement. Arts Endowment’s corrective action plan involves a second reviewer to verify the dollar amounts manually entered in the system for reimbursement requests over \$100,000 for FY 2017 and prior grants.

2. **Payments Held:** \$4,384,925 (5 percent; highlighted in green in table below) of the population of transactions were held for the following reasons:
 - a. Payment file rejected at Treasury;
 - b. Invalid banking information; or
 - c. No System for Award Management (SAM) information.

Non-intragovernmental transactions with a hold that were paid (no “reverse” indicator found in the data for the payment), may result in payments to vendors or awardees not properly vetted or authorized to receive payments.

Hold Reason ³	Count	Amount
GRANTS	2,718	\$71,307,173
PMT FILE REJECTED AT TREASURY	141	\$3,670,979
ESC REJECTION APPROVAL	85	\$2,525,398
CANCELLED CHECK FROM TREASURY (over multiple dates)	93	\$2,451,980
GRANT	90	\$1,540,173
TOTAL OF INVOICE LINES DOES NOT EQUAL INVOICE AMOUNT	13	\$494,952
GRATNS [GRANTS]	17	\$154,726
SUPPLIER BANK ACCOUNT INVALID	7	\$42,818
SAM'S NEEDS UPDATED	1	\$40,000
NEED UPDATED BANKING	1	\$36,176

² National Endowment for the Arts, *Payment Integrity Improvement Analysis FY 2019*, pp. 13-15

³ ‘Hold Reason’ acronyms are reflective of the source population.

Hold Reason ³	Count	Amount
AGENCY BETC REQUIRED OR TP TAS/BETC REQUIRED FOR FEDERAL SUPPLIER	2	\$29,800
NO BANKING	1	\$25,000
FUNDING OR ADDITIONAL INFORMATION NEEDED	7	\$18,476
SAMS NEEDS UPDATED	1	\$15,000
SAMS UPDATE ROUTING	1	\$15,000
KINTANA SENT 121718	1	\$10,000
NEED BANKING INFORMATION RETURNED FROM TREASURY AS BAD BANKING	1	\$10,000
NEED SAMS CORRECTED	1	\$10,000
RETURNED FROM TREASURY	1	\$10,000
SAMS NEEDS TO BE UPDATED	1	\$10,000
WAITING FOR SUPPLIER TO FIX	1	\$10,000
UPDATE BANKING	1	\$8,250
SAMS UPDATE	1	\$5,000
BANKING NOT UPDATING ON SCHEDULED PAYMENT TAB	1	\$2,952
OTHER	4	\$(78,215)
Total	3,191	\$82,365,638

According to the Payment Integrity Improvement Analysis FY 2019⁴ report developed by the Arts Endowment Finance Office, Arts Endowment identified a \$620,594 improper payment, which was an Enterprise Services Center (ESC) system error that resulted in an incorrect supplier number assigned. As a result, ESC, Arts Endowment's financial system shared service provider, modified its internal process to verify banking information on all first grant payments per the Program Office. ESC, as part of the corrective action plan, requests an update to the supplier number when banking information is incorrect.

- Created by One User:** \$74,486,461 (90 percent) of the population of transactions were created by one user:

Created User	Count	Amount
CGUAJARDNEA	2,894	\$74,486,461
GOBOTNEA	239	\$6,326,782
KKING4NEA	41	\$1,003,998
NYOUNGNEA	7	\$401,573
TCOUGHRA NEA	5	\$75,000
MYOUNG3NEA	4	\$71,410

⁴ National Endowment for the Arts, *Payment Integrity Improvement Analysis FY 2019*, pp. 13-15

Created User	Count	Amount
SKEBEDENEA	1	\$413
Total	3,191	\$82,365,638

Of the \$74,486,461, \$4,570,105 (six percent) of this one user’s transactions were flagged in the Benford’s Law Analysis based on the first two digits of these transactions.

One user creating, reconciling, and approving transactions in the system may result in a lack of proper segregation of duties to prevent fraud and error.

4. **Flagged Vendors:** Eighteen vendors \$5,386,480 (seven percent) were flagged as “suspicious” payments based on Benford’s Law Analysis distribution of dollar amounts.

Vendor Name	No. of "Suspicious" Records (Based on First Two Digits)	Amount
JOHN F KENNEDY CENTER FOR THE PERFORMING ARTS	2	\$758,634
MASSACHUSETTS COMMONWEALTH OF ARTS MIDWEST	3	\$663,100
LOUISIANA STATE ARTS COUNCIL	2	\$400,000
SOUTH ARTS, INC	1	\$307,963
NATIONAL ASSEMBLY OF STATE ARTS AGENCIES	1	\$304,956
NEW HAMPSHIRE STATE OF	1	\$303,933
OHIO STATE OF2	1	\$259,059
CONFERENCE OF MAYORS RESEARCH AND EDUCATION FOUNDATION	1	\$255,300
WASHINGTON STATE ARTS COMMISSION	1	\$254,261
MARYLAND STATE OF	1	\$250,035
ARIZONA STATE OF	1	\$209,475
WEST VIRGINIA DIVISION OF CULTURE AND HISTORY/ARTS SECTION	1	\$205,412
NEW JERSEY STATE OF	1	\$204,676
MID ATLANTIC ARTS FOUNDATION	1	\$204,400
NEVADA STATE OF	1	\$203,568
ALASKA STATE OF	1	\$201,619
MONTANA ARTS COUNCIL	1	\$200,089
	1	\$200,000
Total	22	\$5,386,480

The Benford's Law Analysis technique flagged these payments as suspicious because they show a pattern based on the dollar amounts paid. These flagged payments may result in invalid transactions if there is no supporting evidence of the amount paid.

Conclusion

Based on the assessment of inherent risk of Arts Endowment's FY 2019 population of transactions for its grants program, we identified four potential areas of risk:

1. **Manual Invoices Entries:** \$7,347,375 (9 percent) of the population of transactions are sourced from manual invoice entries.

Recommendation: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure manual transactions are reviewed and approved by appropriately assigned personnel, considering proper segregation of duties.

2. **Payments Held:** \$4,374,925 (5 percent) of the population of transactions were held for the following reasons:
 - a. Payment file rejected at Treasury;
 - b. Invalid banking information; or
 - c. No SAM information.

Recommendation: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure vendors or awardees have verified banking information and are properly vetted and authorized to receive payments to minimize payments that are held.

3. **Created by One User:** \$74,486,461 (about 90 percent) of the population of transactions were created by one user. Of the \$74,486,461, \$4,570,105 (6 percent) of this one user's created transactions were flagged in the Benford's Law Analysis based on the first two digits of these transactions.

Recommendation: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure proper segregation of duties is implemented in creating, reconciling, and approving transactions in the system.

4. **Flagged Vendors:** Eighteen vendors (\$5,386,480 or 7 percent) were flagged as "suspicious" payments based on Benford's Law Analysis distribution of dollar amounts.

Recommendation: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure all payments are valid and supporting documentation is maintained as evidence of amount paid. We also recommend the agency review payments flagged as "suspicious" to confirm they are proper.

To: Office of Inspector General

From: Ann Eilers, Deputy Chairman for Management and Budget

ANN EILERS Digitally signed by ANN EILERS
Date: 20200728 09:17:19 -0400

Subject: Management's Response to Improper Payments Risk Assessment

Date: July 28, 2020

Thank you for your report dated July 22, 2020, titled "Improper Payments Risk Assessment." In this report, your office provided a risk assessment on NEA's payment data, using Benford's Law Analysis. The assessment identified possible areas of risk based on the data extracted and related recommendations.

As your report notes, there is an inherent risk with any organization's operation. This inherent risk is mitigated to residual risk based on internal controls that are in place. The Arts Endowment management annually completes a risk assessment where we assess inherent risk, related internal controls, and resulting residual risk. Additionally, we annually complete an improper payments assessment. This report referenced improper payments that our office identified, analyzed, and reported in our annual assessment. Our assessment process includes a review and implementation of controls when improper payments are identified. As you note in your report, your assessment did not evaluate internal controls that are in place.

We offer the below responses to your report recommendations:

Recommendation #1: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure manual transactions are reviewed and approved by appropriately assigned personnel, considering proper segregation of duties.

Response #1: Concur. The Arts Endowment has controls in place to ensure manual transactions are reviewed and approved by appropriately assigned personnel, considering proper segregation of duties. As a result of the one improper payment that we identified during our FY19 improper payments assessment, and was detailed in your report, we implemented additional controls over manual transactions.

Action: We will continue to review internal controls for adequacy to include implementing additional controls to address any improper payments identified, as was done with the exception referenced in the report.

Recommendation #2: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure vendors or awardees have verified banking information and are properly vetted and authorized to receive payments to minimize payments that are held.

Response #2: Concur. The Arts Endowment has controls to ensure vendors or awardees have verified banking information and are properly vetted and authorized to receive payments to minimize held payments. As part of our process we work closely with grantees to ensure that they are aware of the requirement for them to update their banking information in SAM to ensure payments are not held and are properly processed.

Action: We will continue to review internal controls for adequacy to include addressing any improper payments identified, as was done with the exception you referenced in your report.

Recommendation #3: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure proper segregation of duties is implemented in creating, reconciling, and approving transactions in the system.

Response #3 Concur. The Arts Endowment has controls in place and continues to fine tune these controls to ensure proper segregation of duties related to creating, reconciling, and approving transactions in the financial system. The exception you noted was from our FY2019 improper payments assessment, and as part of our process we implemented additional controls. In regard to these grant payments, an initial review is completed by Grants Management staff, with a final review completed by staff authorized to approve payments. The approval indicates the payment can be made to the grantee, pending further reconciliation by our financial services provider (ESC), who works with the U.S. Treasury. The "Created by One User" noted in this section is the group of people who work on our behalf at ESC. There are additional controls in place at ESC to ensure data are being entered correctly for the U.S Treasury system.

Action: We will continue to review internal controls for adequacy to include addressing any improper payments identified, as was done with the exception you referred to in your report.

Recommendation #4: Controls must be designed (policies and procedures are documented) and implemented (operating effectively) to ensure all payments are valid and supporting documentation is maintained as evidence of amount paid. We also

recommend the agency review payments flagged as “suspicious” to confirm they are proper.

Response #4: Concur. The Arts Endowment has controls in place to ensure all payments are valid and that supporting documentation is maintained as evidence of amount paid. The payments listed in the report are to State Arts Agencies and Regional Arts Organizations. These agencies follow their own organizational policies and processes, and they use a government-wide form to request drawdowns. The NEA Grants Management office staff review schedules and progress reports to monitor agency drawdowns, unusual items are followed up on and, if needed, supporting documentation is obtained. We reviewed each of the amounts listed and verified the amount was a valid request.

Action: We will continue to review internal controls for adequacy as part of our annual risk assessment and improper payments review process, and document updates to policies and procedures as deemed necessary based on this review.

We continue to monitor the agency’s payment processes to ensure that improper payments remain at an acceptable level. We will continue to adjust operations and controls (policies and procedures) as is needed to ensure that we have a cost-effective approach to preventing and detecting improper payments, thus further reducing their risk of occurrence. We would like to thank the Office of Inspector General and RMA Associates, LLC staff for their courtesy and professionalism during the completion of their risk assessment.