



State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 1 of 8

INTRODUCTION

Federal grant proceeds account for approximately half of all monies received by the State of Arizona Government. Though various agencies may initially receive grant proceeds from the Federal Government on behalf of the State for a particular project or program, it is the State, as an entity, that is legally the prime recipient of all Federal grant monies.

Agencies that initially receive grant monies from the Federal Government frequently redistribute—or pass-through—grant proceeds to other agencies or to organizations to carry out part or all of a Federal program.

As stewards of public monies, the oversight responsibilities of pass-through grantors begin before and continue after an award is made to a subrecipient. In fulfilling these responsibilities there are a number of specific internal control activities that should be, at the very least, considered and frequently performed by pass-through grantors related to the distribution of grant monies to subrecipients.

The performance of any internal control activity should be reasonable and economically justified under the circumstances. Factors to consider include the dollar amount of the grant proceeds, the contemplated and actual use of the grant proceeds, the cost of controls relative to the amount of the grant, and the personnel available to conduct the activities discussed below. Agency management is responsible for determining which activities are applicable to and should be adopted with respect to a particular grant. That said, some controls, consistent with other reasonable business practices and other sections of SAAM, are always necessary and cannot be avoided when dealing with the disbursement of public monies.

This SAAM section is a reference guide for agency management that can be used to understand and evaluate some of the internal controls related to grants that should be considered.

The GAO is available to discuss any of these or other internal control activities with grantees and pass-through grantors.

POLICIES

1. A pass-through entity must have written policies and procedures on how subawards will be made and subrecipients managed.

State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 2 of 8

1.1. These policies and procedures must comply with the provisions and requirements of:

1.1.1. The Code of Federal Regulations.

1.1.2. The State of Arizona's *Grants Management Manual* (GMM).

1.1.3. The *State of Arizona Accounting Manual* (SAAM).

1.1.4. Any requirements established by the grant agreement or the cognizant Federal agency.

1.2. These policies and procedures must address:

1.2.1. The process for approving applications.

1.2.2. The process for approving applicants, which includes:

1.2.2.1. Investigating an applicant's rating with Dunn & Bradstreet or other credit bureau.

1.2.2.2. Checking an applicant's evaluation with the Better Business Bureau.

1.2.2.3. Requiring an applicant, which is not another State agency or unit of government, to provide audited or reviewed financial statements and evaluating these statements to determine the applicant's financial ability to discharge its duties as subrecipient.

1.2.3. How award determinations are to be made.

1.2.4. How subgrantees are to be monitored.

1.2.5. The pass-through entity's processes for:

1.2.5.1. Pre-award.

1.2.5.2. Post-award.

1.2.5.3. Close-out.

1.2.5.4. Ensuring subrecipients use grant funds in accordance with all Federal, State and program guidelines.

1.2.5.5. Overseeing the day-to-day operations of subrecipients to ensure they achieve performance objectives on schedule and within budget.

State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 3 of 8

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- 1.2.5.6. Confirming subrecipients' timely submission of all documents necessary to meet all the reporting requirements of the awarding agency.
 - 1.2.5.7. Outlining the actions to be taken, if problems arise, to get a subrecipient back on track in terms of compliance and performance.
 2. A pass-through entity's responsibilities related to pre-award processes include, but may not be limited to:
 - 2.1. Ensuring decision makers with respect to authorizing awards have no conflicts of interest involving known awards.
 - 2.2. Taking those steps necessary to avoid duplication or overlapping of efforts among subawards.
 - 2.3. Deciding upon the appropriate type of vehicle for the services needed (i.e., subaward, contract, etc.).
 - 2.3.1. It is to be noted that the substance of the agreement takes precedence over its form.
 - 2.3.2. The ways of distinguishing subrecipients from contractors are addressed in SAAM 7010.
 - 2.4. Having a method for announcing the specific funding opportunities, eligibility requirements, and the allotted timeframe for potential subrecipients to apply.
 - 2.5. Establishing and following a process for reviewing each subrecipient's eligibility for Federal funding, including the criteria to be used to evaluate each application.
 - 2.5.1. Competitive bidding should be used whenever possible and practical to do so.
 - 2.5.2. Reasonableness of proposed charges should always be evaluated. The charges to be evaluated include items such as:
 - 2.5.2.1. The rates a consultant or contractor charges (How do they compare with local market rates?).
 - 2.5.2.2. Travel costs (Coach or first class airfare? Lodging and meals within State allowances?).
 - 2.6. Checking for Federal suspension or debarment and reviewing with SPO any negative vendor performance reports.
 - 2.7. Evaluating the risks posed by applicants before an award is made. The evaluation elements must be described in the solicitation. This pre-award risk assessment should consider such elements as the:

State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 4 of 8

- 2.7.1. Applicant's eligibility.
- 2.7.2. Quality (completeness, responsiveness, etc.) of the application itself.
- 2.7.3. Applicant's financial stability and capacity to perform the necessary work.
- 2.7.4. Applicant's organizational capacity to successfully complete the needed work.
- 2.7.5. Experience of the applicant's management.
- 2.7.6. Applicant's performance history.
- 2.7.7. Audit findings.
- 2.8. The results of the pre-award risk assessment can assist the pass-through entity in determining whether additional terms and conditions should be imposed on the award.
- 2.9. The subrecipient agreement must include specific data elements such as the Federal Award Identification, etc. A complete list of these data elements can be found in 2 CFR 200.331(a).
- 3. A pass-through entity's responsibilities related to post-award processes include, but may not be limited to:
 - 3.1. Maintaining adequate documentation of subaward or procurement contract status determination.
 - 3.2. Conducting appropriate post-award risk assessments focusing on, among other factors:
 - 3.2.1. Failure to comply with:
 - 3.2.1.1. Applicable Federal requirements.
 - 3.2.1.2. The terms and conditions of the award or contract.
 - 3.2.2. The level of monitoring needed under the circumstances.
 - 3.2.3. Timeliness, completeness and accuracy of reports.
 - 3.2.4. Match-up between awards made, subrecipient spending, and subrecipient or contractor progress.
 - 3.3. The attributes used by the pass-through entity to evaluate the overall risk related to subrecipients should be customized to suit the specific program.

State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 5 of 8

- 3.4. There are a number of different attributes to consider when assessing risk. The final score, however, should clearly identify the risk level as high, medium or low.
- 3.5. A pass-through entity should develop criteria to determine risk levels and the reason for assigning each subrecipient into risk categories.
- 3.6. The overall level of risk associated with a subrecipient should dictate the frequency and depth of the monitoring practices to include ways to mitigate risk.
- 3.7. Examples of risk criteria that may be applied include, but are not limited to:
 - 3.7.1. The amount of the award.
 - 3.7.2. Past experience with the recipient or the program.
 - 3.7.3. Timeliness, quantity and quality of progress, other performance measures, and financial results.
 - 3.7.3.1. There should be agreement between and among various reports and activities; lack of such agreement may be an indicator that something is wrong.
 - 3.7.4. Whether the subrecipient is new to the grantor or new to the type of program under consideration. A newcomer to the grantor or the program under consideration may require more oversight, guidance and assistance, which the grantor may not be prepared to provide.
 - 3.7.5. The date of last monitoring.
 - 3.7.6. Excessive cash requirements or draw-down patterns.
 - 3.7.6.1. The cash advanced to the subrecipient must make sense when evaluated in light of the subrecipient's progress and/or performance.
 - 3.7.7. The Single Audit opinion.
- 3.8. The pass-through entity's post-award subrecipient monitoring process should include:
 - 3.8.1. The subrecipients to be monitored.
 - 3.8.2. The monitoring schedule. The monitoring schedule should be based upon risk. The higher the risk, the earlier a subrecipient should be monitored.
 - 3.8.3. The depth and breadth of monitoring activities. The higher the risk, the more extensively a subrecipient should be monitored.

State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 6 of 8

- 3.8.4. The place where monitoring is to take place.
 - 3.8.4.1. In-house monitoring, such as desk reviews of progress, performance and accounting reports, may determine the need for on-site monitoring, auditing, training, investigation, etc.
 - 3.8.5. The effective implementation of a pass-through entity's monitoring plan may also result in the identification of potential areas for training and technical assistance.
- 3.9. Pass-through entities should develop monitoring objectives to ensure that subrecipients:
 - 3.9.1. Carry out program activities as stipulated in the agreement.
 - 3.9.2. Have adequate internal controls to protect Federal funds.
 - 3.9.3. Claim reimbursement for costs that are allowable, reasonable, allocable, and necessary under program guidelines.
 - 3.9.4. Identify any conflicts of interest that exist.
 - 3.9.5. Maintain required supporting documentation and records.
- 3.10. In preparation for an on-site visit, the pass-through entity should review all documentation, such as:
 - 3.10.1. The subrecipient's application for funding.
 - 3.10.2. The written agreement with the subrecipient.
 - 3.10.3. The financial and progress reports submitted by the subrecipient.
 - 3.10.4. The recipient's drawdown history.
 - 3.10.5. Copies of the subrecipient's recent audit reports.
- 3.11. The result of an on-site review may inform the pass-through entity about the subrecipient's operations and identify potential problem areas to be examined during the on-site visit.
- 3.12. There are seven (7) steps to a monitoring site visit:
 - 3.12.1. The notification to the subrecipient of the pass-through entity's intention to conduct and on-site visit.
 - 3.12.2. The entrance conference. This enables the subrecipient and the pass-through entity to come to a common understanding of the purpose and scope of the visit,

State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 7 of 8

as well as the various activities and procedures that pass-through entity may conduct during the visit.

- 3.12.3. The collection of supporting documentation and other data gathering, as well as the evaluation and analysis of the documentation and data acquired.
- 3.12.4. The exit conference. This affords the opportunity for the pass-through entity and the subrecipient to discuss the results of the on-site visit and to reach an agreement as to what corrective actions the subrecipient should take, if any, or follow-up activities the pass-through entity will perform, if deemed necessary.
- 3.12.5. The corrective action plan, if applicable. Not infrequently, the on-site visit reveals certain deficiencies on the part of the subrecipient. This results in the development of a corrective action plan, generally developed cooperatively between the pass-through entity and the subrecipient, to minimize, mitigate or eliminate the noted deficiency. The corrective action plan, while principally requiring actions by the subrecipient, may also involve activities, such as the provision of training, to be conducted by the pass-through entity.
- 3.12.6. Follow-up actions and activities. This involves the accomplishment of any additional actions to be taken by the subrecipient or activities to be performed by the pass-through entity as were detailed in the corrective action plan. This may involve an additional on-site visit by the pass-through entity with the subrecipient to determine the latter's compliance with the corrective action plan.
- 3.12.7. Closure of site visit. When all of follow-up actions and activities have been concluded, the results and recommendations should be documented. This might include recommendations as to whether the subrecipient should continue to receive Federal funds or should be awarded Federal funds in the future. It can also contain a post-mortem on the on-site visit, including lessons learned and suggestions for process improvements.
- 3.13. When monitoring subrecipients, a pass-through entity should:
 - 3.13.1. Confirm that the subrecipient's financial systems meet the guidance provided in 2 CFR 200.302.
 - 3.13.2. Assure that a subrecipient provides accurate, current and complete disclosure of the financial results related to each Federal award. This assurance would be based upon the following:
 - 3.13.2.1. The subrecipient's records must identify the source and application of all Federal funds by award; these records must be supported by adequate documentation.

State of Arizona Accounting Manual

Topic 70 Grants
Section 25 Internal Control Activities for
Pass-through Grantors

Issued 88/88/88
Page 8 of 8

- 3.13.2.2. It must be determinable and determined that the subrecipient is adequately safeguarding monetary and non-monetary assets provided to it by the pass-through entity.
- 3.13.2.3. Comparisons of expenditures to approved budget amounts must be provided to the pass-through entity by the subrecipient. The pass-through entity must take those steps necessary to determine the accuracy of these comparisons.
- 3.13.2.4. A written procedure must be developed by the pass-through entity for determining the propriety of costs and payment requests under 2 CFR 200.305.
- 3.13.2.5. The segregation of grant proceeds from other monies in the possession of the pass-through entity and the subrecipient should be strictly enforced. This may be done by fund accounting, sub-accounts or any other appropriate and effective means.
4. The post-award process may include the development and enforcement of remedies by the pass-through entity to counteract subrecipient noncompliance.
- 4.1. If a subrecipient does not comply with Federal statutes or regulations or the terms and conditions of the subaward, the pass-through entity can impose additional conditions upon the subrecipient. These might involve the subrecipient's having to report more frequently, or to submit to additional on-site visits, or to provide more training to its staff.
- 4.2. If noncompliance cannot be remedied by imposing additional conditions, the pass-through entity can take one or more of the following actions:
- 4.2.1. Temporarily withholding funds pending correction of the deficiency.
- 4.2.2. Disallowing all or part of the activity that is not in compliance.
- 4.2.3. Wholly or partially suspending or terminating the subaward.
- 4.2.4. Initiating suspension of the subrecipient.
- 4.2.5. Withholding future subawards.
- 4.2.6. Asking for the return of money.
- 4.2.7. Involving legal counsel.