Absolute vs. Creative Decision-Making: Weighing Grant Risk

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May 4, 2012, 1:30 PM – 2:30 PM

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Presentation Content

‣ Balancing compliance and performance
‣ Common examples of risk associated with managing grants
‣ Identifying and analyzing the degree of risk built into a funded grant application

What is risk?

Exposure to the chance of injury or loss; a hazard or dangerous chance.

--- Dictionary.com

Is risk always "bad"?

What is risk?

To venture upon; take or run the chance of.

--- Dictionary.com

We make
personal and professional
decisions every day
that factor in degree of risk.

Some are conscious, and some
are subconscious/routine.

Name that risk!

- What shoes should I wear?
- Should I bring an umbrella?
- How quickly should I take my first sip of coffee?
- Is my cell phone charged?
- Should I wear a seat belt?
- Do I need to stop at the gas station on my way to work?
- Should I speed up to beat that red light?
- Should I walk alone down a dark street?

Are these decisions conscious, or subconscious? Can conscious decisions eventually become subconscious?

What are the odds that…

- …the people who work on my grants will make a mistake?
- …my organization will be site visited?
- …an auditor will catch an error?
- …any penalties imposed will be harsh?

May 2012

Risk-Based Grant Decision-Making

- It is natural and normal for grants to be full of risks throughout the lifecycle.
- Some risks can be predicted and controlled, but others cannot – the key is to be proactive wherever and whenever you can, and to have processes in place to be reactive as needed.
- Once you become comfortable with the idea that risk is inherent to grants, making decisions to avoid risk becomes second nature to you.

Risk-Based Grant Decision-Making

▸ There are no hard and fast rules about what makes a decision high risk or low risk

▸ Current proposed changes to the OMB Circulars implies that risk increases relative to the amount of Federal funding received

Risk-Based Grant Decision-Making

- As part of the decision-making routine, conduct a thorough analysis of each issue – seemingly black and white issues may have some gray areas
- "Absolute"- no flexibility
- "Creative" – options are possible
- "Creative" interpretations must always still be compliant – never bypass, twist, or disregard compliance in the name of creativity

Risk-Based Grant Decision-Making

- Pre-award risks primarily relate to preparedness to write a grant proposal, ability to be competitive to win an award, and ability to facilitate smooth grants management. Do you have the time and capacity to develop an accurate and complete proposal designed to win, yet also protect your organization?
- Post-award risks primarily relate to outcomes and compliance. Do you have the resources (grant and non-grant) to deliver and manage what you promised?

Risk-Based Grant Decision-Making

▸ When you receive a grant award:

○ Identify the absolutes and share with internal stakeholders (e.g., supplanting, unallowable costs, minimum outcome measures, participant eligibility requirements)

○ Find potential flexibility within compliance (e.g., equipment vs. supply definitions, outreach approaches)

○ Options selected must remain true to the intent of the original approved application

Post-Award Noncompliance: Beyond a reasonable risk!

▸ There are many consequences associated with noncompliance, including:
  ○ Return of grant funds to funder
  ○ Triggering additional audits
  ○ Media and public relations concerns
  ○ Decreased ability to successfully compete for future grants
  ○ Being labeled a "high risk" grantee

Don't be a high risk grantee!

- History of unsatisfactory performance
- Not financially stable
- Management system does not meet standards
- Has not conformed to terms of previous awards
- Is "otherwise not responsible"

2 CFR 215 (A-110) Subpart B _____.14

Don't be a high risk grantee!

Special conditions may include:

▸ Payment on reimbursement basis

▸ Withholding authority to proceed until acceptable performance

▸ Requiring more detailed financial reports

▸ Additional project monitoring

▸ Requiring additional technical assistance or managerial assistance

▸ Establishing additional prior approvals

How is noncompliance discovered?

- Single Audits (required if you expend more than $500K/year in Federal funding)
- OIG Audits and Investigations (including whistleblowers, False Claims Act/fraud accusations)
- Program Monitoring (e.g., site visit, desk audit, media report)
- Self-Disclosure/Reporting

Identify/Analyze Degree of Risk

- <u>Risk Point A</u>: Lack of grants management and compliance regulatory knowledge.
  - How well do you know the funder's as well as your own organizational rules, regulations, policies, and procedures?
- <u>Risk Point B</u>: Lack of internal controls.
  - Does your organization (at all levels) have a strong internal controls system, and understand the consequences of noncompliance?

Identify/Analyze Degree of Risk

- <u>Risk Point C</u>: Lack of ability to make risk-based decisions due to lack of a system for measuring and assessing risk.
  - How do you determine "degree" of risk?

What are internal controls?

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

1. effectiveness and efficiency of operations,
2. reliability of financial reporting, and
3. compliance with applicable laws and regulations.

Standards for Internal Control in the Federal Government (GAO "Green Book"), November 1999

What are internal controls?

- <u>Sarbanes-Oxley Act of 2002</u> – new internal control requirements imposed on publicly-traded companies – result of the Enron scandal
- <u>OMB Circular A-123</u> Management's Responsibility for Internal Control – re-examination of Federal agency internal controls – issued January 2004, effective October 2005

Internal Control Definitions

▸ <u>Control deficiency</u> – 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 misstatements in a timely basis.

○ Design deficiency – when a control necessary to meet the objective is missing or an existing control is not properly designed, so that even if the control operates as designed the objective is not always met.

○ Operation deficiency – when a properly designed control does not operate as designed or when the person performing the control is not qualified or properly skilled to perform the control effectively.

Internal Control Definitions

▸ <u>Reportable condition</u> - a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report external financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements, or other significant financial reports, that is more than inconsequential will not be prevented or detected.

Internal Control Definitions

▸ <u>Material weakness</u> – a reportable condition, or combination of reportable conditions, that results in more than a remote likelihood that a material misstatement of the financial statements, or other significant financial reports, will not be prevented or detected.

5 Internal Control Standards

1. Control environment
2. Risk assessment
3. Control activities
4. Information and communication
5. Monitoring

Control Environment

- The organizational culture - the foundation for all other components of internal control, providing discipline and structure. Management's leadership in setting values of integrity and ethical behavior.
  - Management must clearly demonstrate its commitment to competence in the workplace, including the need for personnel to possess and maintain the proper knowledge and skills to perform their assigned duties as well as understand the importance of maintaining effective internal control.
  - Problem Examples: recent institutional change; top management unaware of lower level actions; disgruntled employees; budget cuts.

Risk Assessment

▶ Risk assessment involves identifying internal and external risks that may prevent the organization from meeting its objectives, then analyzing the identified risks for potential impact.

○ Problem Examples: If the agency or program does not have adequate performance measures – if you don't know how to measure success, you will not be able to adequately assess risks; inadequate strategic plan.

Control Activities

- Control activities include policies, procedures, and mechanisms in place to help ensure that agency objectives are met.
  - Segregation of duties: separate personnel with authority to authorize a transaction, process the transaction, and review the transaction.
  - Physical controls over assets: limited access to inventories or equipment.
  - Appropriate documentation and access to documentation.
  - Problem Examples: understaffing; employees do things "the way they have always been done"; key documentation is lacking or does not exist.

Information and Communication

▸ Relevant, reliable, and timely information should be communicated internally and externally to relevant personnel at all levels.

  ○ Problem Examples: When top management needs information, there is a mad scramble to assemble the information – it is not readily available; management does not have reasonable assurance that the information it is using is accurate

Monitoring

▸ Monitoring should occur in the normal course of business, ingrained in the agency's operations. Periodic reviews, reconciliations, or comparisons of data should be included as part of the regular assigned duties of personnel. A systematic process should be in place for reporting deficiencies to appropriate personnel and management responsible for that area for evaluation and correction.

The Test of Allowability

▶ Grant costs must meet all four factors to meet the test of allowability

○ Reasonable (prudent person test).
○ Allocable (incurred solely to advance the approved grant work; provides proportionate benefits; necessary).
○ Consistently applied at your organization using generally accepted accounting principles.
○ Conform to grant limitations and exclusions.

2 CFR 220 (A-21) C

Untimely Expenditures

▸ What is the difference?

- Purchased
- Invoiced
- Obligated
- Encumbered
- Expended
- Used

Risk Assessment Systems

▸ Internal Programmatic Review

o Proactive "Checkup"

o Try to cover all grants

- *Progress in achieving outcomes and producing deliverables*

- *Staffing capacity and ability*

- *Assessment processes and evaluation design*

o Follow-up to initial grants management start-up meeting

o Frequency of review individualized based upon complexity of grant project design, regulations, budget size, staffing, etc.

Risk Assessment Systems

- Internal Compliance Review
- Proactive "Checkup"
- Prioritize review order based on internal risk assessment instrument/process
  - *Review applicable grant-related regulations with Project Director, administrator(s), project staff, Finance staff*
  - *Recommend/provide training as appropriate*
  - *Conduct a systems analysis overview to determine if policies and procedures are compliant*
- Follow-up to initial grants management start-up meeting
- Additional follow-up may be needed based on findings