



July 2014

FEDERAL GRANTS

Agencies Performed
Internal Control
Assessments
Consistent with
Guidance and Are
Addressing Internal
Control Deficiencies

GAO Highlights

Highlights of [GAO-14-539](#), a report to congressional requesters

Why GAO Did This Study

In fiscal year 2013, the federal government obligated over \$555 billion for grants. Effective oversight of internal controls is important for providing reasonable assurance that grants are awarded properly, recipients are eligible, and federal grant funds are used as intended.

GAO was asked to review internal control issues over grants. This report (1) examines whether the five largest grant-making agencies' internal control oversight processes for their grant programs were consistent with OMB requirements and (2) describes internal control issues that have been reported related to the grants management process and key grant programs.

To achieve these objectives, GAO reviewed the fiscal year 2012 internal control assessment processes for the five largest grant-making agencies' grants programs, as conducted under OMB Circular No. A-123. GAO reviewed the agencies' assessment documentation and reviewed grants internal control findings reported in other reviews of these agencies for fiscal years 2012 and 2013. GAO did not include Medicaid—the largest federal grant program—which has been well covered in other GAO and HHS OIG reviews.

GAO is not making any recommendations but continues to monitor grants management as part of its work on key issues.

In general, the five agencies concurred with the information in the report. Some agencies also provided technical comments that were incorporated, as appropriate.

View [GAO-14-539](#). For more information, contact Beryl H. Davis at (202) 512-2623 or davisbh@gao.gov.

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FEDERAL GRANTS

Agencies Performed Internal Control Assessments Consistent with Guidance and Are Addressing Internal Control Deficiencies

What GAO Found

For fiscal year 2012, the processes used by the five largest grant-making agencies to conduct their internal control assessments were consistent with the requirements of Office of Management and Budget (OMB) Circular No. A-123, which requires that agencies identify significant areas within their operations in which to implement key controls, continuously monitor and test those controls, and report annually on management's judgment regarding the adequacy and effectiveness of internal control. The five largest grant-making agencies by amount of grant obligations are the Departments of Health and Human Services (HHS), Education, Transportation (DOT), Agriculture (USDA), and Housing and Urban Development (HUD). The agencies identified areas of risk, including grants programs and grants management processes, in which to implement key controls and then monitored and tested those controls. The agencies identified deficiencies through control tests, prepared and implemented corrective action plans to address the deficiencies identified, and reported on their internal control through annual management assurance statements. HHS, DOT, and USDA qualified their internal control management assurance statements for fiscal year 2012, in part because of material weaknesses affecting their grant programs. For fiscal year 2013, HHS, USDA, and HUD gave qualified statements of assurance in part because of material weaknesses in their grant programs.

In addition to issues identified through the OMB Circular No. A-123 process, other audits and reviews have reported internal control issues related to the grants management process and grant programs. For example:

- For fiscal years 2012 and 2013, DOT's financial statement auditors reported that DOT did not timely identify and deobligate unused grant obligations. DOT took actions to address the recommendations, resulting in the auditors reducing the issue from a material weakness in fiscal year 2012 to a significant deficiency in fiscal year 2013.
- In July 2013, HUD's Office of Inspector General (OIG) reported that guidance for ensuring whether grantees are carrying out grant activities in a timely manner in compliance with requirements of the Community Development Block Grant program was not always implemented effectively. HUD generally concurred with the recommendations and stated its intent to address them.
- In both fiscal years 2012 and 2013, HHS reported over \$1 billion in estimated improper payments in grant programs. HHS's OIG determined that HHS did not comply with all requirements of the Improper Payments Elimination and Recovery Act of 2010 for certain grant programs. HHS reported that it has steps planned and under way to help prevent and reduce improper payments.

OMB Circular No. A-123 notes that agency managers and staff should be encouraged to identify control deficiencies, as this reflects positively on the agency's commitment to recognizing and addressing management problems. Financial statement auditors, OIGs, and GAO continue to focus on grants internal controls through their audits and reviews, and the agencies continue to use the results of these reviews and their own assessments to develop corrective actions and oversee internal controls of federal grants to ensure that necessary controls are in place and operating effectively.

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Abbreviations

ACF	Administration for Children and Families
CFDA	Catalog of Federal Domestic Assistance
CHIP	Children's Health Insurance Program
CMS	Centers for Medicare & Medicaid Services
CPD	Office of Community and Planning Development
DOT	Department of Transportation
FFMIA	Federal Financial Management Improvement Act of 1996
FHWA	Federal Highway Administration
FMFIA	Federal Managers' Financial Integrity Act of 1982
FNS	Food and Nutrition Service
FSA	Federal Student Aid
FTA	Federal Transit Administration
HHS	Department of Health and Human Services
HUD	Department of Urban Development
IPERA	Improper Payments Elimination and Recovery Act of 2010
IPIA	Improper Payments Information Act of 2002
NIFA	National Institute of Food and Agriculture
NIH	National Institutes of Health
OESE	Office of Elementary and Secondary Education
OIG	Office of Inspector General
OMB	Office of Management and Budget
OSERS	Office of Special Education and Rehabilitative Services
PIH	Office of Public and Indian Housing
USDA	Department of Agriculture

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July 30, 2014

The Honorable Tom Carper
Chairman
The Honorable Tom Coburn, M.D.
Ranking Member
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable Claire McCaskill
Chairman
Subcommittee on Financial and Contracting Oversight
Committee on Homeland Security and Governmental Affairs
United States Senate

Federal grants are a significant tool for helping to achieve national objectives as they fund many programs important to the public.¹ In fiscal year 2013, the federal government obligated over \$555 billion for grants for a wide array of activities, including building highways, bridges, and mass transit systems; hiring teachers and increasing student access to higher education; funding medical and other types of research; and providing medical services, nutrition programs, and housing assistance

¹As used in this report, “grant” refers to federal financial assistance that federal agencies provide to nonfederal entities for a public purpose pursuant to a grant agreement or a cooperative agreement and “grantee” refers to a nonfederal entity that enters into such agreements. Neither grant agreements nor cooperative agreements include an agreement under which is provided only direct U.S. government cash assistance to an individual, a subsidy; a loan, a loan guarantee, or insurance. Grant and cooperative agreements, however, are not identical. Under a grant agreement, the grantee is free to implement an agreed-upon program without substantial federal agency involvement. Under a cooperative agreement, the grantee has a significant amount of independence in carrying out its program, but the federal agency is involved in selected areas deemed essential to meeting program requirements and ensuring achievement of program objectives. These areas include, for example, approval of work plans, designation of key positions and approval of key personnel, and approval of monitoring and evaluation plans.

for the economically disadvantaged.² Effective financial and management controls, also known as internal controls, are important for providing reasonable assurance to federal managers and taxpayers that grants are awarded properly, recipients are eligible, and federal grant funds are used as intended and in accordance with applicable laws and regulations. In numerous reviews over the years, we and agency Offices of Inspector General (OIG) have reported weaknesses in agencies' internal controls for managing and overseeing grants. (See the Related GAO Products list at the end of this report.)

Because of concerns about reported weaknesses in grants management and oversight across federal agencies, you asked us to review internal control issues over grants. This report (1) examines whether the five largest grant-making agencies' internal control oversight processes for their grant programs were consistent with Office of Management and Budget (OMB) requirements and (2) describes internal control issues that have been reported related to the grants management process and key grant programs. According to fiscal year 2012 USAspending.gov data, the most current available data at the time we started our review, the five largest grant-making agencies by grant dollars obligated were the Departments of Health and Human Services (HHS), Education (Education), Transportation (DOT), Agriculture (USDA), and Housing and Urban Development (HUD), which we selected as the subjects of our review.³

Using fiscal year 2012 USAspending.gov data, we selected 2 or 3 of the largest program offices in each of the five agencies, for a total of 12 program offices, so that our review would cover a large portion of the

²The \$555 billion represents the amount of obligations incurred for grants in fiscal year 2013 based on USAspending.gov data as of January 27, 2014. Established by the Office of Management and Budget pursuant to the Federal Funding Accountability and Transparency Act of 2006, Pub. L. No. 109-282, 120 Stat. 1186 (Sept. 26, 2006), USAspending.gov is a publicly available online database that allows users to search for detailed information about entities that are awarded federal grants, loans, contracts, and other forms of financial assistance. While the General Services Administration currently operates and maintains USAspending.gov, those responsibilities are being transferred to the Department of the Treasury's Bureau of the Fiscal Service. The transition is planned to be completed by September 30, 2014.

³We reviewed USAspending.gov data for fiscal year 2013 (as of January 27, 2014) and confirmed that these five agencies remained the largest grant-making agencies, based on obligations, in fiscal year 2013. See app. I for details.

federal funds awarded for grants.⁴ Although Medicaid, an HHS grant program, amounted to over 43 percent of the total obligations incurred for grants in fiscal year 2012, we elected to exclude the Medicaid grant program from our review because it has been the subject of numerous reviews, including many by GAO and HHS's OIG. Further, by doing so, we were able to include HHS programs that otherwise would not have been covered in our review and still comply with our selection criteria to cover over 80 percent of an agency's grant obligations, excluding Medicaid obligations. Thus our scope covers oversight of internal controls over a large percentage of the non-Medicaid federal grant dollars.

To assess the reliability of the USAspending.gov obligations data, we (1) reviewed recent GAO work that used the data and (2) compared results of ranking agencies by obligation amounts to the results of ranking agencies based on outlay amounts reported by OMB.⁵ In our recent work, we had assessed the reliability of USAspending.gov obligations data for a report we issued in September 2012 by (1) performing electronic testing of required data elements, (2) reviewing existing information about the data and the system that produced them, and (3) interviewing agency officials knowledgeable about the data, and we determined that the data were sufficiently reliable for the purposes of that report. We also determined that the data were sufficiently reliable for the purpose of selecting agencies and program offices to review for this report. Further, to assess the reasonableness of our decision to use USAspending.gov obligations data to select the top five grant-making agencies, we reviewed OMB's Historical Table 12.3, Total Outlays for Grants to State and Local Governments, by Function, Agency and Program: 1940-2013, to determine the five largest grant-making agencies based on outlays for

⁴Federal grant obligations totaled over \$564 billion in fiscal year 2012, according to USAspending.gov data as of November 19, 2012.

⁵An obligation is a definite commitment that creates a legal liability of the federal government for payment of goods and services ordered or received. A federal agency incurs an obligation, for example, when it awards a grant. An outlay is a payment to liquidate a federal obligation.

grants.⁶ We reviewed and summarized the data and found that the same five agencies we selected based on USAspending.gov data were also the top five grant-making agencies according to OMB's data. As the OMB budget data had undergone rigorous review by OMB, we considered it sufficiently reliable for the purposes of this report.⁷ See appendix I for information about our selection of program offices and further details on our scope and methodology.

To examine whether the agencies' internal control oversight processes for their grant programs were consistent with OMB requirements, we focused on the fiscal year 2012 internal control evaluation processes they performed to comply with the internal control assessment and reporting requirements of OMB Circular No. A-123 and its Appendix A.⁸ We reviewed documentation of the OMB Circular No. A-123 internal control assessment processes for the selected program offices in the five agencies, including documentation of deficiencies identified and planned corrective actions. We interviewed agency officials and officials in the agencies' OIGs about the agencies' assessment processes and oversight of grants-related internal controls. We based our evaluation on OMB Circular No. A-123 and *Standards for Internal Control in the Federal Government*, specifically the standard for monitoring.⁹

To identify internal control issues that have been reported related to the grants management process and key grant programs, we reviewed the agencies' financial statement audit reports for fiscal years 2012 and 2013, and relevant GAO and OIG reports issued in fiscal years 2012 and 2013. We also reviewed improper payments information reported by the

⁶OMB collects data from federal agencies each year to prepare the President's budget. OMB uses these data for a number of purposes related to the budget, including producing the *Historical Tables*, which are publicly available on OMB's website. One series of *Historical Tables* contains information on federal outlays for grants to state and local governments. According to OMB, the purpose of this series of *Historical Tables* is to identify federal government outlays that constitute income to state and local governments to help finance their services.

⁷We also reviewed OMB data for fiscal year 2013 and confirmed that the five largest grant-making agencies, based on outlays, remained the same in fiscal year 2013.

⁸Office of Management and Budget, *Management's Responsibility for Internal Control*, OMB Circular No. A-123 (Dec. 21, 2004).

⁹GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

agencies in their fiscal year 2012 and 2013 agency financial reports and the results of the OIGs' reviews of agencies' compliance with improper payments laws. Finally, we reviewed management challenges reported by the agencies' OIGs. Appendix I provides details of our scope and methodology.

We conducted this performance audit from November 2012 to July 2014 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Grant Types and Programs

The federal government uses grants—forms of federal financial assistance to a state, a local government, or a nongovernmental recipient authorized to receive U.S. government assistance (e.g., charitable or educational institutions) for a specified public purpose—to achieve national objectives and respond to emerging trends, such as changing demographics and changing threats to homeland security. Federal grant programs are diverse and can vary in numerous ways including type, size, nature of recipients, and types of programs they fund. Grant programs also vary in the amount of discretion they give to the recipient in how the funds will be used and the way the funds are allocated or awarded. The types of grants awarded by the agencies in our review include the following:

- Block grants allow recipients, predominately states, to fund a broad range of activities within more general policy areas, such as community development or law enforcement.
- Formula grants are awarded to all eligible grantees based on a statutory allocation formula, which may be based on a number of variables, including population, poverty rate in a given area, or tax effort. The grants are typically awarded to states, which often pass funds through to eligible local government agencies and nonprofit organizations.
- Project grants are generally awarded on a competitive basis and provide funding for fixed or known periods for specific projects or the delivery of specific services or products. Project grants can include

fellowships, scholarships, research grants, training grants, traineeships, experimental and demonstration grants, evaluation grants, planning grants, technical assistance grants, survey grants, and construction grants.

These categories are not mutually exclusive and can overlap when used to define grant programs. For example, HUD awards Community Development Block Grant funds to states using a formula, and then the states distribute the funds to localities, sometimes as project grants.

Some agencies also use cooperative agreements, another form of financial assistance similar to grants, but one in which the federal agency is more involved with the recipient in implementing the financial assistance program. The distinguishing factor between a grant and a cooperative agreement is the degree of federal participation or involvement during the performance of the work activities.

Program Offices and Grant Programs in Our Review

Most of the program offices included in our review oversee and monitor large block and formula grant programs, while others award and manage numerous project or other smaller grants, as described in table 1.¹⁰

Table 1: Grant Program Offices Included in Our Review and Their Largest Grant Programs

Department and program office	Description
Department of Health and Human Services	
• Administration for Children and Families (ACF)	ACF's Temporary Assistance for Needy Families program awards block grants to states to help needy families achieve self-sufficiency.
• National Institutes of Health (NIH)	NIH does not administer a specific large grant program; rather it awards and manages a number of project grants for medical research.
• Centers for Medicare & Medicaid Services (CMS)	The Children's Health Insurance Program is the second largest grant program within CMS. ^a It is a formula grant program funded and administered jointly by CMS and the states.

¹⁰We selected for review programs categorized as grants in USAspending.gov. One of the programs selected, the Public Housing Operating Fund, is categorized in the *Catalog of Federal Domestic Assistance* (CFDA) as "direct payments for specified use," which is a form of financial assistance from the federal government provided directly to individuals, private firms, and other private institutions to encourage or subsidize a particular activity by conditioning the receipt of the assistance on a particular performance by the recipient. While not considered a grant program in the traditional sense by CFDA or by HUD, we included the program in our review based on the USAspending.gov categorization.

Department and program office	Description
Department of Education	
• Federal Student Aid (FSA)	FSA's Pell Grant Program provides need-based grants to low-income undergraduate and certain postbaccalaureate students to promote access to postsecondary education.
• Office of Elementary and Secondary Education (OESE)	OESE's Title I grants program to state educational agencies provides financial assistance through formula grants to local educational agencies and schools with high numbers or high percentages of children from low-income families to help ensure that all children meet challenging state academic standards.
• Office of Special Education and Rehabilitative Services (OSERS)	OSERS's Individuals with Disabilities Education Act, Part B Grants to States program provides formula grants to assist the 50 states, the District of Columbia, Puerto Rico, Outlying Areas, and the Freely Associated States in meeting the excess costs of providing special education and related services to children with disabilities.
Department of Transportation	
• Federal Highway Administration (FHWA)	FHWA's major grant program is Highway Planning and Construction, a formula grant program that provides funds to state departments of transportation.
• Federal Transit Administration (FTA)	FTA's major grant program is the Urbanized Area Formula Program, which provides funds through formula grants to public entities in urbanized areas to support transportation services.
Department of Agriculture	
• Food and Nutrition Service (FNS)	FNS's largest grant program is the National School Lunch Program, which consists of formula grants to state agencies to reimburse schools for lunches served to low-income children.
• National Institute of Food and Agriculture (NIFA)	NIFA does not administer a specific large grant program; rather, it provides a number of formula grants to land-grant universities and competitive grants to researchers in land-grant and other universities for research and education.
Department of Housing and Urban Development	
• Office of Community Planning and Development (CPD)	The largest grant program in CPD is the Community Development Block Grant program, which provides annual grants on a formula basis to general units of local government and states to ensure decent affordable housing, provide services to the most vulnerable in our communities, and create jobs through the expansion and retention of businesses.
• Office of Public and Indian Housing (PIH)	The largest grant program in PIH, the Public Housing Operating Fund, provides funds to public housing authorities through formula grants for the operation and management of public housing.

Source: GAO analysis of USAspending.gov data and agency information. | [GAO-14-539](#)

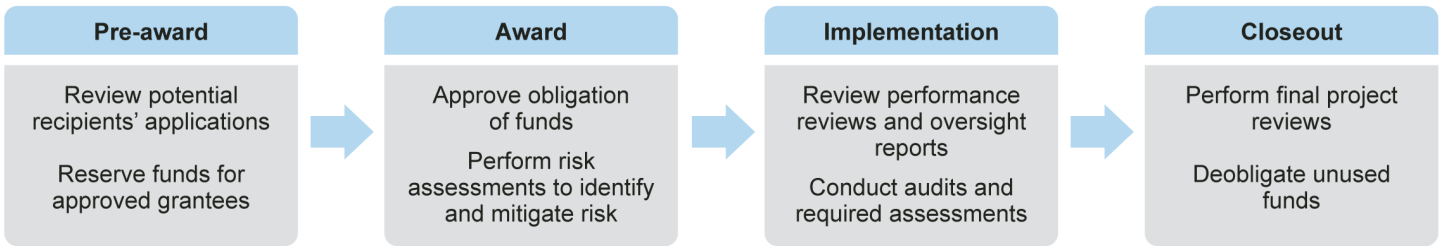
^aMedicaid is CMS's (and the federal government's) largest grant program, accounting for over 43 percent of all federal grant obligations in fiscal year 2012. We elected to exclude Medicaid from our review because it has been the subject of numerous reviews, including many by us and HHS's OIG. Further, by doing so, we were able to include HHS grant programs that otherwise would not have been covered in our review and still comply with our selection criteria to cover over 80 percent of an agency's grant obligations, excluding Medicaid.

Importance of Internal Control

At all stages of the grants life cycle, it is essential that effective internal control systems are in place. Internal control represents an agency's plans, methods, and procedures used to meet its mission, goals, and objectives and serves as the first line of defense in safeguarding assets and preventing and detecting errors, fraud, waste, abuse, and

mismanagement. Effective oversight of internal controls for grant programs is important to provide reasonable assurance to taxpayers that grants are awarded properly, recipients are eligible, and federal funds are used as intended and in accordance with applicable laws and regulations. The term reasonable assurance is important because no matter how well-designed and well-operated, internal control cannot provide absolute assurance that agency objectives will be met. Cost-benefit is an important concept to internal control considerations. Internal control is very broad and encompasses all controls within an agency, covering an agency's entire mission and operations, not just financial operations. Figure 1 shows examples of agencies' control activities in each phase of the grants life cycle.

Figure 1: Internal Control Activities through the Grants Life Cycle



Source: GAO analysis of agencies' internal control documentation. | GAO-14-539

Congress passed the Federal Managers' Financial Integrity Act (FMFIA)¹¹ to help improve the management of federal government programs and strengthen agency internal control systems by requiring ongoing evaluations and reports on the adequacy of executive agency internal control systems.¹² FMFIA, as implemented by GAO standards and OMB guidance, requires agency managers to establish internal control systems that provide reasonable assurance regarding the agency's proper use of funds and resources, compliance with statutes and regulations, and preparation of reliable financial reports. In accordance with FMFIA, OMB has established guidance for agencies for evaluating and reporting on

¹¹The key provisions of the Federal Managers' Financial Integrity Act, Pub. L. No. 97-255, 96 Stat. 814 (Sept. 8, 1982), have been codified at 31 U.S.C. §3512 (c), (d).

¹²See the legislative history for Pub. L. No. 97-255, as reflected in 128 Cong. Rec. 19273-19274 (Aug. 4, 1982) (statement of Senator Roth) and H. Rep. No. 97-38 (May 14, 1981).

their internal controls. This guidance is now contained in OMB Circular No. A-123, *Management's Responsibility for Internal Control*. FMFIA also requires GAO to issue internal control standards for the federal government, which are now contained in *Standards for Internal Control in the Federal Government*.¹³ These standards provide the overall framework for establishing and maintaining internal control and for identifying and addressing major performance and management challenges and areas at greatest risk of fraud, waste, abuse, and mismanagement. The standards also provide that for internal control to be effective, an agency's management should establish both a supportive overall control environment and specific control activities directed at carrying out the agency's objectives.

Annual Internal Control Assessment and Reporting

OMB Circular No. A-123 states that management is responsible for establishing and maintaining internal control to achieve the objectives of effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. OMB Circular No. A-123 provides guidance to federal managers on improving the accountability and effectiveness of federal programs and operations by establishing, assessing, correcting, and reporting on internal control. OMB Circular No. A-123 requires federal agencies and managers to take systematic and proactive measures to, among other things, assess the adequacy of internal control in federal programs and operations and report annually on internal control through management assurance statements.

To assess the adequacy of internal controls, federal agencies conduct an annual assessment that includes testing key controls, identifying needed improvements, and developing and implementing corrective action plans. As part of this assessment, OMB Circular No. A-123 states that management should consider a variety of internal and external sources, including management knowledge and internal program reviews, financial statement audit reports, single audit reports, and improper payment reviews and reports. Further, OMB Circular No. A-123 provides that the agency head should consider input from senior program officials and the OIG.

¹³[GAO/AIMD-00-21.3.1.](#)

OMB Circular No. A-123 requires management to annually provide assurances about the adequacy and effectiveness of its internal control in a management assurance statement. This statement of assurance, which is included in an agency's performance and accountability report or agency financial report, represents the agency head's informed judgment as to the overall adequacy and effectiveness of internal control within the agency based on management's assessment as described above, including the consideration of outside sources such as the results of financial statement audits. Management will give an unqualified statement of assurance when there are no material weaknesses to report and will give a qualified statement of assurance when there are material weaknesses related to internal control.¹⁴

Other Mechanisms for Overseeing and Monitoring Grant Program Internal Controls

Federal agencies, including the five in our review, use other mechanisms and processes, in addition to OMB Circular No. A-123, to oversee and monitor their grants internal controls. The single audit—audit of federal awards, including grant funds, administered by state and local governments and nonprofit organizations—is intended to be an important mechanism used by federal agencies to ensure accountability for federal funds.¹⁵ Single audit reports provide information about the validity of grant expenditures, adequacy of internal controls over federal funds, compliance with grant rules and regulations, and questioned amounts. Grant-making agencies use single audit reports to monitor grantees' compliance with program and financial requirements. The agencies also

¹⁴OMB Circular No. A-123 provides that management categorize deficiencies identified during the annual internal control assessment as *control deficiencies*, *reportable conditions*, or *material weaknesses*. If management determines that a control deficiency, or a combination of deficiencies, could adversely affect the agency's ability to meet its objectives, management should categorize the deficiencies as *reportable conditions*, which are tracked and monitored within the agency. If management determines that the deficiencies are significant enough to report outside the agency, then they are to be considered *material weaknesses* and result in a qualified statement of assurance.

¹⁵The Single Audit Act, as amended and implemented, requires each reporting entity that expends the applicable threshold amount or more in federal awards, including grants and other assistance, in a fiscal year to obtain an annual "single audit," which includes an audit of the entity's financial statements and schedule of the expenditure of federal awards and a review of related internal controls. In December 2013, OMB issued new single audit guidance in *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, which raised the single audit threshold amount from \$500,000 to \$750,000 effective for audits of nonfederal entity fiscal years beginning on or after December 26, 2014. See 78 Fed. Reg. 78590 (Dec. 26, 2013).

use other mechanisms to monitor their grant programs, for example, creating annual grant performance plans, performing eligibility determinations, reviewing grantee financial reports, and conducting management control reviews.

Improper Payments

Congress passed three successive acts from 2002 to 2013 toward eliminating improper payments.¹⁶ The Improper Payments Information Act of 2002 (IPIA) required executive branch agencies to annually review all programs and activities to identify those that are susceptible to significant improper payments, to estimate the annual amount of improper payments for such programs and activities, and to report these estimates along with actions taken to reduce improper payments for programs with estimates that exceed \$10 million.¹⁷ This act was subsequently amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA), which expanded on the previous requirements for identifying, estimating, and reporting on programs and activities susceptible to significant improper payments and for recovering overpayments across a broad range of federal programs.¹⁸ On January 10, 2013, the Improper Payments Elimination and Recovery Improvement Act of 2012 was enacted to impose further requirements to identify, prevent, and recover payment errors.¹⁹

¹⁶Under the Improper Payments Information Act of 2002, as amended, improper payments are statutorily defined as any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements. Incorrect amounts are overpayments or underpayments that are made to eligible recipients (including inappropriate denials of payment or service, any payment that does not account for credit for applicable discounts, payments that are for the incorrect amount, and duplicate payments). An improper payment also includes any payment that was made to an ineligible recipient or for an ineligible good or service, or payments for goods or services not received (except for such payments authorized by law). In addition, pursuant to OMB implementing guidance, when an agency's review is unable to discern whether a payment was proper as a result of insufficient documentation or lack of documentation, this payment must also be considered an improper payment.

¹⁷Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002).

¹⁸Pub. L. No. 111-204, 124 Stat. 2224 (July 22, 2010).

¹⁹We did not consider this statute (Pub. L. No. 112-248) in this report because it was not in effect in fiscal year 2012, the time period covered by our review.

IPERA requires that OIGs determine whether their agencies are in compliance with the criteria listed in IPERA and annually report the results to the head of the agency, among others. OMB also plays a key role in the oversight of the government-wide improper payments issue.²⁰ OMB has established guidance in Appendix C of OMB Circular No. A-123 to implement the requirements of IPERA.²¹ IPERA and the OMB guidance require an OIG to use the following criteria in making a compliance determination on whether the agency has

- published the agency financial report and OMB-required accompanying information on the agency's website,
- conducted a risk assessment for specific programs to determine whether they are susceptible to significant improper payments,
- published improper payment estimates for all high-risk programs,
- reported on actions to reduce improper payments,
- published and met targets for reducing improper payments,
- reported a gross improper payment rate of less than 10 percent for each high-risk program, and
- reported efforts to recapture improper payments.

For the period within the scope of this report, IPERA defined significant improper payments as those in any particular program or activity that exceed both 2.5 percent of program or activity payments and \$10 million annually or that exceed \$100 million.²² For each program identified as susceptible and determined to be at risk of improper payments, agencies are required to report to the President and Congress the annual amount of estimated improper payments, along with steps taken and actions planned to reduce them. Agencies report this information in their annual performance and accountability report or agency financial report.

²⁰Section 2(g)(1) of IPERA required the Director of OMB to prescribe guidance for agencies to implement the requirements of IPERA.

²¹Office of Management and Budget, *Issuance of Revised Parts I and II to Appendix C of OMB Circular A-123*, OMB Memorandum M-11-16 (Washington, D.C.: Apr. 14, 2011), and *Issuance of Part III to OMB Circular A-123, Appendix C*, OMB Memorandum M-10-13 (Washington, D.C.: Mar. 22, 2010).

²²Beginning in fiscal year 2014, IPERA reduced the threshold for "significant" improper payment from 2.5 percent to 1.5 percent. Also, pursuant to the Disaster Relief Appropriations Act, 2013, Pub. L. No. 113-2, § 904(b), 127 Stat. 4, 17 (Jan. 29, 2013), agencies will be required to estimate improper payments in programs funded by Hurricane Sandy relief funds.

Agencies' Assessments of Internal Controls over Grants Programs Were Consistent with OMB Requirements

The processes used by all five agencies to conduct their internal control assessments for fiscal year 2012 were consistent with the requirements in OMB Circular No. A-123. The agencies identified areas of risk in which to implement key controls and then monitored and tested those controls. The agencies identified deficiencies through the control tests, prepared and implemented corrective action plans to address the deficiencies identified, and reported on their internal control through management assurance statements.

Agencies Identified Significant Grants Programs and Processes to Include in Their Fiscal Year 2012 Internal Control Assessments

OMB Circular No. A-123 requires that agencies identify significant areas within their operations in which to implement key controls and then continuously monitor and test those controls. All five agencies conducted a risk assessment to identify significant processes or programs to include in their internal control assessment processes for fiscal year 2012. Based on these risk assessments, as shown in table 2, each agency selected its grants management process (or parts of its grants management process) or it selected grant programs to test controls as part of its fiscal year 2012 OMB Circular No. A-123 internal control assessment process.²³ OMB Circular No. A-123 does not specify a recommended approach for evaluating or testing controls for processes or programs.

Table 2: Grants-Related Processes and Programs Selected for Internal Control Assessment in Fiscal Year 2012

Department and program office	Grants-related process and program selected for review
Department of Health and Human Services	
• Administration for Children and Families	Grants management
• National Institutes of Health	Grants management
• Centers for Medicare & Medicaid Services	Children's Health Insurance Program ^a
Department of Education	
• Federal Student Aid	Pell Grant Program Operations Student Eligibility/Application Processing School Eligibility Service Group Processes
• Office of Elementary and Secondary Education	Grants management – process for ensuring grantees correct findings resulting from monitoring activities ^b

²³The agencies also selected other processes and programs to evaluate controls in fiscal year 2012. The scope of our review is focused on the portions of the OMB Circular No. A-123 process that evaluated grants-related controls.

Department and program office	Grants-related process and program selected for review
• Office of Special Education and Rehabilitative Services	Grants management – process for ensuring grantees correct findings resulting from monitoring activities ^b
Department of Transportation	
• Federal Highway Administration	Grants management
• Federal Transit Administration	Grants management
Department of Agriculture	
• Food and Nutrition Service	Grants management/cooperative agreements
• National Institute of Food and Agriculture	Grants management/cooperative agreements
Department of Housing and Urban Development	
• Community Planning and Development ^c	Disaster Recovery Assistance Neighborhood Stabilization Program #1
• Office of Public and Indian Housing	Public Housing Operating Fund

Source: GAO analysis of agency data. | [GAO-14-539](#)

^aMedicaid, the largest federal grant program, is part of the Centers for Medicare & Medicaid Services. As discussed in app. I, we did not include Medicaid in our review.

^bBased on the deficiencies identified in fiscal year 2011, the Department of Education determined its fiscal year 2012 OMB Circular No. A-123 assessment would focus on the process for ensuring grantee correction of findings resulting from monitoring activities, across multiple program offices, including the Offices of Elementary and Secondary Education and Special Education and Rehabilitative Services.

^cDisaster Recovery Assistance and the Neighborhood Stabilization Program are program areas within the Community Development Block Grant program.

When conducting these risk assessments, the agencies considered the effect that various factors could have on the risk that program objectives may not be met or a misstatement may be made in the financial statements. OMB Circular No. A-123 does not include requirements regarding specific factors to consider when determining which controls to test, and the agencies differed in the number of and specific risk factors they considered, as shown in table 3. Management at all of the agencies approved the selection of processes or programs to be included in their agencies' internal control assessments.

Table 3: Factors Considered by the Five Largest Grant-Making Agencies When Determining the Controls to Test for Their Annual Internal Control Assessments

Factors	Five largest grant-making agencies				
	Department of Health and Human Services	Department of Education	Department of Transportation	Department of Agriculture	Department of Housing and Urban Development
Impact on mission; vision and sensitivity	√		√		
Prior year findings or known issues	√	√	√	√	

Factors	Five largest grant-making agencies				
	Department of Health and Human Services	Department of Education	Department of Transportation	Department of Agriculture	Department of Housing and Urban Development
Included in prior year A-123 review		√	√	√	√
Nature or complexity of process	√	√	√	√	
Human capital	√	√		√	
New or significantly changed programs or operations	√	√		√	
Fraud, waste, and abuse	√	√	√	√	
Material to financial reporting	√	√	√	√	√

Source: GAO analysis of agency documentation. | [GAO-14-539](#)

Agencies Identified Grants Internal Control Issues and Developed Corrective Action Plans

OMB Circular No. A-123 requires agencies to identify needed improvements in controls and take corresponding corrective actions. It also notes that agency managers and staff should be encouraged to identify control deficiencies, as this reflects positively on the agency's commitment to recognizing and addressing management problems. Further, *Standards for Internal Control in the Federal Government* states that findings of audits and other reviews should be promptly resolved.²⁴ The agencies identified deficiencies in certain grants internal controls as a result of their fiscal year 2012 OMB Circular No. A-123 assessment processes. When agencies identified control deficiencies, they prepared corrective action plans that included steps to be taken, responsible parties, and timeframes for completion. We reviewed these plans and determined that if implemented effectively, the steps to be taken should correct the deficiencies. For example:

- HHS's Administration for Children and Families tested controls for the grants management process and identified deficiencies that contributed to delays in receiving grantee financial reports and resolving single audit findings. The Administration for Children and Families developed and implemented corrective actions, including following up with and providing assistance to grantees to improve the timeliness of periodic reporting and taking steps to ensure proper approvals and signatures on documents related to addressing single audit findings.

²⁴[GAO/AIMD-00-21.3.1](#), 20.

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- HHS's National Institutes of Health tested controls for the grants management process and found deficiencies in following up with grantees regarding their late filing of financial reports during the grant closeout phase and resolution of single audit findings. The National Institutes of Health prepared a corrective action plan that includes procedures to improve the timeliness of grantee reports and actions to improve instructions to grantees regarding repayment of disallowed funds found in single audits. It plans to complete these actions by December 2014.
 - Education's Internal Controls Evaluation Group (Evaluation Group) in the Office of the Chief Financial Officer tested related controls for discretionary and formula grants across several program offices, including the Office of Elementary and Secondary Education and Office of Special Education and Rehabilitative Services, and identified deficiencies. Some controls were found to be deficient primarily because of a lack of documentation. The deficiencies resulted in two findings in various offices, including the Office of Elementary and Secondary Education. According to the Evaluation Group, the Office of Elementary and Secondary Education implemented corrective actions, which included ensuring that grantees are making progress on their noncompliance issues before being awarded additional grant funds and providing technical assistance to grantees to help them successfully carry out their projects.
 - DOT's Federal Transit Administration identified a deficiency related to tracking single audit findings. The findings were not being entered into the automated system used to manage oversight program activities and were being tracked offline. The Federal Transit Administration implemented its corrective action plan by issuing a memo to regional offices reiterating the requirements to enter single audit findings in the system in a timely manner and holding routine conference calls and training sessions with regional offices about the issue. Also, according to the Federal Transit Administration, it updated the standard operating procedures for single audit findings, which were in the agency's review process as of April 2014.
 - USDA's Food and Nutrition Service and its National Institute of Food and Agriculture tested controls for the grants management process and identified deficiencies related to grant accruals, completion of site visit reports, and review of single audits. For example, the National Institute of Food and Agriculture identified a deficiency in the control related to timely review and resolution of single audits. Its corrective action plan included drafting standard operating procedures; developing a single audit tracking spreadsheet to document open reviews, findings, and timelines; and obtaining contractor assistance to help clear the extensive backlog of single audit reviews. As of

February 2014, according to the National Institute of Food and Agriculture, the backlog was being addressed.

- HUD's Office of Community Planning and Development assessed controls for the Neighborhood Stabilization Program and identified a deficiency related to the timeliness of grantee reports used to monitor grantees. In response to the finding, a corrective action plan was created to address the untimely filing of these reports. According to HUD, the Office of Community Planning and Development solicited and received recommendations from field offices for improvements to the process. The field office feedback is being incorporated into guidance, and the Office of Community Planning and Development plans to communicate the updated guidance to field offices no later than June 30, 2014.

Agencies Reported on Their Internal Control Assessments in Management Assurance Statements

OMB Circular No. A-123 requires agencies to report annually on management's judgment regarding the adequacy and effectiveness of internal control in assurance statements signed by management. All five agencies included management assurance statements in their annual agency financial reports, as required. Based on their fiscal year 2012 OMB Circular No. A-123 assessment processes, which included testing of key program and process controls, results of financial statement audits, and other information, all five agencies gave a qualified statement of assurance for fiscal year 2012.²⁵

- Three of the five agencies (HHS, DOT, and USDA) qualified their assurance statements because of weaknesses in grants processes or grants programs. Specifically, HHS and USDA reported material weaknesses because of noncompliance with IPERA for some large grant programs, which is discussed later in this report. DOT reported a material weakness involving unliquidated obligations, including in grant programs.²⁶ These weaknesses were also identified by financial statement auditors, as discussed later in this report.
- HUD and Education qualified their fiscal year 2012 assurance for reasons not directly related to grants. HUD qualified its assurance

²⁵Management will give a qualified statement of assurance when there are material weaknesses to report and will give an unqualified statement of assurance when no material weaknesses are being reported.

²⁶Undisbursed balances or unliquidated obligations are funds that the federal awarding agency has obligated by entering into a grant agreement but that the grantee has not drawn down or the federal awarding agency has not disbursed.

because of weaknesses in its human capital operations, and Education qualified its assurance because of weaknesses in its servicing systems for student loan programs.

In their fiscal year 2013 management assurance statements, HHS and USDA continued to qualify their assurance regarding internal controls because of noncompliance with IPERA. For fiscal year 2013, Education management gave an unqualified statement of assurance (no material weaknesses reported). DOT took steps to correct the problems with its unliquidated obligations and no longer reported the issue as a material weakness in fiscal year 2013. However, HUD qualified its fiscal year 2013 assurance because of, among other reasons, a material weakness related to its accounting for formula grants.

Internal Control Issues Reported Include Control Deficiencies, Improper Payments, and Management Challenges

In addition to the issues identified through the OMB Circular No. A-123 process, other audits and reviews have reported internal control issues related to the grants management process and grant programs. We examined the agencies' financial statement audit reports and other reports issued by GAO and the agencies' OIGs and found that internal control deficiencies related to grants, including weaknesses in controls for monitoring and oversight of grantees and unliquidated grant obligations and certain accounting methods for grant programs, have been reported. Further, some of the agencies identified and reported on improper payments in grants programs, and OIGs for some of the agencies reported issues related to agencies' improper payments information. OIGs have also reported management challenges related to grants.

Financial Statement Auditors Reported Significant Deficiencies in Controls over Grants Programs

The primary purpose of a financial statement audit is to provide an opinion about whether an entity's financial statements are presented fairly in all material respects in conformity with an applicable financial reporting framework. Reporting on financial statement audits also includes reports on internal control over financial reporting and on compliance with provisions of laws, regulations, contracts, and grant agreements that have a material effect on the financial statements. Financial statement auditors for three of the agencies reported deficiencies in grants monitoring controls and grants accounting methods.

Specifically, for fiscal years 2012 and 2013, financial statement auditors for DOT, USDA, and HUD reported significant deficiencies, some of which were considered to be material weaknesses, in the agencies' internal controls associated with grant programs.²⁷ Reported grants-related deficiencies primarily related to accounting for grant programs and monitoring procedures over grant activities. A common issue at many agencies is deficiencies in controls over unliquidated grants obligations. Financial statement auditors at DOT, USDA, and HUD reported such deficiencies, as discussed below, and we have previously reported on the issue. In April 2012, we reported that millions of dollars of grant obligations remain in expired grant accounts—accounts that were more than 3 months past the grant end date and had no activity for 9 months or more.²⁸ Agency regulations typically impose closeout procedures upon both the awarding agency and the grantee. Generally, within 90 days after the completion of the grant award, grantees must submit all financial, performance, and other reports as required by the terms and conditions of the award. Also within this 90-day period, grantees generally are to liquidate all obligations incurred under the award. These closeout procedures make funds less susceptible to fraud, waste, and mismanagement; reduce the potential costs to agencies for fees paid to maintain grant accounts; and may enable agencies to redirect resources to other projects.

DOT's financial statement auditors reported deficiencies related to unliquidated obligations in grants programs for both fiscal years 2012 and 2013 and controls over grant accruals in fiscal year 2012.

²⁷A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. Financial statement auditors, who are independent of management, categorize internal control deficiencies as *material weaknesses* or *significant deficiencies*. For financial audit purposes, a *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance. The definitions and reporting requirements for control deficiencies identified in financial statement audits differ from those used under OMB Circular No. A-123.

²⁸GAO, *Grants Management: Action Needed to Improve the Timeliness of Grant Closeouts by Federal Agencies*, [GAO-12-360](#) (Washington, D.C.: Apr. 16, 2012).

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- In fiscal year 2012, the auditors reported a material weakness related to controls over the review and monitoring of grant and nongrant unliquidated obligations, including those at the Federal Highway Administration and the Federal Transit Administration. Specifically, the Federal Highway Administration and the Federal Transit Administration did not timely identify and deobligate unused obligation balances. DOT subsequently performed the necessary deobligations to correct its financial data. Further, to correct the underlying cause, the Federal Highway Administration and the Federal Transit Administration revised their procedures for reviewing and addressing unliquidated obligations in February 2013 and May 2013, respectively. In fiscal year 2013, while the auditors continued to identify issues with unused obligations, they no longer considered the issue a material weakness and reduced it to a significant deficiency.
 - In fiscal year 2012, the auditors reported a significant deficiency related to controls over grant accruals at some program offices, including the Federal Highway Administration. At fiscal year-end, DOT calculated and recorded an estimated liability for amounts owed to its grantees for costs incurred under grant agreements but not yet billed to or reimbursed by DOT. The auditors reported that the Federal Highway Administration did not have adequate controls in place to ensure that all significant grantees and grant programs were properly included in DOT's grant accrual estimate methodology, and as a result, the grant accruals were potentially understated. This issue was no longer reported as a significant deficiency in fiscal year 2013.

For fiscal years 2012 and 2013, USDA financial statement auditors reported a significant deficiency involving unliquidated obligations. They reported that ineffective monitoring and reviewing resulted in invalid obligations remaining open, thus restricting the availability of funding authority and increasing the risk of misstating obligations as of year-end. In the fiscal year 2012 audit report, the auditors noted that substantial improvements had been made to effectively monitor and review unliquidated obligations since fiscal year 2011, when the auditors reported this issue as a material weakness. The auditors made no new related recommendations in the fiscal year 2012 report and downgraded the material weakness to a significant deficiency. In the fiscal year 2013 audit report, the auditors again reported the issue as a significant deficiency and recommended that the department emphasize the importance of complying with USDA's requirements related to unliquidated obligations. The auditors also noted that USDA management

reported that the Forest Service was not in compliance with certain federal requirements related to managing grants programs in fiscal years 2012 and 2013.²⁹

HUD's financial statement auditors reported significant deficiencies related to controls over unliquidated obligations and controls for monitoring some grant programs for fiscal years 2012 and 2013. In addition, the auditors reported a material weakness caused by HUD's noncompliance with the Federal Financial Management Improvement Act of 1996 (FFMIA), including noncompliance associated with the Office of Community Planning and Development's information systems for fiscal years 2012 and 2013.³⁰

- During the financial statement audits for fiscal years 2012 and 2013, HUD's financial statement auditors reported a significant deficiency related to unliquidated obligations. The auditors found inadequate procedures related to timely reviews and recapture of unexpended obligations for several grant programs, including those within the Office of Community Planning and Development, which led to misstatements in HUD's obligation balances. In the fiscal year 2013 audit report, the auditors reported that review and closeout policies had been drafted but not finalized or implemented because of competing priorities. The auditors recommended that the Office of Community Planning and Development review and deobligate invalid obligations.
- For fiscal year 2012, the auditors reported a significant deficiency related to the Office of Community Planning and Development's controls for monitoring grantees, including that the system used to communicate the results and status of on-site monitoring was not

²⁹The Forest Service accounted for about 1 percent of USDA's grant obligations in fiscal year 2012 and was not included in our review.

³⁰FFMIA requires the departments and agencies covered by the Chief Financial Officers Act of 1990 (CFO Act agencies) to implement and maintain financial management systems that comply substantially with federal financial management systems requirements, applicable federal accounting standards, and the *U.S. Government Standard General Ledger* at the transaction level. FFMIA defines the term financial management systems to include the financial systems and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures, controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions. See Federal Financial Management Improvement Act of 1996, Pub. L. No. 104-208, div. A., § 101(f), title VIII, 110 Stat. 3009, 3009-389 (Sept. 30, 1996) (reprinted in 31 U.S.C. § 3512 note).

effective because field offices did not always follow the monitoring handbook and did not always update the information system to reflect current status of monitoring reviews. The auditors repeated recommendations from the prior year to ensure that the monitoring handbook is followed, the information in the grants management system is accurate, and findings from grantee reviews are closed and funds are collected. By fiscal year 2013, most of the recommendations had been implemented, and the auditors no longer reported this issue as a significant deficiency for fiscal year 2013.

- The auditors reported material weaknesses for fiscal years 2012 and 2013 because HUD's financial management systems did not comply with FFMIA, including noncompliance associated with the Office of Community Planning and Development's information systems. The material weakness was due, in part, to the Office of Community Planning and Development's method of accounting and the system used for disbursing obligations, which did not comply with the requirements of FFMIA for maintaining financial management systems that substantially comply with federal financial management systems requirements and applicable federal accounting standards. The auditors reported that the Office of Community Planning and Development was taking steps to address the issues.

Because of many of these internal control issues and ones identified at other federal agencies, we reported a significant deficiency in internal controls related to grants management in our audit reports on the U.S. government's consolidated financial statements for fiscal years 2012 and 2013.³¹ Deficiencies in grants management internal controls could adversely affect the federal government's ability to ensure that grant funds are being properly reported and used in accordance with applicable program laws and regulations.

In addition to reporting on deficiencies in internal controls, financial statement auditors also report on instances of noncompliance with certain laws and regulations. Auditors for HHS and USDA reported instances of noncompliance with IPERA for some grant programs for fiscal years 2012 and 2013, which are discussed later in this report.

³¹GAO, *Financial Audit: U.S. Government's Fiscal Years 2013 and 2012 Consolidated Financial Statements*, [GAO-14-319R](#) (Washington, D.C.: Feb. 27, 2014), and *Financial Audit: U.S. Government's Fiscal Years 2012 and 2011 Consolidated Financial Statements*, [GAO-13-271R](#) (Washington, D.C.: Jan. 17, 2013).

GAO and OIGs Reported Issues Related to Grants Monitoring and Other Aspects of Grant Programs

We and agency OIGs have reviewed federal grants programs and reported findings and recommendations related to monitoring and other aspects of grant programs at many federal agencies, including the five in our review. For example:

- In December 2012, we reported on HHS's Administration for Children and Families Temporary Assistance for Needy Families program.³² We found that the Temporary Assistance for Needy Families program's accountability framework provided incomplete information on how states' noncash services were contributing to the program's purposes. States are required to submit several reports to HHS. Taken together, these reports serve as the accountability framework in place to help HHS and Congress ensure that states use Temporary Assistance for Needy Families program funds for proper purposes and identify needed program improvements. We recommended that HHS develop a detailed plan with timelines to revise reporting categories for program expenditures. HHS formed an internal workgroup to review and revise a Temporary Assistance for Needy Families program reporting form for collecting more-detailed expenditure data, and published two *Federal Register* notices in September 2013 and January 2014, regarding proposed revisions to the financial reporting form. HHS plans to issue the form effective for fiscal year 2015.
- In June 2011, we reported on education reform grants to states required by the American Recovery and Reinvestment Act of 2009 (Recovery Act).³³ We found that Education had provided extensive support to grantee states and had begun monitoring states' progress in meeting program goals.³⁴ Education also developed ways for grantees to share information, such as hosting meetings on specific initiatives. Some officials from grantee states said they would find this information useful, but they were generally unaware of these resources or were unable to access them. We recommended that Education facilitate information sharing among grantees. Among other things, Education established communities of practice to address multiple topics. Education oversees the activities of each community

³²GAO, *Temporary Assistance for Needy Families: More Accountability Needed to Reflect Breadth of Block Grant Services*, [GAO-13-33](#) (Washington, D.C.: Dec. 6, 2012).

³³Pub. L. No. 111-5, 123 Stat. 115 (Feb. 17, 2009).

³⁴GAO, *Race to the Top: Reform Efforts Are Under Way and Information Sharing Could Be Improved*, [GAO-11-658](#) (Washington, D.C.: June 30, 2011).

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- by managing a work plan that includes the target dates for each activity. In addition, Education communicates these activities to members of each community of practice via emails and calls as well as a monthly update to all grantees with upcoming dates and events.
- In December 2011, HHS's OIG reported on a science awards program at the National Institutes of Health.³⁵ The program is administered through cooperative agreements, which are similar to grants but require more involvement by the awarding agency. The OIG reported that it found documentation and reporting issues, which the National Institutes of Health is taking steps to correct. Specifically, the Clinical and Translational Science Awards Program did not properly document awardees' progress under their cooperative agreements. The OIG recommended that the National Institutes of Health ensure that program staff document their monitoring of awardee progress; ensure timely submission of required reports; maintain official files in accordance with federal policy; and, as required for cooperative agreements, provide substantial involvement to Clinical and Translational Science Awards Program awardees. The National Institutes of Health concurred with the recommendations and stated that it had taken or planned to take steps to implement them.
 - In August 2012, DOT's OIG reported on weaknesses in grants oversight at the Federal Transit Administration and made several related recommendations.³⁶ Specifically, the OIG reported that the Federal Transit Administration lacked adequate guidance for ensuring that findings from grantee oversight reviews were consistently identified and adequately tracked to ensure grantees were complying with laws and regulations and implementing corrective actions. In response, the Federal Transit Administration stated that it was (1) revising its oversight and review processes to, among other things, identify grant recipients needing technical assistance and (2) developing standard operating procedures to provide more consistency across regions and implementing new performance measures. The OIG reported that these actions, both those taken and planned, were responsive to the recommendations.

³⁵Department of Health and Human Services Office of Inspector General, *NIH Administration of the Clinical and Translational Science Awards Program*, OEI-07-09-00300 (Washington, D.C.: December 2011).

³⁶Department of Transportation Office of Inspector General, *Improvements Needed in FTA's Grant Oversight Program*, MH-2012-168 (Washington, D.C.: Aug. 2, 2012).

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- In February 2012, USDA's OIG performed work related to the Recovery Act and reported that it found that the Food and Nutrition Service did not create adequate, proactive controls to ensure that states awarded grants for schools to purchase and renovate food service equipment based on Recovery Act criteria, and did not ensure timely reporting of Recovery Act spending data on Recovery.gov as required by OMB guidance on using funds pursuant to the Recovery Act.³⁷ The OIG recommended that the Food and Nutrition Service continue to update and implement adequate, proactive controls for its standard competitive grant award process. The Food and Nutrition Service agreed that continuous improvement of controls over the competitive award process was warranted and agreed with the OIG's recommendation to update controls. According to USDA's Office of the Chief Financial Officer, the Food and Nutrition Service took corrective action and the recommendation was closed in February 2013.
 - In July 2013, HUD's OIG reported that HUD's guidance for ensuring grantee compliance with the Community Development Block Grant program's timeliness spending requirement was not always implemented effectively, and documentation of HUD's rationale for not sanctioning noncompliant grantees was inadequate.³⁸ HUD is to annually determine whether Community Development Block Grant grantees—states, cities, and counties—are carrying out grant activities in a timely manner, which includes timely drawdown of grant funds. HUD is to generate a monthly report to help field offices monitor grantees' compliance with the timeliness spending requirement. The OIG recommended, among other things, that HUD (1) strengthen controls over Community Development Block Grant procedures related to the monthly timeliness report and notification to noncompliant grantees and (2) establish documentation requirements and procedures for grantees that do not comply with the timeliness spending requirement. HUD generally concurred with these recommendations and stated that it would enhance current procedures to address the recommendations.

³⁷Department of Agriculture Office of Inspector General, *American Recovery and Reinvestment Act of 2009, National School Lunch Program Equipment Assistance Grants*, Report 27703-0001-HQ (Washington, D.C.: Feb. 15, 2012).

³⁸Department of Housing and Development Office of Inspector General, *Controls Over the Timeliness of CDBG Entitlement Spending*, 2013-NY-0003 (Washington, D.C.: July 19, 2013).

Agencies Reported Improper Payments in Grant Programs

In both fiscal years 2012 and 2013, four of the largest grant-making agencies reported almost \$5 billion in estimated improper payments in grants programs. Agencies are required by IPIA, as amended by IPERA and implemented by OMB guidance, to periodically review and assess all programs and activities to identify those susceptible to significant improper payments, estimate the annual amount of improper payments, and report these estimates along with actions taken to reduce improper payments when the estimates exceed both \$10 million annually and 2.5 percent of program or activity payments (or 1.5 percent of program or activity payments starting in fiscal year 2014) or when the estimates exceed \$100 million.

As shown in table 4, four of the agencies reported improper payment estimates and error rates (i.e., amount of estimated improper payments divided by total program outlays) in grant programs administered by the program offices in our review for fiscal years 2012 and 2013.³⁹

Table 4: Improper Payment Estimates and Error Rates in Grant Programs, Fiscal Years 2012 and 2013

Dollars in millions

Department and grant program	Fiscal year 2012		Fiscal year 2013	
	Improper payments	Error rate (percentages)	Improper payments	Error rate (percentages)
Department of Health and Human Services (HHS)				
• Head Start	\$46.2	0.6	^a	^a
• Foster Care	80.2	6.2	\$70.0	5.3
• Child Care and Development Funds	474	9.2	306.0	5.9
• Children's Health Insurance Program	704	8.2	646	7.1
Department of Education (Education)				
• Pell Grants	829	2.5	731	2.3
• Title I Grants	28.3	0.2	56.7	0.4

³⁹ HUD did not report estimated improper payments for its grant programs. According to the OIG's April 2014 report on HUD's compliance with IPERA, HUD had previously identified Community Development Block Grant programs as susceptible to improper payments; however, HUD found that estimated improper payments in those programs were below the \$10 million threshold for 2 consecutive years. Therefore, in 2007, OMB approved HUD's request for relief from the annual improper payment reporting for the Community Development Block Grant programs. In its fiscal year 2013 agency financial report, HUD noted that it will continue to conduct an annual risk assessment of the programs and provide results annually to OMB.

Dollars in millions

Department and grant program	Fiscal year 2012		Fiscal year 2013	
	Improper payments	Error rate (percentages)	Improper payments	Error rate (percentages)
Department of Transportation (DOT)				
• Planning and Construction	103.2	0.2	91.4	0.2
• Formula Grants	38.1	0.4	62.6	0.7
Department of Agriculture (USDA)				
• School Lunch Program	1,557	15.5	1,774	15.7
• Special Supplemental Nutrition Program for Women, Infants, and Children	202	4.1	198	4.4
• School Breakfast Program	752	25.2	831	25.3
• Child and Adult Care Food Program	14	1.6	10	1.1

Source: Agency financial reports for fiscal years 2012 and 2013 for HHS, Education, DOT, and USDA. | [GAO-14-539](#)

³According to HHS, OMB granted HHS relief from reporting annual error rate estimates for fiscal year 2013 because of Head Start's strong internal controls, monitoring systems, and low reported error rates.

OIGs Reported Issues with Agencies' Improper Payments Information

IPERA requires, among other things, OIGs to determine whether their agencies are in compliance with the criteria listed in IPERA and annually report the results to the heads of their agencies, the Comptroller General, and certain congressional committees. Many OIGs do so by reviewing their agencies' improper payment reporting in the annual agency financial report and accompanying materials. For fiscal years 2012 and 2013, the OIGs reported the following for their respective agencies.

- The HHS OIG reported that while HHS met many of IPERA's compliance requirements, it did not fully comply with IPERA for fiscal years 2012 and 2013 for some of its grant programs.⁴⁰ Specifically, the OIG reported that HHS did not comply with IPERA for the Children's Health Insurance Program for fiscal year 2012 because it did not publish a corrective action plan for the program's improper payments. HHS did publish a corrective action plan for this program for fiscal year 2013. For the Foster Care program, the OIG reported

⁴⁰Department of Health and Human Services Office of Inspector General, *U.S. Department of Health and Human Services Met Many Requirements of the Improper Payments Information Act of 2002 But Was Not Fully Compliant*, A-17-13-52000 (Washington, D.C.: March 2013), and *U.S. Department of Health and Human Services Met Many Requirements of the Improper Payments Information Act of 2002 But Did Not Fully Comply for Fiscal Year 2013*, A-17-14-52000 (Washington, D.C.: April 2014).

that HHS did not comply for fiscal year 2012 because the improper payment rate of 6.2 percent exceeded HHS's target rate of 4.5 percent. For fiscal year 2013, HHS's Foster Care improper payments rate of 5.3 percent met the target rate of 6 percent for that year. In the case of the Temporary Assistance for Needy Families program, the OIG reported that HHS did not report an improper payments estimate for either fiscal year 2012 or fiscal year 2013. According to HHS, statutory limitations related to obtaining state data prohibited HHS from developing an estimate. However, HHS has reported that it is taking steps and has planned actions to help prevent and reduce improper payments, including providing technical assistance to help strengthen state program integrity efforts, revisions to the Temporary Assistance to Needy Families financial reporting form so that states can provide more accurate information about how they are using program funds, and sharing with states information and best practices for reducing improper payments.

- The USDA OIG reported that USDA did not meet IPERA's compliance requirements for fiscal years 2012 and 2013 for some of its grants programs, including the School Lunch and School Breakfast Programs and the Child and Adult Care Food Program.⁴¹ The OIG reported that the School Lunch and School Breakfast Programs did not comply because they reported improper payment rates that exceeded 10 percent for both fiscal years 2012 and 2013. According to the OIG, the Food and Nutrition Service's administration of these programs was highly decentralized and involved many governmental and nongovernmental organizations to provide benefits at approximately 100,000 locations. The OIG reported that Food and Nutrition Service officials stated that they were aware of the significant improper payment rate in these two programs, and they hired a contractor to conduct a study to help develop initiatives and practices to address this problem. The OIG reported that the results of the study were pending at the time of its review for fiscal year 2013 and noted that Food and Nutrition Service officials believed it would take time to achieve an error rate less than 10 percent.⁴² For the Child and Adult

⁴¹Department of Agriculture Office of Inspector General, *U.S. Department of Agriculture Improper Payments Elimination and Recovery Act of 2010 Compliance Review for Fiscal Year 2012*, 50024-0004-11 (Washington, D.C.: Mar. 14, 2013), and *U.S. Department of Agriculture Improper Payments Elimination and Recovery Act of 2010 Compliance Review for Fiscal Year 2013*, 50024-0005-11 (Washington, D.C.: Apr. 15, 2014).

⁴²According to the Food and Nutrition Service, the study will develop and validate models for updating erroneous payment estimates, among other things. The Food and Nutrition Service expects the final report on the study in early 2015.

Care Food Program, the OIG reported that USDA reported only a partial estimate of improper payments for both fiscal years 2012 and 2013 because the Food and Nutrition Service did not have a cost-effective method for estimating improper payments for one of the program's two components—Family Day Care Homes Meal Claims. Food and Nutrition Service officials continued to report difficulties in determining a gross estimate for the Child and Adult Care Food Program, which included over 190,000 participating day care homes and centers with varied eligibility requirements for each of the program's two components. According to the OIG's report on its fiscal year 2013 review, the Food and Nutrition Service has conducted feasibility studies since 2006 to develop a reliable method for estimating improper payments, but the studies were not reliable. The Food and Nutrition Service told us that it continues to assess methods of estimating erroneous payments and that a new study will be conducted in 2014 to explore an alternative method of measuring the rate of erroneous payments.

- For both fiscal years 2012 and 2013, Education's OIG reported that Education met IPERA's compliance requirements; however, improvements were needed in the estimation methodology for both the Pell Grant and Direct Loan Programs.⁴³ The OIG recommended that Education (1) continue working with OMB to obtain approval for an estimation methodology that addresses current limitations with some data used and (2) where estimates are based on the results of program reviews, include all program review results for a sufficient period of time in the universe of potential improper payments. Education agreed with the OIG's recommendations and noted that it had modified its fiscal year 2014 estimation methodologies.
- For fiscal years 2012 and 2013, DOT's OIG reported that although DOT met IPERA's compliance requirements, some of the information reported in its agency financial reports was inaccurate.⁴⁴ The OIG recommended, among other things, that DOT implement procedures

⁴³Department of Education Office of Inspector General, *U.S. Department of Education's Compliance with the Improper Payments Elimination and Recovery Act of 2010 for Fiscal Year 2012*, ED-OIG/A03N0001 (Washington, D.C.: Mar. 15, 2013), and *U.S. Department of Education's Compliance with the Improper Payments Elimination and Recovery Act of 2010 for Fiscal Year 2013*, ED-OIG/A19O0002 (Washington, D.C.: Apr. 15, 2014).

⁴⁴Department of Transportation Office of Inspector General, *DOT's FY 2012 Improper Payment Reporting Generally Complies with IPERA*, FI-2013-053 (Washington, D.C.: Mar. 14, 2013), and *Accuracy and Reliability of DOT's Improper Payment Reporting Can Be Improved*, FI-2014-037 (Washington, D.C.: April 15, 2014).

to ensure that all elements required for IPERA reporting are accurate and supported by documentation. The OIG also reported that while DOT's programs met IPERA's required improper payment rate of less than 10 percent for both fiscal years 2012 and 2013, the Federal Transit Administration did not meet its target error rates for those years. In its 2012 and 2013 agency financial reports, DOT reported error rates of 0.44 percent and 0.73 percent, respectively, for its Formula Grants Program. These rates did not meet the target error rates reported in DOT's fiscal year 2012 and 2013 agency financial reports of 0.25 percent and 0.50 percent, respectively.

OIGs Reported Management Challenges Related to Grant Programs

The Reports Consolidation Act of 2000 requires each OIG to prepare a statement that summarizes what the OIG considers to be the most serious management and performance challenges facing its agency.⁴⁵ Agencies are to include the OIG's summary of management challenges in their annual agency financial report or performance and accountability report.

- HHS's OIG reported grants management and identifying and reducing improper payments as top grants-related management challenges for fiscal year 2012. HHS is the largest grant-making agency in the federal government, and oversight and management of both new and continuing grant programs are crucial to HHS's mission. The OIG has found internal control deficiencies, problems with financial stability, inadequate organizational structures, inadequate procurement and property management, and inadequate personnel policies and procedures among grantees. In addition, the OIG reported that HHS faces challenges complying with IPERA for some of its programs, including the Temporary Assistance for Needy Families program, as discussed above. For fiscal year 2013, the OIG reported a similar challenge for grants management—protecting HHS grants and contract funds from fraud, waste, and abuse. The improper payments-related challenge reported by the OIG for fiscal year 2013 was focused on Medicare programs and not on grants programs.
- Education's OIG reported management challenges for fiscal years 2012 and 2013, including oversight and monitoring of the department's programs and grantees and improper payments. Regarding oversight and monitoring, the OIG reported that the

⁴⁵Pub. L. No. 106-531, 114 Stat. 2537 (Nov. 22, 2000), *codified, as amended*, at 31 U.S.C. § 3516.

number of different entities and programs requiring monitoring and oversight, the amount of funding that flows through the department, and the impact that ineffective monitoring could have on stakeholders make monitoring and oversight a challenge. The OIG also reported that Education faces challenges in its efforts to successfully prevent, identify, and recapture improper payments in some programs, including the Pell Grant and Title I Programs. For fiscal year 2013, while the OIG noted progress was being made in some areas, it reported management challenges similar to those for fiscal year 2012.

- For fiscal year 2012, DOT's OIG reported a grants-related management challenge: ensuring effective oversight of Recovery Act projects and applying related lessons learned to improve DOT's infrastructure programs. For fiscal year 2013, the OIG reported challenges in strengthening existing highway and transit project oversight mechanisms and improving financial management over grants to better use funds, create jobs, and improve infrastructure.
- For fiscal years 2012 and 2013, USDA's OIG reported a management challenge: identifying, reporting, and reducing improper payments, including those in some grant programs. The OIG reported, among other things, that USDA continues to struggle to meet IPERA's compliance requirements for reporting and preventive measures. Also, the OIG noted that related quarterly reports did not always provide accurate, complete, and timely information.
- Among other issues, HUD's OIG reported oversight and monitoring of some of its grant programs as a management challenge in fiscal years 2012 and 2013. The challenges included oversight of Recovery Act funds and monitoring grants for housing assistance programs and for disaster recovery. For example, the OIG reported that HUD faces challenges in monitoring Community Development Block Grant Disaster Recovery Assistance funds because of, among other things, limited resources for performing oversight, the broad nature of HUD projects, a lack of understanding of disaster recovery grants by the recipients, and the length of time needed to complete projects.

Concluding Observations

In fiscal year 2013, the federal government obligated over \$555 billion in grants for a wide array of activities. Effective oversight of internal controls is important for providing reasonable assurance to federal managers and taxpayers that grants are awarded properly, recipients are eligible, and federal grant funds are used as intended and in accordance with applicable laws and regulations. Our review found that the five largest grant-making agencies' internal control assessment processes were consistent with the requirements in OMB Circular No. A-123 and its Appendix A. The findings from these assessment processes and from

other reviews identified material weaknesses and significant deficiencies in grants management. OMB Circular No. A-123 notes that agency managers and staff should be encouraged to identify control deficiencies, as this reflects positively on the agency's commitment to recognizing and addressing management problems. Further, agencies are estimating that billions of dollars in improper payments occur each year in the grants programs. Financial statement auditors, OIGs, and we continue to focus on grants internal controls through audits and reviews, and the agencies continue to use the results of these reviews and their own assessments to develop corrective actions and oversee internal controls of federal grants to ensure controls are in place and operating effectively.

Agency Comments

We provided a draft of this report to the Secretaries of Health and Human Services, Education, Transportation, Agriculture, and Housing and Urban Development. In general, all five agencies concurred with the information in the report. Education, DOT, USDA, and HUD also provided technical comments that were incorporated as appropriate. In addition, Education provided written comments, which are reprinted in appendix II. We also provided a draft of the report to the Director of OMB, and OMB responded that it had no comments.

We are sending copies of this report to the Secretaries of Health and Human Services, Education, Transportation, Agriculture, and Housing and Urban Development; the Director of the Office of Management and Budget; appropriate congressional committees; and other interested parties. In addition, the report is available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at (202) 512-2623 or davisbh@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last

page of this report. GAO staff members who made key contributions to this report are listed in appendix III.

A handwritten signature in cursive script that reads "Beryl H. Davis".

Beryl H. Davis
Director, Financial Management and Assurance

Appendix I: Objectives, Scope, and Methodology

Our objectives were to (1) examine whether the five largest grant-making agencies' internal control oversight processes for their grant programs were consistent with Office of Management and Budget (OMB) requirements and (2) describe internal control issues that have been reported related to the grants management process and key grant programs.¹

Agency Selection

To select the agencies to include in our review and to obtain adequate coverage of federal grant dollars for fiscal year 2012—the most recently completed fiscal year at the time we started our review—we reviewed and summarized grant obligations data reported by agencies through USAspending.gov (as of November 19, 2012).² We decided to include the five agencies with the highest amounts of grants obligations, which accounted for almost 75 percent of total federal grant obligations for fiscal year 2012, excluding Medicaid, as discussed further below. The Departments of Health and Human Services (HHS), Education (Education), Transportation (DOT), Agriculture (USDA), and Housing and Urban Development (HUD) were the top five federal grant-making agencies based on grants obligations for fiscal year 2012. We also reviewed USAspending.gov data for fiscal year 2013 (as of January 27,

¹As used in this report, “grant” refers to federal financial assistance that federal agencies provide to nonfederal entities for a public purpose pursuant to a grant agreement or a cooperative agreement and “grantee” refers to a nonfederal entity that enters into such agreements. Neither grant agreements nor cooperative agreements include an agreement under which is provided only direct U.S. government cash assistance to an individual, a subsidy, a loan, a loan guarantee, or insurance. Grant and cooperative agreements, however, are not identical. Under a grant agreement, the grantee is free to implement an agreed-upon program without substantial federal agency involvement. Under a cooperative agreement, the grantee has a significant amount of independence in carrying out its program, but the federal agency is involved in selected areas deemed essential to meeting program requirements and ensuring achievement of program objectives. These areas include, for example, approval of work plans, designation of key positions and approval of key personnel, and approval of monitoring and evaluation plans.

²Established by OMB pursuant to the Federal Funding Accountability and Transparency Act of 2006, Pub. L. No. 109-282, 120 Stat. 1186 (Sept. 26, 2006), USAspending.gov is a publicly available online database that allows users to search for detailed information about entities that are awarded federal grants, loans, contracts, and other forms of financial assistance. While the General Services Administration operates and maintains USAspending.gov, those responsibilities are being transferred to the Department of the Treasury's Bureau of the Fiscal Service. The transition is planned to be completed by September 30, 2014.

2014) and confirmed that the five largest grant-making agencies, based on obligations, in fiscal year 2012 remained the same in fiscal year 2013.

To assess the reliability of the USAspending.gov obligations data, we (1) reviewed recent GAO work that used the data and (2) compared results of ranking agencies by obligation amounts to the results of ranking agencies based on outlay amounts reported by OMB, as discussed below.³ In our recent work, we had assessed the reliability of USAspending.gov obligations data for a report we issued in September 2012 by (1) performing electronic testing of required data elements, (2) reviewing existing information about the data and the system that produced them, and (3) interviewing agency officials knowledgeable about the data, and we determined the data were sufficiently reliable for the purposes of that report. We also determined the data were sufficiently reliable for the purpose of selecting agencies and program offices to review for this report.

Further, to assess the reasonableness of our decision to use USAspending.gov obligations data to select the top five grant-making agencies, we reviewed OMB's Historical Table 12.3, Total Outlays for Grants to State and Local Governments, by Function, Agency and Program: 1940-2013, to determine the five largest grant-making agencies based on outlays for grants.⁴ We reviewed and summarized the data and found that the same five agencies we selected based on USAspending.gov data were also the top five grant-making agencies according to OMB's data. As the OMB budget data had undergone

³An obligation is a definite commitment that creates a legal liability of the federal government for payment of goods and services ordered or received. A federal agency incurs an obligation, for example, when it awards a grant. An outlay is a payment to liquidate a federal obligation.

⁴OMB collects data from federal agencies each year to prepare the President's budget. OMB uses these data for a number of purposes related to the budget, including producing the *Historical Tables*, which are publicly available on OMB's website. One series of *Historical Tables* contains information on federal outlays for grants to state and local governments. According to OMB, the purpose of this series of *Historical Tables* is to identify federal government outlays that constitute income to state and local governments to help finance their services.

rigorous review by OMB, we considered them sufficiently reliable for the purposes of this report.⁵

In our review of the USAspending.gov data, we noted that grant obligations for Medicaid, one of HHS's grant programs, amounted to over 43 percent of total obligations incurred by the federal government for grants in fiscal year 2012. We elected to exclude the Medicaid program from our review because it has been the subject of numerous reviews, including many by GAO and HHS's OIG, and by doing so, we were able to include HHS grant programs that otherwise would not have been covered in our review and still comply with our selection criteria to cover over 80 percent of each agency's grant obligations. (See table 5 and the related discussion.) Even after excluding Medicaid funds for fiscal year 2012, HHS was still the largest grant-making agency as measured by grant obligations.

During our initial planning work, we learned that agencies generally include cooperative agreements as part of their grants programs.⁶ We also learned that although USAspending.gov data for Education categorize Pell Grants as "direct payments for a specified use" and do not identify them as "grants," Education considers Pell Grants to be grants, and the Pell Grant Program is Education's largest grant program.⁷ Therefore, in addition to USAspending.gov's obligations for grants, we included in the scope of our review USAspending.gov amounts for cooperative agreements for the five agencies and Pell Grants. In addition, while HUD considers its Public Housing Operating Fund a subsidy program, and the *Catalog of Federal Domestic Assistance* categorizes

⁵We also reviewed OMB data for fiscal year 2013 and confirmed that the five largest grant-making agencies, based on outlays, remained the same in fiscal year 2013.

⁶Like grants, cooperative agreements are a form of financial assistance. The distinguishing factor between a grant and a cooperative agreement is that cooperative agreements require a greater degree of federal participation or involvement during the performance of the work activities.

⁷"Direct payments for a specific use" is another form of financial assistance whereby the federal government directly provides payments to individuals, private firms, and other private institutions to encourage or to subsidize a particular activity by conditioning the receipt of the assistance on a specific action by the recipient.

the program as “direct payments for specified use,” we included the program in our review based on the USAspending.gov categorization.⁸

In addition, during our planning work, we found that federal agencies rely on their program offices to provide assurance statements regarding the effectiveness of their internal controls. The program office assurance statements are then rolled up into the agency-wide management assurance statement, which the agencies are required by OMB to provide in their performance and accountability reports or agency financial reports. Therefore, to obtain the most dollar coverage and cover the greatest subject area during our review, we selected the 2 or 3 largest program offices from each agency in order to cover over 80 percent of grant obligations for each agency, resulting in a total of 12 program offices, as shown in table 5. These 12 program offices together represented almost 75 percent of the total government-wide grants obligations (excluding Medicaid) for fiscal year 2012. If we had not excluded Medicaid, the National Institutes of Health grant programs would not have been selected for inclusion in our review as the Centers for Medicare & Medicaid Services and the Administration for Children and Families together would have accounted for about 88 percent of HHS grant obligations. By excluding Medicaid, we were able to include the National Institutes of Health grant obligations, allowing us to cover additional grant programs.

⁸As we reported in our September 2012 report *Grants to State and Local Governments: An Overview of Federal Funding Levels and Selected Challenges*, GAO-12-1016, determining a definitive number of federal grant programs presents certain difficulties. The *Catalog of Federal Domestic Assistance* (CFDA) is the single authoritative, government-wide compendium and source document for descriptions of federal programs that provide assistance or benefits to the public. Officials from the General Services Administration told us that each agency determines how to organize and describe its programs for publication in the CFDA, as long as the agency adheres to the underlying requirement to describe the program’s legal authority, administering office, funding, purpose, benefits, and beneficiaries.

Table 5: Amount and Percentage of Grant Obligations (Excluding Medicaid) for the Five Largest Grant-Making Agencies and Their Largest Program Offices, Fiscal Year 2012

Dollars in millions

Agency and program offices	Amount of grant obligations	Percentage of grant obligations ^a
Department of Health and Human Services	\$98,400	100.0
• Administration for Children and Families	47,517	48.3
• National Institutes of Health	22,242	22.6
• Centers for Medicare and Medicaid Services ^b	10,569	10.7
Total percentage of obligations for selected program offices		81.6
Department of Education	77,696	100.0
• Federal Student Aid	33,647	43.3
• Office of Elementary and Secondary Education	21,859	28.1
• Office of Special Education and Rehabilitative Services	15,840	20.4
Total percentage of obligations for selected program offices		91.8
Department of Transportation	51,932	100.0
• Federal Highway Administration	34,454	66.3
• Federal Transit Administration	11,871	22.9
Total percentage of obligations for selected program offices		89.2
Department of Agriculture	30,876	100.0
Food and Nutrition Service	28,296	91.6
• National Institute of Food and Agriculture	1,238	4.0
Total percentage of obligations for selected program offices		95.6
Department of Housing and Urban Development	12,107	100.0
• Office of Community Planning and Development	6,845	56.5
• Office of Public and Indian Housing	5,131	42.4
Total percentage of obligations for selected program offices		98.9
Total for agencies (excluding Medicaid)	\$271,011	
Total for program offices (excluding Medicaid)	\$239,509	

Source: GAO analysis of USAspending.gov data for fiscal year 2012 (as of November 19, 2012). | [GAO-14-539](#)

^aThe program offices listed in this table are the two or three largest program offices in the agency, based on grant obligations. We selected those program offices that together constitute over 80 percent of an agency's grants obligations. Therefore, percentages for program offices in this table do not add up to 100 percent.

^bThe Centers for Medicare & Medicaid Services amounts exclude Medicaid obligations.

Examination of Agencies' Internal Control Oversight

To examine whether the five largest grant-making agencies' internal control oversight processes for their grants programs were consistent with OMB requirements, we focused on the agencies' fiscal year 2012 internal control evaluations performed to meet the internal control assessment and reporting requirements of OMB Circular No. A-123 and its Appendix A. We also considered *Standards for Internal Control in the Federal Government*, specifically, the standard for monitoring.⁹ The standards provide the overall framework for establishing and maintaining internal control in federal programs. The monitoring standard states that internal control monitoring should assess the quality of performance over time and ensure that the findings of audits and other reviews are promptly resolved.

We obtained and analyzed documentation from the 12 program offices and from each of the five agencies' Office of the Chief Financial Officer. This documentation included or described relevant policies and procedures, risk assessments, testing methodologies and results, deficiencies found and corrective action plans developed and implemented as part of the fiscal year 2012 OMB Circular No. A-123 internal control assessment process. We used a data collection instrument to collect and summarize information obtained from the agencies. We did not reperform agency testing of internal controls or conduct our own testing of controls.

We also interviewed officials in the 12 program offices and officials from each of the five agencies' Office of the Chief Financial Officer and OIG about the agencies' assessment processes and oversight of grants-related internal control.

Identification of Reported Internal Control Issues

To identify internal control issues that have been reported related to the grants management process and key grant programs, we reviewed the

⁹GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

agencies' financial statement audit reports for fiscal years 2012 and 2013 and relevant GAO and OIG reports issued in fiscal years 2012 and 2013 to identify grants-related internal control findings and recommendations. We also reviewed improper payment information reported by the five agencies in their agency financial reports for fiscal years 2012 and 2013 to determine whether the agencies identified improper payments in their grants programs.¹⁰ We reviewed the OIGs' reports on their agencies' compliance with the criteria listed in the Improper Payments Elimination and Recovery Act of 2010 for fiscal years 2012 and 2013. We also reviewed management challenges reported by the agencies' OIGs for fiscal years 2012 and 2013.

We conducted this performance audit from November 2012 to July 2014 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

¹⁰The amounts and error rates the agencies reported for improper payments are based on the amounts of program outlays, which differ from the obligation amounts we used to select the agencies. The differences could be related to timing differences, as obligations are recorded when grants are awarded, and outlays are recorded when funds are actually disbursed to grantees. Also, the sources for the amounts differ. We used obligations data reported to USAspending.gov (as of November 19, 2012), and the outlay data the agencies reported came from other agency sources of expenditure data.

Appendix II: Comments from the Department of Education



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF THE CHIEF FINANCIAL OFFICER

THE CHIEF FINANCIAL OFFICER

July 10, 2014

Ms. Beryl Davis
Director, Financial Management and Assurance
Government Accountability Office
Washington, DC 20548

Dear Ms. Davis:

Thank you for the opportunity to respond to the Government Accountability Office's (GAO's) draft report titled "Federal Grants: Agencies Performed Internal Control Assessments Consistent with Guidance and Are Addressing Internal Control Deficiencies" (GAO-14-539).

Department of Education (Department) officials found the report generally balanced and informative. As the report indicates, we believe the Department's implementation of internal controls is consistent with Office of Management and Budget (OMB) guidance and continues to improve and be more robust. Ensuring program integrity and safeguarding taxpayers' interests are top priorities for the Department. To this end, the Department continues to strengthen internal controls over all programs through the use of innovative internal controls reviews, strategic training initiatives to build program capacity, and efficient use of technology. This increases our effectiveness in overseeing and monitoring the Department's programs and grantees, which includes identifying, correcting, and, in many cases, preventing the improper use of Federal funds.

It is important to note the methodologies we use to estimate improper payments for the Pell and Title I Grant Programs are both thorough and complex, yet are approximations that may tend to overestimate the expected overpayments. For example, these estimates are based on audit and review data that often include grant expenditures or award amounts that are found to be appropriate but were initially lacking sufficient documentation. They are also based in large part on independent, single audits of varying quality, and usually lacking in specific and comprehensive detail by their very nature as organization-wide audits. Department offices, managers, and staff responsible for programs are held accountable for promptly detecting, investigating, and recovering any improper payments that may occur through a variety of mechanisms. These mechanisms include the establishment, monitoring, and reporting of sufficient internal controls, including a control environment that focuses on preventing improper payments from being made.

OMB designated Pell Grants as a "high-priority" program per Executive Order 13520. In developing the estimation methodologies for Pell, our Office of Federal Student Aid (FSA) leveraged the substantial investment in and available data from its existing internal control

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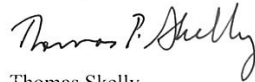
Page 2 - Ms. Beryl Davis

framework (to include compliance and assessment functions, such as program reviews). Leveraging existing investments in and data from the program review process avoids significant costs. Further, the analysis of this rich data set helps inform tangible corrective actions. This approach provides for a more efficient allocation of resources and enables improvements to these core underlying processes over time.

In 2012 and 2013, the OIG found the Department to be in compliance with the Improper Payments Elimination and Recovery Act of 2010. The OIG suggested that estimating improper payments for FSA programs as well as Title I could be strengthened, and the Department has acted promptly on those recommendations. The Department will continue to prioritize top-quality internal controls in grant programs, especially with respect to improper payments.

The Department appreciates GAO's thorough reporting on this important topic. Should you have any questions or need additional assistance, please contact Phillip Juengst in the Department's Office of the Chief Financial Officer at 202-245-8030.

Sincerely,



Thomas Skelly
Director, Budget Service and Delegated to Perform
Functions and Duties of the Chief Financial Officer

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

Beryl H. Davis, (202) 512-2623 or davisbh@gao.gov

Staff Acknowledgments

In addition to the contact named above, Kimberly McGatlin (Assistant Director), Laura Bednar, Maria C. Belaval, Bruce David, Lauren S. Fassler, Maxine Hattery, Diane Morris, Danietta Williams, and Elizabeth Wood made significant contributions to this report.

Related GAO Products

School-Meals Programs: USDA Has Enhanced Controls, but Additional Verification Could Help Ensure Legitimate Program Access. [GAO-14-262](#). Washington, D.C. May 15, 2014.

Recovery Act: Grant Implementation Experiences Offer Lessons for Accountability and Transparency. [GAO-14-219](#). Washington, D.C.: January 24, 2014.

Grants Performance: Justice and FEMA Collect Performance Data for Selected Grants, but Action Needed to Validate FEMA Performance Data. [GAO-13-552](#). Washington, D.C.: June 24, 2013.

Grants Management: Improved Planning, Coordination, and Communication Needed to Strengthen Reform Efforts. [GAO-13-383](#). Washington, D.C.: May 23, 2013.

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WIC Program: Improved Oversight of Income Eligibility Determination Needed. [GAO-13-290](#). Washington, D.C.: February 28, 2013.

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Highway Infrastructure: Federal-State Partnership Produces Benefits and Poses Oversight Risks. [GAO-12-474](#). Washington, D.C.: April 26, 2012.

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Improper Payments: Remaining Challenges and Strategies for Governmentwide Reduction Efforts. [GAO-12-573T](#). Washington, D.C.: March 28, 2012.

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National Institutes of Health: Employment and Other Impacts Reported by NIH Recovery Act Grantees. [GAO-12-32](#). Washington, D.C.: November 10, 2011.

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Medicaid and CHIP: Reports for Monitoring Children's Health Care Services Need Improvement. [GAO-11-293R](#). Washington, D.C.: April 5, 2011.

Department of Education: Improved Oversight and Controls Could Help Education Better Respond to Evolving Priorities. [GAO-11-194](#). Washington, D.C.: February 10, 2011.

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