Appendix 4
Transparency and Accountability:
A Governmental Primer on Grant Accountability
(Excerpt from SAO ARRA Implementation Guidance)

Transparency and Accountability

(from SAO ARRA Implementation Guidance)

Overview

The American Recovery and Reinvestment Act (ARRA) enacted on February 17, 2009 came with unprecedented levels of accountability, transparency and reporting requirements.

ARRA Accountability Objectives

- Funds are both awarded and distributed in a prompt, fair and reasonable manner.
- Agencies clearly and accurately report the recipients and uses of all funds in a timely manner. This reporting will allow the use and benefit of the funds to be transparent to the general public.
- Funds are used solely for authorized purposes and any instances of fraud, waste, abuse or error are properly mitigated.
- Any projects funded under the ARRA avoid both delays and cost overruns.
- Program goals are achieved, including specific program outcomes and improved economic conditions.

Federal Government's Role to Ensure Accountability

The Federal Government will focus on the following:

- Internal Controls
- Reporting Accuracy
- Anti-Fraud program and processes

The Federal Government will perform Data Quality Reviews on Section 1512 Reporting and focus on 2 key areas:

- Material Omissions
- Significant Reporting Errors

Material Omissions

Those instances where required data is not reported or reported information is not otherwise responsive to the data request and such reporting gaps result insignificant risk that the public will be misled or confused by the recipient report in general. In general, material omissions should be minimized by the www.FederalReporting.gov solution, which will require fields to be completed for successful transmission, as well as include edits and cross-edits to ensure data validity. However, a material omission may still occur to the extent submitted data is not responsive to a specific data request. For example, a recipient required to report a description of a purchase made from a vendor may not provide sufficient detail in the description for the reader to derive the nature of the purchase.

Significant Reporting Errors

Those instances where required data is not reported accurately and such erroneous reporting results in significant risk that the public will be misled or confused by the recipient report in question. An example of this would be a recipient, or sub-recipient who reports expenditures in excess of the amount awarded by the Federal funding agency, excluding funding resulting from match requirements.

Internal Controls

All agencies and institutions receiving ARRA funds, need to develop an internal control framework that addresses the accountability objectives of the Act. Recipients should establish internal controls to ensure data quality, completeness, accuracy and timely reporting of all amounts funded by the Recovery Act. Recipients reporting Section 1512 reporting data must initiate a review of the data both prior to and following the formal submission of data. The internal control framework should ensure that the following elements are represented:

- Data integrity
- Source documentation
- Audit Trails

Data Integrity

Each agency and institution receiving ARRA funds must establish a system that provides reasonable assurance that required data elements for Section 1512 reporting are recorded in an accurate and timely manner. Each agency must ensure that all data are recorded correctly.

Correct transactions must:

- Reflect the actual values involved
- Define report data elements consistently
- Contain sufficient detail for proper identification and classification
- Be posted in a timely manner in the proper period
- Be stored securely
- Be readily retrievable for inquiry or reporting, and

- Be safeguarded against improper alteration

Source Documentation

Source documents are important because they establish the authenticity and provide evidence to support transactions. The evidence must be valid, reliable, accurate and complete. Evidence in the form of documents and written representation is more reliable than oral representations. Documentary evidence is the most common form of evidence and may come in many forms including:

- Award letters
- Contracts
- Invoices
- Written policies and procedures
- Management Reports
- Internal Audit Reports
- Accounting records
- Databases maintained by the entity

Audit Trails

The purpose of the audit trail is to allow verification of a transaction by tracing it from the source documentation to the final report. Agencies and institutions receiving ARRA funds should perform walkthroughs of their ARRA transactions. A walkthrough is simply the act of tracing a transaction through organization records and procedures to understand how the information is flowing through the organization. In a walkthrough the agency traces a transaction from the origin or source document through the information system(s) until it is reflected in a report.

The advantages of performing walkthroughs include:

- A determination of whether controls have been designed effectively and actually placed in operation.
- An identification of points in organizational processes where material omissions or significant reporting errors might occur.

The primary objective when performing a walkthrough is to develop an understanding of how transactions are initiated, authorized, recorded, processed, and ultimately reported.

To get started in developing your internal control framework consider the following:

- Document your processes by first identifying all the steps necessary in gathering all of the required data for Section 1512 reporting.

- Identify and list all source documents where the data is coming from to include documents, systems, and business process owners.
- Trace transactions from the source documents to the report.
- Create checklists that list all data requirements, due dates, business process owners, and source documents.
- Perform data quality reviews for material omissions and/or significant reporting errors and work with sub-recipients to address any data quality issues.
- Establish control totals for reasonableness and verifying that reported information matches the established control totals.
- Establish a data review protocol or automated process that identifies irregular or abnormal results.

The General Accounting Office has recommended that some of the following controls be considered:

- Validating data used in decision making against other government or third party sources
- Whenever possible inspecting information to confirm its validity prior to payment
- Conducting system edit checks to identify problems before payments are made; and
- Train staff on fraud awareness

Anti-Fraud Program and Processes

(from SAO ARRA Implementation Guidance)

The Recovery Act requires the state to ensure funds are used for authorized purposes and to mitigate instances of fraud, waste, and abuse.

- Fraud is the intentional misrepresentation of facts with the intention of achieving personal gain.
- Waste is considered unnecessary spending or careless squandering of resources whether intentional or unintentional. Example: spending state or federal funds to purchase items that have no business purpose.
- Abuse is the intentional destruction, diversion, manipulation, misappropriation, or misuse of State or Federal resources. Example: use of a state vehicle for personal use.

Fraud

A. Fraud is defined as an intentional deception, misappropriation of resources or the manipulation of data. It usually involves the deliberate concealment of facts. Fraud can range from minor employee theft and unproductive behavior to misappropriation of assets and fraudulent financial reporting.

B. Some examples of fraud include:

- Altering documents (changing an actual document with the intention of deceiving) including cash receipts, checks, expense reports, and time sheets
- Falsifying documents (creating a fictitious document) including cash receipts, checks, expense reports, and time sheets
- Forging signatures on documents including cash receipts, checks, expense reports, and time sheets
- Bribery
- Collusion between two or more parties for fraud or deceit
- Failure to account for monies collected
- Theft of inventory items or theft of scrap or surplus items
- Misappropriation or misuse of assets, including cash, equipment, property, and supplies
- Payroll- creating fictitious employees, inflating hours worked, theft of time, and keeping former employees on the payroll.
- Purchasing- bid rigging, kickbacks, purchase of inferior products, purchase of personal items
- Theft of assets, including cash, equipment, property, and supplies

C. Reporting of Fraud or Corruption

- Allegations and concerns about fraudulent or corrupt activity may come from various sources including;

  Employees
  Vendors
  Customers
  Results of internal or external audit reviews
  Any other interested parties

- All employees have a duty to report concerns they have or information provided to them about the possible fraudulent or corrupt activity of any manager, employee, vendor or any other party with any association with the state agency.

D. Management Antifraud Programs and Controls

1. Create and maintain a culture of honesty and high ethics
   - It is the organization's responsibility to create a culture of honesty and high ethics and to clearly communicate acceptable behavior and expectations of each employee.
   - Such a culture is rooted in a strong set of core values that provides the foundation for employees as to how the organization conducts its business.

- It also allows an entity an ethical framework that covers (1) fraudulent financial reporting, (2) misappropriation of assets, and (3) corruption as well as other issues
- Creating a culture of honesty and ethics should include the following:
  - Setting the tone at the top: Directors, managers, and supervisors set the “tone at the top” for ethical behavior within any organization.
  - Creating a positive workplace environment: Wrongdoing occurs less frequently when employees have positive feelings about an entity than when they feel abused, threatened, or ignored. Without a positive workplace environment, there are more opportunities for poor employee morale, which can affect an employee’s attitude about committing fraud
  - Hiring and promoting appropriate employees
  - Training
  - Discipline

2. Antifraud Processes and Controls
   - Identifying and Measuring Fraud Risks: Management has primary responsibility for establishing and monitoring all aspects of the agency’s fraud-risk assessment and prevention activities. The fraud risk assessment process should consider agency vulnerabilities and its exposure to material losses, taking into account the agency’s size and complexity of its operations
   - Mitigating Fraud Risk: Management should conduct an internal risk assessment to identify and prioritize the different types of fraud risks and apply appropriate fraud mitigation strategies.
   - Implementing and Monitoring Appropriate Internal Controls: Most risks can be mitigated with an appropriate set of internal controls. Once a fraud risk assessment has been performed, the agency must identify the ongoing processes, controls, and other monitoring procedures that are needed to identify and/or mitigate those risks

3. Appropriate Oversight Process
   - Management: Fraud prevention and detection requires commitment from both management and the decision makers of the agency. Ideally, managers must be assigned direct responsibility to develop, implement, and maintain effective fraud prevention measures within their area of expertise
   - Internal Audits: The Internal Audit department can provide expertise, knowledge, experience, and objective, independent, input into the agency’s fraud risk assessment process. They can assist in developing prevention and mitigation measures and in the resolution of allegations or suspicions of fraud.