

DEPARTMENTAL GRANT APPEALS BOARD

Department of Health, Education, and Welfare

SUBJECT: Trenton Board of Education  
Docket No. 78-2  
Decision No. 74

DATE: JAN. 11, 1980

DECISION

This is an appeal from a determination by the Acting Regional Commissioner for Educational Programs, Region II, that the Trenton Board of Education is required to refund \$419,119 expended under grants for a Dropout Prevention Program. The grants were made under section 807 of the Elementary and Secondary Education Act of 1965, as amended, and totaled \$1,086,540 for the two fiscal years ending June 30, 1973. The specific disallowances and the reasons for them are described in the Panel Chairman's Order to Develop Record, dated December 28, 1978.

At the outset the panel wishes to note that its work would have been much easier if the parties had made a greater effort to provide timely and thoughtful presentations. There was too much reliance on submitting documents consisting of the arguments made at earlier stages of the audit process and a number of those documents were submitted for the record several different times. Once a document is in the record it normally serves no purpose to submit it again each time additional comments are filed. Moreover, we remind those who present matters to the Board that 45 CFR 16.6(a)(2) asks that the application for review "clearly identify the question or questions in dispute and contain a full statement of the grantee's position with respect to such question or questions and the pertinent facts and reasons in support of such position."

Usually it will be in the applicant's interest to make a new statement of the position it wishes the Board to consider rather than to rely on what it submitted in earlier stages of the audit determination process. It is instructive to consider the preamble to 45 CFR Part 16 as published on August 12, 1975 in 40 Federal Register 33936:

The attention of the grantees is called to the need for brief and discriminating identification of the real matters in dispute and of basic factual background which will normally include: the terms of the grant award; a specification of the action taken by the grantee now in dispute; the text of pertinent HEW policy statements and regulations relied on by the grantee; correspondence between the grantee and HEW relied on by the grantee; the audit report, if relevant; the determination appealed from; and a brief statement of the grantee's grounds for

appeal. Agency responses should normally identify relevant statements of fact that are considered incorrect or misleading and should include such additional documents as are considered necessary for an understanding of the agency position.

The Panel also notes with disappointment the inability of the parties to enter into stipulation on any of the factual issues on which they were asked to seek to reach agreement. Most of these should have been susceptible to resolution at an intermediate level of administration. Instead, representatives at top echelons of each party met in Washington, rather than where the grantee's records were located, without any positive result.

We do not seek to assign fault and mention this matter only in the hope it may cause parties in future matters to make greater efforts to reach agreement on those matters as to which there should be no issue. If so, the parties and the public will benefit.

#### Administrative Finality of Prior Regional Office Action

Page 11 of the Order to Develop Record asked the parties to comment on the administrative finality of a notification in which the Assistant Regional Commissioner informed the Grantee that the disallowances would be reduced to \$169,129. Having the benefit of their comments and additional material, the Panel is now prepared to decide that question.

The audit report, which recommended disallowances of \$419,119, and the Grantee's responses to it were reviewed by officials in the Regional Office. On October 21, 1976, Charles A. O'Connor, Jr., Assistant Regional Commissioner, Occupational and Adult Education, wrote the Grantee enclosing "preliminary determinations" to the effect that the disallowances should be reduced to \$189,197. His letter stated that those determinations would become final after 30 days unless "this office is provided with supplemental information of such substance as to cause us to amend one or more of our determinations." The Grantee then submitted further information which caused Regional Office officials to allow an additional \$20,068 for indirect costs. Accordingly, in a letter dated June 9, 1977, Mr. O'Connor informed the Grantee that the balance of disallowed costs was \$169,129 (\$189,197 less the newly allowed \$20,068). The letter, however, added:

Dr. Tilroe [who had recommended the "preliminary determinations" to reduce the disallowance to \$189,197] is no longer with this office. Should this matter not be settled promptly and should there be re-negotiation, you should be aware that the \$439,187 will be the figure since there is not concurrence with the \$249,990 of cost disallowances reinstated by Dr. Tilroe at the earlier date.

The last chance nature of the offer was repeated in a terse letter from Mr. O'Connor to the Grantee, dated June 27, 1977, which stated in full:

Referring to my letter of 9 June 1977, if you wish to reopen negotiation at this time, we will do so on the basis of the \$439,187. There can be no further extention of time. Please advise promptly your intentions.

The Grantee refused to agree to refund the \$169,129 and on December 30, 1977, John Sokol, Acting Regional Commissioner for Educational Programs, informed the Grantee that the findings and recommendations of the audit report were sustained, except for an allowance of indirect costs. It stated:

Our final determination is that it will be necessary for the Trenton Board of Education to refund \$419,119 to the U.S. Office of Education. Previously disallowed indirect costs in the amount of \$20,068 have been reinstated.

The Grantee asserts that the greater allowances proposed in the October 21, 1976 letter of the Assistant Regional Commissioner should not have been affected because it sought further consideration of the remaining disallowances. It views the rescision of those allowances as an attempt by regional officials to coerce it into a compromise. It, therefore, argues that it should get the benefit of the allowances and this appeal should concern only the \$169,129 which was proposed for disallowance under the October 21, 1976 letter.

The Office of Education, on the other hand, says that there was never a decision by an authorized official to make the allowances. According to it, the Acting Regional Commissioner was the only official who had authority to make a final determination on an audit report. Mr. O'Connor, an Assistant Regional Commissioner, made only the preliminary determinations described in the October 21, 1976, letter and enclosure on the basis of Dr. Tilroe's recommendations. When Dr. Tilroe left, the matter was reviewed by others who disagreed with his recommendations. The Agency explains the letters of June 9 and 27, 1977, by saying that when disagreement with Dr. Tilroe's recommendations arose, Mr. O'Connor decided that even though they did not provide a proper basis for allowances, in order to avoid backing down on what already had been presented to the Grantee as a basis for settling the audit, he would honor the recommendations if the matter could be settled promptly. It thus concludes that a binding decision was never made to allow any of the audit report's recommended disallowances, except for the \$20,068 in indirect costs. In support of that position, Agency cites the rule that the Government can be bound only through the actions of those authorized to bind it.

The Government's position is weakened by the evident fact that Mr. O'Connor was acting in the course of an established office procedure for arriving at a final determination on the audit.<sup>1/</sup> Perhaps under that procedure the "preliminary determinations" in the letter of October 21, 1976, which were favorable to the Grantee could have been withdrawn if the deciding officials believed that Dr. Tilroe's recommendations did not evaluate the facts correctly or apply agency policy properly. The letters of June 9 and 27, 1977, however, confirmed willingness to make the allowances without any reservation that that was a "preliminary" determination, subject only to the improper condition that the Grantee not question the remaining disallowances.

We do not agree with the Grantee that this was done for the purpose of depriving it of a right to further consideration of the disallowed items. The record shows that the Agency gave the Grantee more than the specified time for making submissions and there is no indication that it attempted to deny the Grantee the benefit of the regular administrative process. We accept the version that the Agency was taking what it believed to be the easier course of avoiding the appearance of backing down on its

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<sup>1/</sup> Page 2 of the Agency's memorandum of April 3, 1978 to the Board states:

Prior to the issuance of the final audit report the Assistant Regional Commissioner for Occupation and Adult Education (ARC/OAE) was the Office of Education representative on the HEW Audit Agency during the HEW prelease report procedures. When the final [audit] report was issued, the ARC/OAE and a program officer on his staff [Dr. Tilroe] were responsible for coordinating the resolution of the audit. [Emphasis in original.] The ARC/OAE did not have the authority to actually resolve audit 02-60100. By July 1977, the ARC/OAE and the aforementioned program officer were no longer employed by the Regional Office of Education.

There is no claim that the rejection of these officials' views was other than an honest difference of judgment; nothing in the record suggests that their employment was terminated as a result of wrongdoing in this matter. The characterization of their function as "coordinating the resolution of the audit" and not including "authority to actually resolve" ignores the fact that as a part of "coordinating", the Grantee was informed that the preliminary determination would become final in the absence of the submission of additional information. It is clear that the ARC/OAE's proposal transmitted to the Grantee was intended to become the final decision of the Agency by the passage of time and nothing more. In effect, it showed what the Agency had decided, in the absence of a further submission by the Grantee. We note also that in its memorandum of June 29, 1979, the Agency states that the Acting Regional Commissioner in an attempt to save face advised the Grantee "to forward their remittance of \$169,129 instead of exercising his authority and perhaps better judgment to reopen the audit."

preliminary evaluation rather than following the more straightforward and legally acceptable course of notifying the Grantee that the preliminary determinations were withdrawn.

But regardless of why it was done, the preliminary determinations were not withdrawn but confirmed in the June letters as final determinations for the allowed items, coupled with an improper condition with respect to the Grantee's waiver of its right to further consideration of the disallowed items. We, therefore, accept the June determination but reject the condition which precludes consideration of the remaining disallowances.<sup>2/</sup> Accordingly, we shall proceed to consider the items in the disallowances which make up the \$169,129.

## II

### 1. Special Pregnancy Education Classes (SPEC)

The \$5,787 remaining disallowance under this item was based on a finding that \$5,787 in salaries and related costs were paid for Deborah Perry and Brenda Lanier, outreach counselors, who replaced two social workers employed by the Grantee in prior years. This was determined to be a supplanting of local funds. The Grantee states that it had an educational program for unwed mothers prior to the commencement of the section 807 project, but that program used no outreach counselors. In addition, it asserts that in 1970-71, it spent some \$50,270 for the unwed mothers' program, of which \$25,900 came from local sources and \$24,370 from Titles I and VI grants.

In the first project year involved here, ending in 1972, the Grantee seems to have retrenched on SPEC, having claimed to have spent \$26,000 in local funds and \$313 of section 807 grant funds. It withdrew its Title I and Title VI funds from this activity. In the second year of the project, it claims to have spent another \$26,000 in local funds and \$12,982 in section 807 grant funds, still a reduction in total expenditures from the year ending in 1971.

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<sup>2/</sup> The allowances turn upon fact and policy judgments; if allowance of the expenditures constituted a clear violation of the statute a different case for review would be presented. See LEGIS 50/The Center for Legislative Improvement, DGAB Docket No. 76-17, Decision No. 48, September 26, 1978, p. 2.

The reduced expenditures under the project conflict with the undertaking described in the abstract of the grant application for "an expanded Special Pregnancy Education Class (SEPC) program to meet more adequately the educational, health, and social service needs of girls who would leave school because of pregnancy." We find no explanation of the reason for the reduction. We do not, however, regard that as a basis for disallowance; rather it should have been a concern of the OE program officials who were working with the Grantee during the life of the project.

The Order to Develop Record suggested that the maintenance of local funds complied with the no supplant provisions of 45 CFR 124.26, then applicable, and that a reduction of use of Titles I and VI funds for SPEC was not, in itself, cause for disallowance. Nothing in the additional information submitted argues against that interpretation. We hold, therefore, that the \$5,787 disallowance should be restored.

## 2. Team Teaching

A \$55,495 disallowance was made for the cost of personnel whom the Assistant Regional Commissioner found did not work in the team teaching effort or whose activities previously had been supported by local funds.

We do not regard this as a matter of tracing the salaries of particular individuals to determine whether they were paid from local funds one year and project grant funds the next. Rather, the burden is on the Grantee to show that the local fiscal effort for the activity did not diminish. It has not sustained that burden here. The facts are undisputed that the teaching activity did not involve an expansion from the year before the project commenced so local fiscal effort in the teaching involved was replaced by the grant funds. The \$55,495 should be disallowed. It, therefore, is not necessary to resolve the factual issue of whether salaries of individuals who did not work in the program were charged to this account.

## 3. Early Warning System

The enclosure transmitted with the Assistant Regional Commissioner's letter of October 21, 1976, proposed a disallowance of \$35,758 as having been in excess of amounts budgeted for the early warning system to identify potential dropouts. No requests for budget changes were made. While the terms and conditions of the grant permitted transfers to assure effectiveness of the project, they provided that "no transfers may be made which alter the approved project." The Regional Office's acceptance of project activity reports was not tantamount to an approval of the transfer.

Here the Grantee claimed more than double the budgeted amount and still failed to put any early warning system into effect. This cannot be characterized as a transfer to "assure effectiveness of the project."<sup>3/</sup> The \$35,758 should be disallowed.

4. Salaries and Fringe Benefits of Employees Not Listed for Payment of Grant Funds

A disallowance of \$1,514 was made for payments with respect to two employees not listed as being paid from grant funds. A mere statement by the Grantee that the individuals were engaged in project work, unsupported by records, does not permit recognition of the expenditures; accordingly, the amount must be disallowed.

5. Unapproved Programs

A disallowance of \$3,525 was made for rent for an alternative school facility because it was not included in the project budget. The Order to Develop Record recognized that 45 CFR 124.9 (January 28, 1969) required approval for the rental of space as being necessary for the success of the project, but stated that unless OE asserts that the rental charge was unnecessary, the Panel would consider that the requirement was met.

The OE response of June 29, 1979, to questions in the Order to Develop Record states that the rent was disallowed by the Assistant Regional Commissioner because it was included in indirect costs. The enclosure to that official's letter of October 21, 1976, however, stated that the disallowance resulted from the fact that the amount was not in the approved budget.

The item is identified solely with the project and would not appropriately be an indirect cost (see item 7); the audit report transferred this item from the indirect cost claim of the Grantee to a direct cost item but then disallowed it as having been expended for an unapproved activity. In light of the allowance by the Assistant Regional Commissioner of \$115,341 for the instructional program, the further allowance of the \$3,525 for rent is reasonable and it should be allowed. The absence of a budget item for this purpose is not fatal because, unlike the excess expenditures for the early warning system, the nature and size of the transfer was not such as to "alter the approved project" and it is reasonable to conclude that the amount of rent claimed for an activity of the size involved here was necessary to assure "effectiveness of the project."

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<sup>3/</sup> We need not consider whether validity of the transfer provision is in question because of a possible failure to publish properly. In the absence of the provision there would be no authority to transfer budgeted amounts; accordingly, a determination that it is invalid would not benefit the Grantee.

## 6. Unapproved Alterations

The enclosure to the Assistant Regional Commissioner's letter of October 21, 1976, provided for a disallowance of \$5,203 for alterations as having been in excess of the \$3,000 in the project budget for that purpose. For the reasons stated under item 3 above this amount should be disallowed.

## 7. Indirect Costs

The grantee originally charged \$114,288 as indirect costs. The audit action disallowed \$32,643 of that amount as being chargeable to direct costs which, however, were held not to be allowable under the rule prohibiting the use of the grant for supplanting State and local funds. An additional amount of \$3,525, determined to be direct costs of rental space, also was disallowed as being for an unapproved activity. Those two items were thereafter considered further and disposed of in the audit process under the direct cost allocations.

The remaining amount of \$78,120 was disallowed as not having been computed in accordance with the rule requiring use of an approved percentage rate to ascertain indirect costs. During the period that this matter was under consideration in the Regional Office, an indirect cost rate was established for each of the two grant years and that resulted in an indirect cost allowance of \$20,068, assuming recognition of direct costs as shown in the attachment to Assistant Regional Commissioner O'Conner's letter of October 21, 1976.

The grantee now contends that it incurred other costs which should offset the disallowed \$78,120. It argues that the budgets had contained \$80,485 for overhead costs which, however, were not transferred to reimburse such costs; and instead the funds were left in the project accounts. It further asserts that because expenditures under the project were in excess of budgeted amounts it transferred \$66,095 of local funds to the project. The grantee concludes that at least some of the disallowances represent expenditures of local rather than Federal funds. It, however, provides no further details.

The most that can be said for the grantee's contention is that the use of the amounts available for the project, consisting of the Federal grant plus a substantial amount of local funds, was in an amount sufficient to provide expenditures equal to, or in excess of, the Federal grant. That, however, falls short of accounting for expenditures as actually having been made and as having been made in accordance with the terms and conditions of the grant. The grantee has not established that any expenditures other than those already allowed have been made in accordance with the terms and conditions of the grant. As a result there is no basis for making a further allowance to offset any part of the \$78,120. The appeal on that item must, therefore, be denied.



Our conclusion does not, of course, affect the allowance of indirect costs under the established rates. Because such costs are a percentage of allowed direct costs, we assume a further computation will be made to reflect the \$9,312 of direct costs allowed here in excess of those considered when the prior computation of indirect costs was made.

8. Fringe Benefits

A disallowance of \$3,795 was made for expenditures for fringe benefits which were not properly chargeable to the project. The Grantee does not contest that disallowance unless to claim that the amount was offset by application of the non-Federal funds described under item 7 above. For the reasons stated under that item, such an offset is not proper. The \$3,795 should be disallowed.

CONCLUSION

The allowances proposed in the Assistant Regional Commissioner's letter of October 21, 1976, plus the \$20,068 of indirect costs allowed in his letter of June 9, 1979, should be recognized. This leaves a balance of \$169,129 which, for the reasons given above, should be treated as follows:

Items	Allowed	Disallowed
1. Special Pregnancy Education Classes	\$ 5,787	\$
2. Team Teaching		55,495
3. Early Warning System		35,758
4. Salaries and Fringe Benefits		1,514
5. Unapproved Programs	3,525	
6. Unapproved Alterations		5,203
7. Indirect Costs		58,052*
8. Fringe Benefits		<u>3,795</u>
	<u>\$9,312</u>	<u>\$159,817*</u>

\*Subject to adjustment for additional allowances in this appeal.

/s/ Edwin Yourman, Panel Chairman

/s/ Thomas Malone

/s/ Malcolm S. Mason