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NATIONAL ENDOWMENT FOR THE ARTS OFFICE OF INSPECTOR GENERAL

Performance Audit on Selected Awards to

North Carolina Arts Council
Raleigh, North Carolina

Report No. OIG-20-04

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SUMMARY

Based on our performance audit, we concluded that the North Carolina Arts Council (NCAC) generally complied with financial management system and recordkeeping requirements established by the Office of Management and Budget (OMB) and the National Endowment for the Arts (Arts Endowment). However, we identified some areas requiring improvement.

NCAC:

1. Reported unallowable subaward costs on its Federal Financial Report (FFR).
2. Did not maintain current policies and procedures for subawards.
3. Did not have debarment and suspension policies and procedures.
4. Did not have policies and procedures for the management of Federal awards.

INTRODUCTION

AUDITEE BACKGROUND

NCAC is a state government agency of the North Carolina Department of Natural and Cultural Resources, founded in 1967. NCAC is dedicated to delivering resources to arts organizations and artists to support projects and programs of public value. Through its grants program, NCAC invests in arts activities that benefit communities in North Carolina. Specifically, in 2019, NCAC granted \$7.5 million to non-profit arts organizations, schools, local governments, and individual artists.

OBJECTIVES, SCOPE AND METHODOLOGY

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

The objectives of this audit were to determine whether:

- NCAC complied with the award management requirements established by OMB and the Arts Endowment's *General Terms and Conditions for Partnership Agreements (General Terms)*;
- NCAC fulfilled the financial and performance requirements set forth in the award documents, including any required cost share/matching; and
- Reported award costs were reasonable, allocable, and allowable.

We limited the scope of our audit to awards issued or closed during the period of October 1, 2016 through September 30, 2019. Review of NCAC's internal controls was limited to those relevant to the audit objectives. As a result, we are not stating an opinion on the effectiveness and efficiency of NCAC's overall internal control system.

NCAC had five active Arts Endowment awards within the audit scope period. For this audit, we reviewed three Partnership awards that were closed within the audit scope period (see table below). All three Partnership awards were issued to support partnership agreement activities consisting of: General Partnership (including Poetry Out Loud), Arts Education, Folk Arts Partnership, and Underserved Communities. NCAC received extensions for Arts Endowment award Nos. 15-6100-2035 and 16-6100-2031 to close out subawards. NCAC also received an extension for Arts Endowment award No. 17-6100-2056 to hire a Folklife Specialist and close out subawards. The awards had a one-to-one cost share/match, with the exception of Arts Endowment award No. 16-6100-2031. That award included \$6,000 in non-matching funds for the Creativity Connects Roundtables program.

Arts Endowment Award No.	Award Period	Award Amount	Total Reported Costs
15-6100-2035	07/01/15 – 12/31/16	\$ 899,100	\$2,697,300
16-6100-2031	07/01/16 – 12/31/17	957,300	2,871,900
17-6100-2056	07/01/17 – 12/31/18	946,500	1,893,000
TOTAL		\$2,802,900	\$7,462,200

We identified three significant internal control components that were relevant to our audit objectives; control environment, control activities, and monitoring. Control environment principles require NCAC to establish an organizational structure, assign responsibility, and delegate authority to achieve the entity’s objectives. Control activity principles require NCAC to design and implement control activities that achieve mission objectives and respond to risks. Monitoring principles require NCAC to establish and operate activities to monitor and evaluate the internal control system, addressing deficiencies on a timely basis. We conducted audit work to identify significant controls within NCAC’s internal control system, then tested their operation and reliability. These tests included audit work to verify the reliability of computer-processed data provided by NCAC. We determined the data obtained and used for the purposes of this audit was reliable.

Additionally, we conducted reviews of NCAC’s financial procedures and performance outcomes to determine compliance with award requirements. This audit work included reviews of procedures and support documents, and interviews with NCAC staff.

Finally, we conducted tests of subawards and transactions to determine the allowability of reported costs. More specifically, we conducted risk assessments to determine the methods for selecting subawards and cost transactions for testing, and levels of testing necessary to support findings and conclusions. Based on the risk assessment results, we judgmentally selected 10 subawards from each award for compliance testing with subaward requirements. We also judgmentally selected 25 cost items from each award for transaction testing, to include subaward costs and procurement costs.

PRIOR AUDIT COVERAGE

The Arts Endowment Office of Inspector General (OIG) had not issued any audit reports on Federal awards to NCAC in the past five years. However, NCAC is included in the North Carolina Single Audit report. As of the planning phase of this audit, the most recent audit report was issued by the North Carolina Office of State Auditor for the fiscal year ended June 30, 2018. In its opinion, the Schedule of Expenditure of Federal Awards was fairly stated, in all material respects, in relation to the basic financial statements as a whole. NCAC was subject to the audit requirements of OMB Circular A-133 and 2 CFR 200, Subpart F (Audit Requirements).

AUDIT RESULTS

SUBAWARD COSTS

NCAC reported three unallowable subaward costs on its FFR for Arts Endowment award No. 17-6100-2056, totaling \$30,000. Specifically, NCAC awarded three individuals Artist Fellowship subawards in which the payments were made in full during the Arts Endowment award period. However, the subaward periods ended on June 30, 2019, which is three months after the Arts Endowment award was closed. The final reports of those subawards were not submitted until July 29, 2019 and September 4, 2019. As a result, the subawards were not closed until several months after the Arts Endowment award.

Awards issued by the Arts Endowment are subject to the following requirements:

Arts Endowment General Terms. Requirements for Subawards made under a Partnership Agreement 23.13. Closeout: All subawards made with Federal or matching funds must be closed out (including submission and approval of all subrecipient final reports and disbursement of all Federal and matching funds) prior to closing out your Federal award. If you extend a subaward to allow a subrecipient more time to complete the activities for which the subaward was made, the period of performance for the prime award must also be extended accordingly. However, subawards that encounter significant delays should (unless required to meet the cost share/match) be removed from the scope of the NEA award to avoid continued delays in closing out the Federal award.

NCAC's subaward periods for Artist Fellowships extended beyond the closeout period of the Arts Endowment award. NCAC officials were unable to determine a specific reason why the issue occurred; however, they believe that the discrepancy could be due to the subaward periods' alignment with NCAC's fiscal year. Reporting subaward costs that are not closed prior to closing out Federal awards could result in a refund due to the Arts Endowment. Thus, we are questioning subaward costs totaling \$30,000. To determine if a refund was due, we reduced the award's total costs by its respective unallowable amounts (see Appendix A). We determined that without these costs, NCAC does not meet the one-to-one cost share/match requirement resulting in a potential refund due to the Arts Endowment in the amount of \$14,976.

We recommend NCAC adjust its subaward period for Artist Fellowship and other programs as necessary to ensure the closeout process is completed prior to the closing of the Arts Endowment award.

We also recommend that the Arts Endowment determine if unallowable subaward costs in the amount of \$30,000 for Arts Endowment award No. 17-6100-2056 should be disallowed and if a refund is due.

NCAC concurs with this finding and recommendation. (*See Appendix B*)

SUBAWARD POLICIES AND PROCEDURES

NCAC did not have updated subaward policies and procedures. Based on our review of NCAC's subaward policy, we identified annotations in multiple areas to indicate changes in the subawards process. These updates were not finalized prior to the initiation of the audit.

Awards issued by the Arts Endowment are subject to the following requirements:

- **2 CFR 200.302(b)(4). *Financial Management:*** Effective control over, and accountability for, all funds, property, and other assets. The non-Federal entity must adequately safeguard all assets and assure that they are used solely for authorized purposes. See § 200.303 Internal controls.
- **2 CFR 200.303. *Internal Controls:*** The non-Federal entity must:
 - (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework”, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).
 - (b) Comply with Federal statutes, regulations, and the terms and conditions of the Federal awards.
 - (c) Evaluate and monitor the non-Federal entity's compliance with statutes, regulations and the terms and conditions of Federal awards.
 - (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings.
 - (e) Take reasonable measures to safeguard protected personally identifiable information and other information the Federal awarding agency or pass-through entity designates as sensitive or the non-Federal entity considers sensitive consistent with applicable Federal, state, local, and tribal laws regarding privacy and obligations of confidentiality.

NCAC was not aware that the policies and procedures were outdated. Without current subaward policies and procedures, NCAC could rely on improper procedures for processing and distributing subawards. Thus, we recommend that NCAC update its policies and procedures for managing subawards.

NCAC concurs with this finding and recommendation. (See Appendix B)

DEBARMENT AND SUSPENSION

NCAC does not have written policies and procedures in place to ensure that recipients are not debarred or suspended prior to the award of Federal funds. According to NCAC officials, Federal funds recipients are required to self-certify in the contracts; however, we reviewed the contracts and determined that debarment and suspension language was not included.

Awards issued by the Arts Endowment are subject to the following requirements:

- **Subpart C of 2 CFR Part 180.300. OMB Guidelines to Agencies on Government-wide Debarment and Suspension (Non-procurement) states, in part:** Awardees must verify that the person with whom you intend to do business is not excluded or disqualified. You do this by:
 - (a) Checking SAM.gov; or
 - (b) Collecting a certification from that person if allowed by the Federal agency responsible for the transaction; or
 - (c) Adding a clause or condition to the covered transaction with that person.
- **Arts Endowment General Terms. Debarment and Suspension:** You must comply with requirements regarding debarment and suspension in Subpart C of 2 CFR part 180, as adopted by Arts Endowment in Title 2 CFR, Chapter 32, Part 3254.

NCAC was not aware that its contracts did not include suspension and debarment language. Without written debarment and suspension policies and procedures in place, NCAC could have instances of debarred or suspended individuals or organizations receiving Federal funds.

We recommend that NCAC establish written policies and implement procedures to ensure that contractors and recipients are not debarred or suspended from receiving Federal assistance prior to the payment or award of Federal funds.

NCAC concurs with this finding and recommendation. (See Appendix B)

MANAGEMENT OF FEDERAL AWARDS

NCAC does not have policies and procedures for the management of Federal awards. NCAC adheres to the North Carolina Office of the State Controller (OSC) policies and procedures. According to NCOSC Policy 900.7, state agencies are required to maintain current documentation of business processes and procedures and other elements of internal controls. However, we determined that NCAC did not maintain internal policies and procedures for grants management.

Awards issued by the Arts Endowment are subject to the following requirements:

- **2 CFR 200.302 (a). Financial Management:** Each state must expend and account for the Federal award in accordance with state laws and procedures for expending and

accounting for the state's own funds. In addition, the state's and the other non-Federal entity's financial management systems, including records documenting compliance with Federal statutes, regulations, and the terms and conditions of the Federal award, must be sufficient to permit the preparation of reports required by general and program-specific terms and conditions; and the tracing of funds to a level of expenditures adequate to establish that such funds have been used according to the Federal statutes, regulations, and the terms and conditions of the Federal award.

- **2 CFR 200.302 (b). *Financial Management*** states, in part: The financial management system of each non-Federal entity must provide for the following:
 - (1) Identification, in its accounts, of all Federal awards received and expended and the Federal programs under which they were received. Federal program and Federal award identification must include, as applicable, the Catalog of Federal Domestic Assistance title and number, Federal award identification number and year, name of the Federal agency, and name of the pass-through entity, if any.
 - (2) Accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the reporting requirements set forth in §§ 200.327 Financial reporting and 200.328 Monitoring and reporting program performance. If a Federal awarding agency requires reporting on an accrual basis from a recipient that maintains its records on other than an accrual basis, the recipient must not be required to establish an accrual accounting system. This recipient may develop accrual data for its reports on the basis of an analysis of the documentation on hand. Similarly, a pass-through entity must not require a sub-recipient to establish an accrual accounting system and must allow the sub-recipient to develop accrual data for its reports on the basis of an analysis of the documentation on hand.
 - (3) Records that identify adequately the source and application of funds for federally-funded activities. These records must contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, expenditures, income and interest and be supported by source documentation.
 - (4) Effective control over, and accountability for, all funds, property, and other assets. The non-Federal entity must adequately safeguard all assets and assure that they are used solely for authorized purposes. See § 200.303 Internal controls.
 - (5) Comparison of expenditures with budget amounts for each Federal award.
 - (6) Written procedures to implement the requirements of § 200.305 Payment.
 - (7) Written procedures for determining the allowability of costs in accordance with Subpart E – Cost Principles of this part and the terms and conditions of the Federal award.

According to NCAC, they have internal procedures; however, they are not documented. Without written policies in place, NCAC could fail to implement Federal award requirements. Thus, we recommend that NCAC develop written policies and implement procedures for the management of Federal awards.

NCAC concurs with this finding and recommendation. (*See Appendix B*)

RECOMMENDATIONS

We recommend that NCAC:

1. Adjust its subaward period for Artist Fellowship and other programs as necessary to ensure the closeout process is completed prior to the closing of the Arts Endowment award.
2. Update its policies and procedures for managing subawards.
3. Establish written policies and implement procedures to ensure that contractors and recipients are not debarred or suspended from receiving Federal assistance prior to the payment or award of Federal funds.
4. Develop written policies and implement procedures for the management of Federal awards.

We recommend that the Arts Endowment:

1. Determine if unallowable subaward costs in the amount of \$30,000 for Arts Endowment award No. 17-6100-2056 should be disallowed and if a refund is due.

APPENDIX A

North Carolina Arts Council Breakdown of Award Calculations

Award No. 17-6100-2056

Total Reported Costs	\$ 1,893,049
Less Unallowable Subaward Costs	<u>(30,000)</u>
Adjusted Allowable Reported Costs	\$ 1,863,049
Adjusted Allowable Reported Costs	\$ 1,863,049
Less NEA Share of the Costs*	<u>(931,524)</u>
NCAC Cost Share/Match	\$ 931,525
NEA Share of the Cost	\$ 931,524
Less Arts Endowment Disbursement	<u>(946,500)</u>
NCAC Potential Refund	\$ <u>(14,976)</u>

**NEA share is half of the Adjusted Allowable Reported Costs.*



North Carolina Arts Council
Fifty years of leadership

APPENDIX B

Wayne Martin
Executive Director

Susi H. Hamilton
Secretary

Roy Cooper
Governor, State of
North Carolina

June 11, 2020

Ron Stith
Inspector General
National Endowment for the Arts
400 7th Street, SW
Washington, DC 20506

Dear Mr. Stith:

I have reviewed the Performance Audit on Selected Awards to North Carolina Arts Council (No. OIG-20-04) and discussed this report with NCAC staff and with auditor Rashaad Lee. I concur with the findings and recommendations contained in the report.

Our agency values the partnership with the National Endowment for the Arts and looks forward to implementing best practices regarding stewardship of NEA funds.

Sincerely,

Wayne Martin

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