



Office of Inspector General

Audit Report

Report of Audit on the Center for Chesapeake Communities

E6DEP8-03-0014-9100117

March 31, 1999

Inspector General Division
Conducting the Audit:

Mid-Atlantic Audit Division
Philadelphia, PA

Region Covered:

Region 3

Program Office Involved:

Chesapeake Bay Program Office



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March 31, 1999

MEMORANDUM

SUBJECT: Final Audit Report on the Center
for Chesapeake Communities
Report Number E6DEF8-03-0014-9100117

FROM: *Carl A. Jannetti*
Carl A. Jannetti
Divisional Inspector General for Audit (3AI00)

TO: W. Michael McCabe
Regional Administrator (3RA00)

Attached is our final audit report on the Center for Chesapeake Communities (CCC). It contains findings concerning the formation of the CCC, and issues related to the cooperative agreement EPA awarded to this nonprofit. This report also discusses the method used to award contracts to obtain Local Government Advisory Committee (LGAC) support services, and the CCC's procurement and financial procedures.

ACTION REQUIRED

In accordance with EPA Order 2750, you as the action official are required to provide this office a written response to the audit report within 90 days of the final audit report date. For corrective actions planned but not completed by the response date, reference to specific milestone dates will assist in deciding whether to close this audit. Your response should address all recommendations, and include milestone dates for corrective actions.

This audit report contains findings that describe problems the Office of Inspector General (OIG) has identified and corrective actions the OIG recommends. This report represents the opinion of the OIG. Final determinations on matters in this report will be made by EPA managers in accordance with established EPA audit resolution procedures. We have no objection to further release of this report to the public. Should your staff have any questions, please contact me or Lisa White at 215-814-5800.

Attachment

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EXECUTIVE SUMMARY

Purpose

The purpose of this audit was to evaluate the activities surrounding the formation of the Center for Chesapeake Communities (CCC). Our objectives included a review of: EPA's award and administration of the cooperative agreement to the CCC, the method used to obtain LGAC support services, and the CCC's procurement and financial procedures. Our objectives also focused on determining the validity of concerns raised by LGAC.

Results-in-Brief

EPA awarded a noncompetitive cooperative agreement to the CCC without adequate justification. Awarding the cooperative agreement noncompetitively, without adequate justification, created an appearance of preferential treatment that compromises the integrity of the Chesapeake Bay Program.

Moreover, EPA awarded cooperative agreements to intermediaries which in turn awarded contracts to provide LGAC support services. To obtain these support services, the intermediaries awarded contracts to Redman/Johnston Associates. EPA officials explained that by awarding cooperative agreements to obtain the services of an LGAC support contractor, it was able to avoid Federal procurement regulations, making the procurement for support services easier. However, while easing the process for awarding the support contracts, EPA did not comply with the intent of Public Law 95-224 entitled the Federal Grant and Cooperative Agreement Act of 1977, 31 U.S.C. 6301 et seq.

As a nonprofit recipient of EPA funds, the CCC's conduct is governed by 40 CFR Part 30. This regulation addresses a recipient's ethical responsibilities. Among such responsibilities is the requirement to avoid a contract award that would raise a real or apparent conflict of interest on the part of the award official. In the case of the CCC, the Executive Director acted favorably toward Redman/Johnston Associates by awarding it two contracts after

Redman/Johnston Associates absorbed costs totaling approximately \$2,300 for incorporating the CCC. This action compromised the integrity of the CCC's contract award process and violated EPA's regulations.

We also found that neither the CCC nor Redman/Johnston Associates had financial management systems in place to properly account for Federal funds. As a result, the abilities of these organizations to record, process, summarize and report financial data were adversely affected.

Recommendations We recommend that the Region III Administrator:

- 1) Terminate the existing cooperative agreement awarded to the CCC. Once terminated, if Region III continues to believe the services are needed, attempts should be made to award a new cooperative agreement competitively. If advertisements and requests for proposals do not identify entities able to perform the services required, then Region III can award the cooperative agreement noncompetitively. This award should only be made after Region III has ensured that an adequate justification has been provided.
- 2) Obtain LGAC support services directly, without using an intermediary.
- 3) Discontinue all payments to the CCC and review all costs already incurred under the cooperative agreements for allowability and reasonableness. To that end, labor amounts billed by Redman/Johnston Associates not supported by adequate timesheets should be disallowed.
- 4) Prior to awarding assistance agreements and before allowing advance payments, ensure that recipients have developed and implemented adequate internal controls and financial management systems that comply with Office of Management and Budget (OMB) and EPA regulations.

- 5) Contact our office prior to closeout of the cooperative agreement awarded to the CCC to afford us the option of performing a final audit.

Region III Response

The Region concurs with virtually all the recommendations outlined in the draft report, and in a number of instances has already taken actions which have the effect of carrying out the recommendations in whole or in part. This includes: a site review and evaluation of the CCC's financial management and records systems; development of a management plan for competing nonprofit grants in the Chesapeake Bay Program Office; issuance of the first Request for Proposals under the new competitive procedures outlined in the management plan; and initiation of a vulnerability assessment for all Chesapeake Bay Program grants. Other actions will be taken in full response to the recommendations made in the final report.

OIG Evaluation

EPA's response meets the intent of our recommendations, however, Region III deferred responding to the recommendation in Chapter 4. We expect that the Region's response to the final audit report will address all of our recommendations.

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ACRONYMS

CCC/or Center	Center for Chesapeake Communities
CBPO	Chesapeake Bay Program Office
CFR	Code of Federal Regulations
COG	Metropolitan Washington Council of Governments
EPA	Environmental Protection Agency
LGAC	Local Government Advisory Committee
NWI	National Wilderness Institute
OIG	Office of Inspector General
OMB	Office of Management and Budget
RFP	Request for Proposal
RFQ	Request for Qualifications
SRO	Senior Resource Official

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CHAPTER 1

INTRODUCTION

Purpose

The purpose of this audit was to evaluate the activities surrounding the formation of the Center for Chesapeake Communities (CCC). Our objectives included a review of: EPA's award and administration of the cooperative agreement to the CCC, the method used to obtain LGAC support services, and the CCC's procurement and financial procedures. On December 15, 1997, the Office of Inspector General (OIG) received a letter from the Chair of the Chesapeake Bay Local Government Advisory Committee (LGAC). This letter requested that the OIG evaluate issues raised by LGAC members regarding the CCC¹. Our objectives also focused on determining the validity of LGAC's concerns regarding:

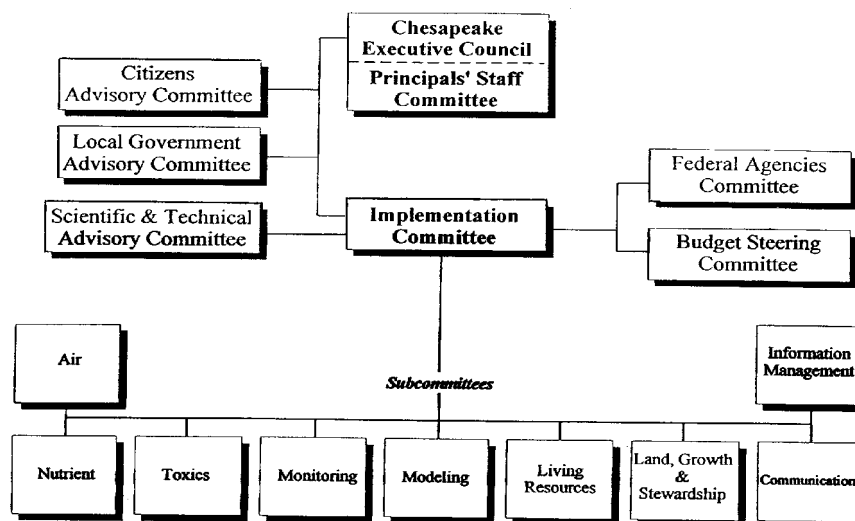
- ◆ The relationship between the CCC and the LGAC. Specifically, several members of the LGAC also served on the Board of the CCC leading to perceptions of conflict of interest.
- ◆ The possible conflict of interest by the Executive Director of the CCC because he was a member of the LGAC and Chair of the LGAC's nonprofit study workgroup.
- ◆ The process by which the LGAC nonprofit workgroup performed its feasibility study.
- ◆ The actions of Redman/Johnston Associates (the contractor used to provide staff support to the LGAC) to pay the filing fees and other costs associated with the incorporation of the CCC.

1. On May 12, 1998, the OIG also received a request from the Landmark Legal Foundation, on behalf of itself and the National Wilderness Institute (NWI) formally requesting our review into the incorporation of the CCC. The NWI also placed a report on the Internet discussing some of the issues addressed in this report.

Background

The Chesapeake Bay Program is the unique regional partnership which has been directing and conducting the restoration of the Chesapeake Bay since the signing of the 1983 Chesapeake Bay Agreement. The Chesapeake Bay Program partners include the States of Maryland, Pennsylvania, and Virginia; the District of Columbia; the Chesapeake Bay Commission; EPA; and participating advisory groups.

The EPA Region III Chesapeake Bay Program Office (CBPO) in Annapolis, MD coordinates the cleanup initiatives of the Chesapeake Bay. It provides administrative and technical support to the network of regional committees, subcommittees and workgroups that participate in the Chesapeake Bay Program under the overall direction of the Chesapeake Executive Council.



The Chesapeake Executive Council membership includes the EPA Administrator; the Governors of Virginia, Maryland and Pennsylvania; the Mayor of the District of Columbia; and the Chair of the Chesapeake Bay Commission. The Council establishes policy direction for the restoration and protection of the Chesapeake Bay and its living resources.

The Principals' Staff Committee acts as the policy advisors to the Executive Council, accepting items for Council consideration and approval. Membership includes the EPA Region III Administrator, EPA's Director of the Chesapeake Bay Program, the Executive Director of the Chesapeake Bay Commission, and various state Department Secretaries and Directors. The Implementation Committee is responsible for the annual workplan, budget, technical and computer support, and public outreach.

Establishing the LGAC in March 1988 fulfilled a commitment in the Chesapeake Bay Agreement. LGAC is composed of local government representatives from the States of Maryland, Virginia and Pennsylvania, as well as the District of Columbia. Each of the states may appoint up to six members to serve on LGAC. The District of Columbia may appoint three. All members serve without compensation. This committee is charged with developing and implementing a strategy for local government participation in the Chesapeake Bay Program. The committee gives advice on matters relating to local governments to the Chesapeake Executive Council, the Principals' Staff Committee and the Implementation Committee. To accomplish this task, LGAC holds quarterly meetings to discuss current Chesapeake Bay Program policy. In addition to its policy role, the LGAC provides information and technical assistance to local governments throughout the Chesapeake Bay watershed.

In recognition of the vital role local governments play in the Chesapeake Bay restoration effort, the Chesapeake Executive Council adopted the Local Government Partnership Initiative in 1995. This Initiative was a commitment to strengthen the Chesapeake Bay Program's partnership with local governments. To ensure that the objectives of the Initiative were achieved, LGAC formed a task force to develop a Local Government Participation Action Plan. The goal of this Action Plan was to establish a strategy to broaden the participation of local governments in the Chesapeake Bay Program.

The Local Government Participation Action Plan was endorsed by the chief executives of the Chesapeake Bay Program in October 1996, and contained a commitment to improve and establish technical and financial assistance programs to local governments. These programs were intended to enhance local governments' capacity to implement Chesapeake Bay restoration and protection measures. One of the many tasks under this commitment was to investigate the feasibility of establishing a nonprofit entity to further assist local governments in implementing Chesapeake Bay protection and restoration activities. As a result, the LGAC formed a workgroup to examine the feasibility of establishing a nonprofit entity. Prior to the completion of this study, the Center for Chesapeake Communities (CCC), a nonprofit organization, was incorporated on August 5, 1997. The LGAC Vice Chair became the Executive Director of the nonprofit.

As a result of the workgroup's efforts, a draft feasibility report was prepared in September 1997. This report concluded that:

Although government groups provide services to local governments, and nonprofit organizations work with local government constituents, there is currently not a nonprofit organization that serves as a regional resource organization in the watershed with a local government focus.

Soon after the CCC was incorporated, EPA awarded it a noncompetitive cooperative agreement on September 30, 1997. This agreement was amended twice. The first amendment was for a time extension. The second amendment, dated March 2, 1998, increased funding and extended the project and budget periods. Details of the cooperative agreement and amendments follow.

<i>Assistance Number</i>	<i>EPA Amount</i>	<i>Project Period</i>	<i>Budget Period</i>
CB993675-01-0	\$45,000	9/8/97-12/31/97	9/8/97-12/31/97
CB993675-01-1	-0-	9/8/97-3/31/98	9/8/97-3/31/98
CB993675-01-2	\$314,370	9/8/97-12/31/03	9/8/97-3/15/99

The purpose of the initial cooperative agreement was to support start-up of the CCC, prepare a local government training module, and plan a local government summit. The second amendment included funding for the CCC to:

- ❑ Conduct activities that will enhance its ability to provide technical assistance, as well as seek financial assistance opportunities for local governments interested in Chesapeake Bay restoration and protection activities.
- ❑ Complete various projects including enhancing efforts to implement the tributary nutrient reduction strategies, broadening the engagement of local governments, and supporting toxic reduction pollution prevention goals.
- ❑ Provide staff support for the LGAC.

Almost one-half of the cooperative agreement funds provided to the CCC were used for a contract award to obtain LGAC support. LGAC support includes items such as: coordination and scheduling of meetings, interaction with local governments through press releases, managing the Chesapeake Bay Program Local Government homepage, planning and holding media events, and providing technical support to local governments. For the past five years, Redman/Johnston Associates has been awarded this contract.

Scope and Methodology

Our audit was performed in accordance with the *Government Auditing Standards* (1994 Revision) issued by the Comptroller General of the United States, except that we did not follow all of the elements of the planning standards in Chapter 6. Since this review was initiated as a result of a letter sent from the Chair of the LGAC, our work focused on determining the validity of the issues raised in his letter. The audit included tests of the program records and other auditing procedures we considered necessary.

To accomplish our objectives, we performed our review at EPA Region III's Chesapeake Bay Program Office in

Philadelphia. We also conducted work at the CCC's and Redman/Johnston's offices. We interviewed the Executive Director of the CCC, the President of Redman/Johnston Associates, and some of the LGAC members.

Our review in Region III included interviews and meetings with the Project Officer, the Grants Specialist and the Deputy Director of the Chesapeake Bay Program Office. We reviewed the program and grant files for the cooperative agreement awarded to the CCC. We also reviewed the grant file for the cooperative agreement awarded to the Metropolitan Washington Council of Governments (COG) because it previously awarded contracts to Redman/Johnston Associates to provide support to the LGAC.

Our review at the CCC included files pertaining to cooperative agreement number CB993675-01 awarded by EPA. We did not include the Small Watershed Grant and the Sustainable Development Challenge Grant in the scope of our review. At the time of our fieldwork, these assistance agreements had not been awarded. We reviewed the procedures the CCC used to award the contracts to Redman/Johnston Associates, and any internal controls affecting our review that the CCC had in place at the time of our audit. We performed a detailed review of the CCC's check register, canceled checks, invoices, receipts, and bank statements.

During our visit to Redman/Johnston Associates office, we reviewed invoices submitted to both the COG and the CCC along with canceled checks, a transaction report from January 1997 through April 1998, documentation supporting the incorporation of the CCC, the proposal to the CCC for the contract award and various documents pertaining to LGAC support work.

We reviewed Title 40 of the Code of Federal Regulations Part 30, *Grants and Agreements with Institutions of Higher Education, Hospitals and Other Nonprofit Organizations*. We also reviewed Public Law 95-224, the Federal Grant and Cooperative Agreement Act of 1977, U.S.C. 6301 et seq., EPA Order 5700.1 titled Policy for Distinguishing Between

Assistance and Acquisition, OMB Circulars A-110 and A-122, the Grants Management Fact Sheet for Agency Leaders, titled, *Competition for Assistance Agreements*, and Executive Order 12674, *Principles of Ethical Conduct for Government Officers and Employees*.

We did not review EPA's oversight procedures for the administration of the cooperative agreement awarded to the COG. Moreover, we did not review the COG's costs or conduct a site visit at the COG. However, we did request various documents from the COG and interviewed some of its personnel.

We reviewed the CBPO's annual assurance letter for fiscal year 1998 prepared as a result of the Federal Managers' Financial Integrity Act. There were no weaknesses identified that pertained to the scope of work we reviewed. However, the letter indicates that this review was requested and that the findings would be used to strengthen the CBPO's management controls.

Our review began on January 9, 1998 and ended on September 18, 1998. To obtain a preliminary response to the issues in this report, we issued position papers to the Director of the Chesapeake Bay Program Office on November 5, 1998. We received verbal comments from him on November 10, 1998, and written comments from the Deputy Director on November 12, 1998.

We issued a draft report on November 20, 1998 to the Region III Administrator. In order to obtain comments from the CCC, we provided them Chapter 4, the applicable portion of Chapter 5, and Exhibits A and C. We also provided Redman/Johnston Associates Exhibit B and the portion of Chapter 5 applicable to the contractor in order to obtain their comments. Subsequently, the CCC Executive Director asked if he could provide Redman/Johnston Associates Chapter 4 so that they both could respond. We granted that request. The CCC provided comments on January 21, 1999, and Redman/Johnston Associates provided comments on December 24, 1998 and January 4, 1999. Several meetings were conducted with Region III officials to discuss the issues

in the report. EPA Region III provided their written response on March 10, 1999. After evaluating these responses, our position remains unchanged on the issues discussed in this report.

Exit conferences were held on March 17, 1999 with the CCC Executive Director, on March 24, 1999 with the Director of the CBPO and on March 26, 1999 with the Deputy Director of the CBPO. We also conducted an exit conference with the contractor on March 26, 1999. During that exit conference the contractor qualified his responses to the audit report because he was not given the opportunity to comment on Chapters 2 and 3. In our opinion, the contractor had the opportunity to comment on all of the major points in the report. All of the responses are summarized at the end of each chapter and provided in their entirety as Appendices.

Prior Audit Coverage

There has been no prior audit coverage of the nonprofit organization that is discussed in this report.

CHAPTER 2

EPA NEEDS TO ADEQUATELY JUSTIFY NONCOMPETITIVE COOPERATIVE AGREEMENT

EPA officials are responsible for ensuring that there is adequate justification for assistance agreements awarded noncompetitively. Competition is essential to ensure that the government obtains the most qualified organizations at the best price. EPA received no such assurances when it awarded a noncompetitive cooperative agreement to the CCC. Moreover, awarding the cooperative agreement noncompetitively, without adequate justification, created an appearance of preferential treatment that compromises the integrity of the Chesapeake Bay Program.

EPA Responsibilities Unfulfilled

On May 31, 1994, the EPA Deputy Assistant Administrator for Administration and Resources Management sent a memorandum to all Senior Resource Officials (SROs) addressing SRO responsibilities. One responsibility he specified was to ensure that there is “adequate justification for assistance agreements awarded noncompetitively” when reviewing assistance funding packages. According to a Grants Management Fact Sheet for Agency Leaders, titled, *Competition for Assistance Agreements*, dated December 1995, Agency managers must develop a solid justification if they do not use competition.

Awarding a noncompetitive cooperative agreement without adequate justification seriously challenges the concept of free and open competition embraced by the Agency. Listed below are some of the effects of awarding a cooperative agreement noncompetitively without adequate justification:

- Gives the appearance EPA may be giving preferential treatment to any single assistance applicant.
- Reduces EPA’s opportunity to receive a wide range of innovative and creative ideas to support its mission by limiting the range of potentially eligible recipients.

- ❑ May fund organizational start-up costs at the expense of performing direct project activities.
- ❑ Is inconsistent with the intent of the Federal Grant and Cooperative Agreement Act of 1977 which encourages competition, where appropriate, in the award of grants and cooperative agreements.

Even a Region III Chesapeake Bay Program document recognized the need for competition. According to a questions and answers document prepared by Region III officials to supplement LGAC's feasibility report,

It would be inappropriate for the Bay Program or any of its subcommittees to directly launch or approve a specific nonprofit organization.

By awarding the CCC a noncompetitive cooperative agreement without adequate justification, Region III officials also did not comply with the intent of Executive Order 12674, *Principles of Ethical Conduct for Government Officers and Employees*. Section 101(h) of the Executive Order states that Government employees shall act impartially and not give preferential treatment to any private organization or individual.

Although in retrospect they now agree that the cooperative agreement awarded to the CCC should have been competitively awarded, Region III officials contend that the level of detail contained in the justification for this assistance agreement was common for Region III assistance agreements, and not unique to this award. They also contend that our conclusion that this award portrays preferential treatment to a single grantee is not appropriate. We disagree with Region III. We believe the events paralleling the award of this cooperative agreement support our conclusion about the appearance of preferential treatment in Region III's handling of this matter. These same events also indicate that a competitive award was needed.

**LGAC Vice Chair
Forms the CCC**

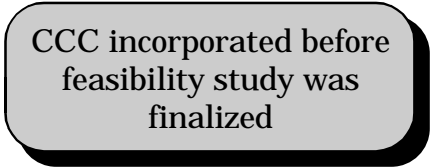
The LGAC headed by a Chair and several Vice Chairs, commissioned a task force to prepare the Local Government

Participation Action Plan. (One of these LGAC Vice Chairs became the task force Chair). The Action Plan that this task force prepared called for broadening local government participation in the Chesapeake Bay Program, and committed to study the feasibility of establishing a nonprofit to assist local governments. LGAC then established a workgroup to perform this feasibility study.

The feasibility study workgroup members included representatives from EPA's Chesapeake Bay Program Office, the COG, and various representatives from other organizations involved with Chesapeake Bay protection efforts. (The Chair of this workgroup was the same person who chaired the task force and later became Executive Director of the CCC.) The workgroup also included the President of Redman/Johnston Associates, acting in his role as Executive Director to the LGAC. According to EPA personnel, this workgroup met often to evaluate the feasibility of establishing a nonprofit.

In effect, one LGAC member was the Chair of the task force that prepared the Action Plan committing to study the feasibility of establishing a nonprofit. This same person was also the Chair of the workgroup that performed this feasibility study. Finally, this same person became the Executive Director of the CCC.

Before the feasibility study was finalized, the CCC was incorporated and awarded a cooperative agreement by EPA to do the work contemplated by the



CCC incorporated before
feasibility study was
finalized

feasibility study. The CCC's Executive Director and the President of Redman/Johnston Associates involvement in the feasibility study, coupled with EPA's decision to award the cooperative agreement to the CCC, caused some LGAC members to request this audit. The following chart provides a timeline that shows the CCC being incorporated before the feasibility study was finalized.

Executive Council adopts the <i>1995 Local Government Partnership Initiative</i> which is a commitment to strengthen the Chesapeake Bay Program's partnership with local governments	
Informal discussions begin concerning the establishment of a nonprofit	<i>August 1996</i>
Executive Council adopts the <i>Local Government Participation Action Plan</i> that committed to broaden participation by local governments in CBP	<i>October 1996</i>
Redman/Johnston Associates discusses incorporating a new nonprofit with an attorney	<i>January 1997</i>
LGAC establishes workgroup to study the feasibility of a nonprofit	<i>February 1997</i>
Redman/Johnston Associates incorporates CCC and LGAC Vice Chair becomes CCC Executive Director	<i>August 1997</i>
EPA sends letter to CCC confirming funding and prepares Program Decision Memorandum justifying award to CCC	<i>September</i>
Draft feasibility study published that indicates nonprofit does not exist with local government focus. Contained draft bylaws, articles, and a budget for an entity named the CCC	<i>September 1997</i>
LGAC publishes progress report to Chesapeake Executive Council LGAC considering workgroup findings but not ready to make recommendation on nonprofit	<i>October 1997</i>

Before LGAC began the feasibility study to determine if a nonprofit was the method of choice for increasing local government participation, a new nonprofit was being planned. Soon after the CCC was incorporated in August 1997, EPA sent the CCC a letter confirming the award of the cooperative agreement and issued the Agency's Program Decision justifying the noncompetitive award to the CCC. This justification stated that:

Establishing this new nonprofit center is one of the commitments of the Chesapeake Bay

Program Local Government Participation Action Plan.
No other organization would have been suitable for
the task.

As previously noted, EPA made this determination before the LGAC finalized its feasibility study indicating there was not currently a nonprofit that provided this service. The fact that the Chair of the workgroup and Redman/Johnston Associates, as participants in that workgroup, had a personal financial interest in the conclusion that no nonprofit existed, raises concern about the workgroup's objectivity and the validity of its conclusion.

EPA personnel told us that the workgroup contacted other organizations, and could not identify an existing organization that fulfilled the mission contemplated by the feasibility study. Region III personnel believed it was important to note that the draft feasibility report indicated that:

Staff contacted local government associations and representatives to inform them of the study and seek their input to the needs analysis ... Representatives of existing regional non-profits served on the workgroup ... and were consulted on the merits of a new organization.

Although the workgroup studied the need for a nonprofit to assist local governments to participate in the Chesapeake Bay Program, neither EPA personnel nor the LGAC's feasibility report documented that the possibility was explored that an existing nonprofit would be able to provide this service. Moreover, because an existing nonprofit did not have a local government focus does not mean such a focus could not have been developed.

In the process of making the award to the CCC, there was no evidence that EPA solicited proposals from the nonprofit community for the type of work contemplated. Without efforts to seek out other nonprofits willing or capable of performing the services EPA wanted, Region III did not fulfill its responsibility to obtain competition. The principal problem we found with EPA's justification for awarding the CCC a cooperative agreement noncompetitively was that

Region III did not independently confirm that no other nonprofits were able to perform the work desired.

Using an existing organization could have avoided the costs of creating a new organization and capitalized on the existing organization's experience. Apparently, duplication of effort was a concern of some LGAC members. This is evidenced by a letter dated September 9, 1997 from the Director of the Virginia Department of Conservation and Recreation to the Chair of the LGAC which stated:

Unfortunately, Virginia was not consulted during the feasibility study and, as it turns out, much of what is planned for the Center is duplicative of the work being done by the Chesapeake Bay Local Assistance Department.

When we discussed this letter with Region III officials, they disagreed with the Director's comments. They asserted that Virginia was represented on the workgroup, and if the Virginia officials had concerns, these concerns were not relayed to the workgroup when the feasibility study was being drafted. Conversely, the Virginia representative contended he was unaware that the CCC was being incorporated at this time.

**Feasibility Study
Inappropriately
Helps the CCC**

When asked what was the basis for awarding a noncompetitive cooperative agreement, the Region III Project Officer replied the feasibility study was the basis for the award. Ultimately, this study indicated:

Feasibility study did not justify noncompetitive award

There is currently not a nonprofit organization that serves as a regional resource organization in the watershed with a local government focus.

In our opinion, the feasibility study does not provide a basis for not competing this cooperative agreement because the workgroup never formally considered the option of using an already existing nonprofit. Rather, the study focused on incorporating a new nonprofit.

The feasibility study resulted in the creation of a mission statement and business plan for the CCC, as well as bylaws, articles of incorporation, and a budget. These items should not have been prepared as part of the feasibility study because the establishment of a nonprofit was not within the scope of work of the feasibility study. The generation of these documents, however, certainly enhanced the CCC's incorporation process. The *Statement of Purpose* section of the feasibility study indicated the study was intended to:

- ❑ Ensure that the mission of a new nonprofit did not duplicate the activities of existing organizations;
- ❑ Create opportunities for local governments to participate in the investigation process; and
- ❑ Assess the availability of resources needed to establish and maintain a nonprofit organization.

While EPA Region III was awarding the CCC a cooperative agreement noncompetitively, the LGAC was still not convinced about using a new nonprofit. The progress report to the Chesapeake Executive Council, dated October 30, 1997, summarized the actions taken by LGAC to implement the Local Government Participation Action Plan. This report, issued after Region III had awarded the cooperative agreement to the CCC, did not mention the CCC. To the contrary, the report discussed the nonprofit workgroup results. The workgroup concluded that:

A nonprofit organization ... will contribute to the overall effort to protect and restore the Bay.... The LGAC is currently considering the workgroup's findings and is not ready to make a recommendation at this time.

Despite this report, Region III officials had already awarded a cooperative agreement to the CCC in order to fund the start-up of the nonprofit.

EPA officials indicated that it was important to note that during the LGAC's November 1997 meeting, it ultimately endorsed the feasibility report and the working relationship

with the CCC. However, we noted that the minutes of this meeting showed that the LGAC endorsed the CCC after a tie vote was broken by the LGAC Chair, who was a board member of the CCC. At this same meeting, a second motion was passed which called for the OIG to perform this audit.

The LGAC members who requested this audit contend there were several reasons why Region III awarded this grant to the CCC. Chief among them was the relationship between Region III officials, the CCC's Executive Director, and the President of Redman/Johnston Associates. It has also been asserted that this current arrangement provides Region III more control of Chesapeake Bay Program funds destined for local governments. However, we could not confirm the validity of the reasons.

Conclusion

The advance incorporation of the CCC gives the appearance of preferential treatment because of:

- ◆ the Executive Director of the CCC and Redman/Johnston Associates integral participation in the feasibility study;
- ◆ EPA's award to the CCC before the final publication of the study;
- ◆ EPA's reliance on the study's conclusion, before the final publication of such conclusion, to justify a grant award to the CCC; and
- ◆ the study's subsequent conclusion which provided a financial benefit to the CCC's incorporators.

Region III's actions did not fulfill its responsibility for ensuring that there was adequate justification for the noncompetitive award to the CCC. Instead Region III's actions compromised local initiative, promoted a noncompetitive award, and gave the appearance of preferential treatment.

Recommendations We recommend that the Region III Administrator:

- 2-1 Terminate the existing cooperative agreement awarded to the CCC.
- 2-2 Attempt to award a new cooperative agreement competitively if Region III continues to believe the services are needed. If advertisements and requests for proposals do not identify entities able to perform the services required, then Region III can award the cooperative agreement noncompetitively. This award should only be made after Region III has ensured adequate justification has been provided.

Region III Response

In retrospect, given the clarification of policies which will result from the draft report, as well as controversy within the LGAC over the formation of the Center, it would have been better to have competed this grant. This would have eliminated any appearance of preferential treatment even where there was none, as in this case. The Bay Program is currently engaged in a process to do just that for a successor grant. At the same time, it is important to note that the Bay Program was following normal and customary practice, and that Agency policy provides a considerable degree of discretion to the Program Manager to make determinations of the need for formal competition. The Chesapeake Bay Program employs considerable competition in the selection of priority projects and tasks through an open Budget Steering Committee process involving dozens of organizations, and it was assumed that this provided ample competition to meet the intent of Agency policy. Given the concerns identified in the draft report, the Region will evaluate its procedures for competition and implement changes as may be necessary.

The Region further agrees that as the new nonprofit was formed, the Center and the contractor should have acted in ways which would have eliminated any appearance of a conflict and the complaints that resulted. Simple preventative measures should have been taken much earlier in the process: the LGAC Vice Chair should have stepped down from the Workgroup Chairmanship when he first started considering launching a nonprofit; he should have informed the LGAC of the Center's creation in a timely manner and recused himself on all matters affecting the nonprofit decision; and a clearer separation should have been made between the work of the contractor and the Center's issuance of a Request For Qualifications used to employ the new LGAC support staff. We recognize the inherent difficulty of anyone conducting business with the LGAC without interacting with their official

support staff, Redman/Johnston and Associates. However, greater efforts should have been employed to ensure separation of the roles and avoid any appearance of conflict in contracting. The Region took strong action in September 1997, prior to the award of the first Center grant, to seek written assurances from the CCC Director about avoiding even the appearance of a conflict of interest in future actions.

The Region agrees with Recommendation 2-1 that the existing cooperative agreement should be brought to an end and be replaced by a new grant arrangement as determined by the outcome of a competitive Request for Proposals (RFP). The Region also commented that it is critical to maintain LGAC and other project support, and a precipitous action to replace it could lead to the same issues of non-competition raised by the Inspector General. We will transition to the successful candidate(s) under the new RFP on or around August 1, 1999.

Region III concurs with Recommendation 2-2. The Region has taken steps to compete the local government assistance functions consistent with an overall Chesapeake Bay Program management plan. By taking such action, the Region does not indicate concurrence that the initial justification for non-competition was inadequate. In fact, the file justification for this award far exceeded in level and detail what is typical for other similar grants. No extraordinary efforts were taken by the Region to streamline the award of this grant so as to deny others the opportunity to compete.

A broad-based Workgroup was employed to develop the Feasibility Report which was essentially completed on schedule in June 1997, prior to the CCC's incorporation. This consensus report of the Workgroup, involving 12 participants in total and 5 existing nonprofit entities, made a clear recommendation that "there is currently not a non-profit organization that serves as a regional resource organization in the watershed with a local government focus." Significant efforts were also made by the Workgroup staff to contact existing service providers in the Region to see if the work could be done through existing means. Staff reported directly to the Workgroup, which included EPA, that they could not identify a willing nonprofit entity. Documentation of this search and of the Workgroup's serious concern for impacts on existing service providers is provided in the Feasibility Report.

Other serious inaccuracies in the draft report relate to compliance with law and Agency policies. The draft report makes declarative statements that the Region did not comply with Agency Fact Sheets and the Federal Grant and Cooperative Agreement Act with respect to competition for grants. While we acknowledge above that, in retrospect, competing this grant could have averted any appearance of

conflict, we do not concur with these statements and wish to point out the full context of these documents.

Agency policy, as articulated in the Grants Management Fact Sheet for Agency Leaders entitled Competition for Assistance Agreements, Number 9, states that “the Agency **encourages** fair and open competition in the award of **discretionary** assistance agreements.” (Emphasis added.) This does not constitute a requirement to do so in the case of every grant awarded. In fact, the Fact Sheet clearly states that “Program Leaders **should determine up-front** if a competitive process **is appropriate** for your assistance program.” (Emphasis added.) Further, the Federal Grant and Cooperative Agreement Act of 1977 “encourages competition, **where appropriate**, in the award of grants and cooperative agreements.” (Emphasis added.)

Citing Executive Order 12674, Principles of Ethical Conduct, the report asserts that Region III did not act impartially and without preferential treatment to an organization or individual. At the time of grant award, the Region was not aware of any other eligible and interested prospective grantee, after months of extensive consultations and research conducted by the Feasibility Workgroup and by Region III independently. The COG had not expressed interest in continuing this grant at that point. Therefore, EPA could not have acted in preference to one organization at the exclusion of a known, alternative option. There are no assertions of personal friendship or association in the report. Further, no one in EPA directly benefitted from any of these actions. Therefore, this assertion that Region III officials did not comply with the Principles of Ethical Conduct is incorrect and should be deleted in its entirety.

OIG Evaluation

Region III’s agreement to terminate the existing cooperative agreement with the CCC, and to award future cooperative agreements competitively meets the intent of our recommendations.

The Region stated it conducted a thorough assessment to determine that a “new” nonprofit was needed. However, without asking the existing nonprofit community if it had any interest in providing this service, the Region did not provide them the opportunity to develop an interest in serving the Chesapeake Bay Program. This opportunity was given to the CCC. Moreover, there was no documentation for the “assessment” the Region stated it performed. These two factors, coupled with the CCC Executive Director’s actions to incorporate the CCC before the feasibility study was finalized, are the basis for the findings in this chapter.

We recognize that EPA is not mandated to award all cooperative agreements competitively. However, there must be an adequate justification for all noncompetitive awards. Awarding assistance agreements noncompetitively without a valid reason or justification would open the Agency to allegations of preferential treatment. We disagree that the Budget Steering Committee process fulfilled the need to compete a specific cooperative agreement. It merely defined which projects will get funding.

We disagree with Region III's comments regarding the Executive Order. Region III allowed events to occur that benefitted the contractor and the CCC. The formulation of the CCC's bylaws, mission statement, and articles of incorporation gave preferential treatment. Also, Region III was aware the CCC was being formed by the people performing the feasibility study, which again gives the appearance of preferential treatment. This awareness was evidenced by the written assurance Region III obtained from the CCC Executive Director about avoiding even the appearance of a conflict of interest, except that Region III's actions did not go far enough. The Region did not exercise its responsibility to ensure that the CCC Executive Director complied with the written assurance he gave to Region III.

CHAPTER 3

IMPROPER USE OF COOPERATIVE AGREEMENTS

EPA should not have awarded cooperative agreements to intermediaries who awarded contracts to obtain LGAC support services. EPA officials explained that by awarding cooperative agreements to obtain the services of an LGAC support contractor, it was able to avoid Federal procurement regulations, making the procurement for support services easier. According to these same officials, they were attempting to get LGAC support work accomplished in a more efficient manner, since they believed they had the option to award either a contract or assistance agreement. However, Region III's actions did not comply with the intent of the Federal Grant and Cooperative Agreement Act of 1977 and fostered a perception of preferential treatment.

Assistance Agreement Misuse Triggers Concerns

While easing the process for awarding the support contracts, EPA did not comply with the intent of the Federal Grant and Cooperative Agreement Act of 1977. This Act was passed because Congress was concerned that Federal agencies were misusing assistance agreements to circumvent competition and other procurement rules. Moreover, EPA Order 5700.1 prohibits using cooperative agreements to circumvent procurement regulations.

EPA Order 5700.1 is designed to inform program, assistance, and procurement award officials of circumstances that require the use of contracts rather than assistance agreements. The Order provides that EPA may not award an assistance agreement to an eligible intermediary [such as a nonprofit entity] to provide assistance to an ineligible recipient [such as a profit making entity].

Legislative History of the Competition in Contracting Act of 1984, while not governing assistance agreements, explains Congress' desire for competition in Federal awards. Senate Report Number 98-50, at 3-4 (1984), states that:

. . . possibly the most important benefit of competition is its inherent appeal of ‘fair play.’ Competition maintains the integrity in the expenditure of public funds by ensuring that government contracts are awarded on the basis of merit rather than favoritism. . . . The Attorney General has interpreted congressional intent as preventing favoritism. . . .

**EPA Improperly
Used Assistance
Agreements**

For a number of years the COG used an employee to provide LGAC support. After this person resigned, the COG began using contracts to obtain LGAC support. For more than four years EPA awarded noncompetitive cooperative agreements to the COG, which in turn awarded contracts to provide LGAC support services. To obtain these support services, the COG awarded contracts to Redman/Johnston Associates. For example, during fiscal 1996, EPA awarded a \$201,000 cooperative agreement to the COG. Using these cooperative agreement dollars, the COG then awarded a \$192,000 time-and-materials contract for LGAC support. The remaining \$9,000 was kept by COG as compensation for administering the contract. Similarly, in fiscal 1997, EPA awarded the COG \$214,000 which resulted in a \$204,000 time-and-materials contract to Redman/Johnston Associates. The remaining \$10,000 was used for contract administration and miscellaneous expenses such as LGAC meeting lunches, newsletters and photocopying.

According to COG personnel, the LGAC workplan for the contract to Redman/Johnston

COG was “middle man without a role”

Associates was a product of EPA and the contractor. The COG was merely the procurement intermediary EPA used to award the support contract. COG personnel explained that they were simply a “middle man without a role.” In our opinion, there is no legitimate basis for an agency to make an assistance or contract award to an entity that has no role performing the work called for under such award. The award to COG was essentially an award directly to Redman/Johnston Associates which, as a profit making entity, is not eligible to receive this assistance agreement under the Clean Water Act.

COG Excluded In Favor of CCC

After the CCC was incorporated, EPA decided that the COG would no longer be used as the vehicle to award LGAC support contracts. Instead, EPA used the CCC, which awarded a contract to the same contractor that received it in the past. The cooperative agreement awarded to the CCC provided \$314,000, of which \$155,000 was used for the current contract. By providing the contract funds for LGAC support to the CCC, EPA continued the practice of improperly using an intermediary to award a contract.

When we asked why the COG was no longer receiving the cooperative agreement to award the contract, EPA representatives told us that the COG was no longer interested in continuing this service. We determined that the COG initially said it no longer wanted to provide LGAC support; however, the COG informed the nonprofit workgroup in September 1997 of its potential desire to continue providing this support. Subsequently, we also discovered that the COG informed EPA in a letter dated October 22, 1997 of its continued interest in providing staff support to LGAC.

In response to the COG's letter, the EPA Region III Administrator wrote to the COG Chair explaining that Region III understood that COG was no longer interested in providing LGAC support. EPA indicated that based on this understanding and a variety of other factors, EPA had been actively pursuing other options. In our opinion, Region III's action to exclude the COG strengthens the perception of Region III's preferential treatment toward the CCC.

By awarding a contract, as opposed to a cooperative agreement for LGAC support services, Region III could have relied on the expertise of its procurement officials, who are not closely involved with the Chesapeake Bay Program or Redman/Johnston Associates. Such reliance would have enhanced the integrity of the Chesapeake Bay Program Office and not subjected that office to charges of preferential treatment.

Recommendation 3-1 We recommend that the Region III Administrator obtain LGAC support services directly, without using an intermediary.

Region III Response

The Region has agreed to a future limit on the amount of contracting under cooperative agreements for this and similar Chesapeake Bay Program efforts. We have done this by specifying evaluation criteria under the RFP which promote work being done in-house by prospective grantees.

EPA has an obligation under the Clean Water Act to ensure adequate support to the operations of the Chesapeake Bay Program, which is comprised of over a dozen major committees and three advisory committees. The active grant in 1997 was scheduled to come to a close in early March 1998 and the COG had indicated for years its desire to terminate its role. The Region was therefore required to expeditiously identify an alternative, prospective grantee. Time urgency weighed heavily since the grant for LGAC services was expiring. Because of the impending expiration of the grant and the time required to process a new grant, the Chesapeake Bay Program could not wait an indefinite amount of time for final LGAC approval due to the need to support the Advisory Committee. LGAC's meeting schedule and a pattern of intentional delays were not conducive to providing input to this decision in a timely manner.

There are a number of other places in the draft report which are not clear, and where the material presented or analyzed could lead the reader to a misleading or incorrect conclusion. For example, extensive parts of the report are based on the erroneous assumption that the Region's motivation was to use the nonprofit grant recipient as a means to fund a profit-making contractor in violation of procurement regulations. In fact, the contracting out of some services to a profit-making organization by the nonprofit grantee is a practice that had a history predating the current grantee and is permissible under EPA rules. The selection of the contractor was within the full authority and discretion of both previous and current grantees.

Under these circumstances, it is misleading to include in the Introduction and Chapter 3 of the draft report allegations that the Region was trying to avoid procurement regulations. This is simply not the case. The Region sought out no contractors, instructed no grantee to contract, was not the direct beneficiary of the grant, and avoided no procurement regulations. This section of the Report and the relevant parts of the Introduction should therefore be deleted or corrected.

OIG Evaluation

Region III's proposed action meets the intent of our recommendation. However, we do not agree that portions of this finding should be deleted or corrected. We do not dispute that grantees are permitted to use subagreements to accomplish work. Moreover, the draft report does not contend that the LGAC support work is for the direct benefit of EPA or another Federal agency. Our finding demonstrates that Region III should procure the LGAC support services directly (not using an intermediary) either through a contract or an assistance agreement.

Awarding an assistance agreement to a nonprofit organization that results in 95% of the funds going to a contractor, with the remainder used for contract administration, indicates that obtaining these services directly (using either an assistance agreement or a contract) was the method that should have been used initially. Moreover, by using an assistance agreement, EPA avoided awarding the contract itself and allowed the CCC to award the contract under less than ideal conditions.

We have noted EPA's perceived need to act expeditiously in the award to the CCC. However, we do not agree that acting so quickly was necessary. Instead, EPA should have considered extending its agreement with COG.

CHAPTER 4

CONFLICT OF INTEREST SHOULD HAVE PRECLUDED AWARD OF CONTRACT

As a nonprofit recipient of EPA funds, the CCC's conduct is governed by 40 CFR Part 30. This regulation addresses a recipient's ethical responsibilities. Among such responsibilities is the requirement to avoid a contract award that would raise a real or apparent conflict of interest on the part of the award official. In the case of the CCC, the Executive Director acted favorably toward Redman/Johnston Associates by awarding it two contracts after Redman/Johnston Associates absorbed costs totaling approximately \$2,300 for incorporating the CCC. This action compromised the integrity of the CCC's contract award process and violated EPA regulations.

**Contractor Should
Have Been
Disqualified**

Title 40 CFR 30.42 states that no recipient official shall participate in a contract award if a real or apparent conflict of interest would be involved. This regulation further establishes that the recipients shall neither solicit nor accept gratuities, favors, or anything of value from contractors, or parties to subagreements.

Contractor and CCC
interaction was
improper

Title 40 CFR 30.43 requires all procurement transactions to be conducted in a manner that provide, to the maximum extent practical, open and free competition. The regulations require the recipient to be alert to organizational conflicts of interest as well as noncompetitive practices among contractors that may restrict or eliminate competition. It also requires that in order to eliminate an unfair competitive advantage, contractors that develop or draft specifications, requirements, statements of work, invitations for bids, and/or requests for proposals shall be excluded from competing for such procurements.

Title 40 CFR 30.44 requires a clear and accurate description of the technical requirements for the services to be procured. Moreover, this **written** description should contain technical requirements in terms of functions to be performed, including the minimum acceptable standards.

Title 40 CFR 30.46 requires a recipient to have procurement records that include, at a minimum, the basis for contractor selection; justification for lack of competition when competitive bids or offers are not obtained; and the basis for award cost or price.

Title 40 CFR 30.45 requires that some form of cost or price analysis shall be made and documented in the procurement files in connection with every procurement action.

Redman/Johnston Associates participated in the preparation of the assistance applications submitted by the CCC and had advance knowledge about the cooperative agreement and intended contracts. Despite this, Redman/Johnston Associates subsequently entered into a sole source verbal agreement with the grantee to receive \$10,000 from the cooperative agreement awarded to the CCC.

Verbal agreement prohibited

EPA Region III awarded the CCC a \$45,000 cooperative agreement on September 30, 1997. According to this agreement, the money was to be used to support start-up functions for the CCC; conceptualize and begin to prepare a local government training module and clearinghouse; and plan a local government summit.

Initially, the CCC's application for assistance, dated July 30, 1997, indicated that it would award a \$10,000 contract for preparation and filing of the articles of incorporation, attorney fees, accountant fees, and staff support to create the nonprofit organization. Ultimately, the CCC revised its application for this assistance agreement, and indicated that the \$10,000 would be used for a contract to obtain "technical assistance and organization start-up support to initiate the activities of the Center [CCC]." Our review found that the

contractor signed the Executive Director's name with his own initials (ADR) next to the Executive Director's name on the revised application for Federal Assistance that was submitted to EPA (See Exhibit C). Because of this signatory arrangement, it is not clear to us what role the Executive Director may have played in the submission of this revised application. However, the contractor stated in his response that the CCC Executive Director authorized this signature.

Although he subsequently resigned, it is important to note that at the time the CCC was incorporated, the President of Redman/Johnston Associates was listed as a member of the Board of Directors in the CCC's articles of incorporation. Moreover, the CCC's application for the cooperative agreement listed the President of Redman/Johnston Associates as the project manager. The assistance application also contained this same contractor's name and telephone number as the point of contact for EPA questions.

Contrary to what was in the CCC's application, both the Executive Director of the CCC and the President of Redman/Johnston Associates told us the \$10,000 was for additional work needed to complete the feasibility study. The invoice submitted by the contractor to the CCC confirmed that the contractor billed for work on the feasibility study. These costs are unallowable because this work was not authorized under the cooperative agreement awarded to the CCC.

Subsequently, we asked for a copy of the contract and the applicable scope of work. Both the Executive Director of the CCC and the President of Redman/Johnston Associates told us they entered into a verbal agreement for \$10,000 with the approval of EPA. However, they had no supporting documents to validate this verbal agreement or EPA's approval.

Our review of the CCC's financial records revealed that as of May 6, 1998, the contractor was paid only \$3,300 for his services. The CCC's Executive Director told us the contractor had not been paid the full \$10,000 billed because the CCC was experiencing cash flow problems. He explained that the payments would be made later. In any event, the verbal

agreement for \$10,000 should not have been made between the CCC and the contractor because 40 CFR Part 30 prohibits this type of agreement.

On March 31, 1998, the CCC awarded another contract for the LGAC support services to Redman/Johnston Associates. It appears from the steps that preceded this award that

Contract awarded with only pretense of competition

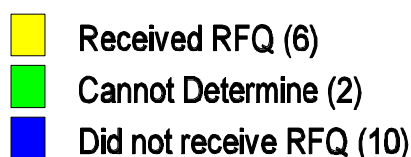
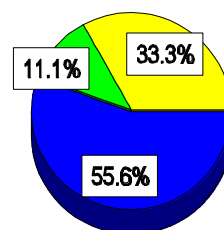
Redman/Johnston Associates had an inside track to the award of the contract and should have been excluded. In our opinion, documents in Region III's and the CCC's files indicated that the CCC's award to Redman/Johnston Associates was accomplished with only the pretense of competition.

This second contract was funded by an amendment to the cooperative agreement awarded to the CCC. The amendment, dated March 2, 1998 was to increase the funding by \$314,000 and extend the project and budget periods. Of this amount, \$155,000 was to fund the contract award to Redman/Johnston Associates. To award the second contract, the CCC used a Request for Qualifications (RFQ) method for selecting the contractor. The RFQ specified that if the CCC continued to receive financial assistance from EPA, the CCC reserved the right to extend the contract through four subsequent years.

According to the CCC's Executive Director, the RFQ for the LGAC support contract was sent to eighteen companies on February 6, 1998. We obtained the names of the eighteen companies and began contacting them by telephone on March 31, 1998, the day the contract was awarded. Our review was able to confirm that only six of the eighteen received the RFQ. Two companies did not return our telephone calls. Of the remaining ten companies, four could not be located² and six indicated they never received it.

2. There were no telephone, Internet, or Dunn & Bradstreet listings available for any of these four firms. This search was performed shortly after the RFQ was mailed.

Receipt of RFQ



Of the six companies that received the RFQ, only Redman/Johnston Associates submitted a proposal and was awarded the contract on March 31, 1998. The five companies that did not respond told us they did not bid because:

- P two were not qualified;
- P one believed the incumbent would be awarded the contract and, therefore, decided not to submit a proposal³;
- P one bid on a prior contract and never received a response; and
- P one did not give a reason for not responding.

When we initially requested the list of companies that were mailed the RFQ, this document was faxed from Redman/Johnston Associates to the EPA Project Officer, and ultimately was sent to us. Although the Executive Director of CCC and Region III officials said that the contract was awarded competitively, the only entity that could provide a list of the RFQ recipients was Redman/Johnston Associates. This document should have been generated by the CCC in the course of a competitive procurement; it should have been in the CCC's files; and it should not have been released to Redman/Johnston Associates, which should have been completely separated from the CCC's contract award process.

3. This company later sent a solicitation letter to the CCC for the preparation of an educational outreach program.

Other documents also showed the contract was awarded with only the pretense of competition.

- EPA files contained the Region III Project Officer's notes that indicated "competitive procurement—Tony prefers RFQ." Tony Redman is a partner of Redman/Johnston Associates, the company that received the support contract, and the RFQ was the method used to award the contract.
- The CCC's 1998 Application for Federal Assistance included the CCC's projected income and budgets. It also included the estimated amounts budgeted for the LGAC support contract. This budget is titled Draft #2 revised and includes handwritten changes on various line items. It was faxed from Redman/Johnston Associates to the CCC on September 11, 1997. This was six months before the contract was awarded on March 31, 1998. Redman/Johnston Associates access to such information should have disqualified it from the contract award.
- The Application for Federal Assistance, dated December 16, 1997, signed by the Executive Director of CCC was faxed to the Region III Grants Management Branch from Redman/Johnston Associates on February 25, 1998. These funds were awarded by EPA to the CCC on March 2, 1998, and included the funds for the LGAC support award.

Redman/Johnston Associates' integral involvement in the procurement process should have eliminated its eligibility to compete for this contract. Such involvement gave Redman/Johnston Associates a significant competitive advantage that 40 CFR Part 30 is designed to prohibit. Such involvement also casts doubt on the legitimacy of the RFQ process which resulted in Redman/Johnston Associates being the sole bidder.

**CCC's
Procurement
Records Were
Incomplete**

Title 40 CFR 30.45 requires some form of cost or price analysis shall be made and documented in connection with every procurement. Because there was only one bidder, it was essential that the CCC perform this cost or price

analysis. Price analysis compares a contractor's prices to market prices. A cost analysis reviews each element of cost to determine reasonableness. Without a cost or price analysis, EPA had no assurance that contract expenditures were reasonable. Neither of these documents were found in the CCC's files. Moreover, there was no documentation showing a reason for contractor selection.

Also, the CCC did not maintain written standards of conduct for employees awarding and administering contracts as required by 40 CFR 30.42. The Executive Director explained to us on April 28, 1998 that he had no such standards because EPA had never provided him with a copy of the governing EPA regulation.

The Application for Federal Assistance included a Procurement System Certification, which required the applicant to certify that it will follow EPA regulations. This would have been the time the Executive Director should have ensured that CCC complied with all applicable EPA regulations. However, we found that the Executive Director of the CCC did not sign this certification. Rather, the contractor signed the Executive Director's name with his own initials next to the Executive Director's name. The CCC's certification states:

This is a new nonprofit organization. Its procurement procedures will comply with US Environmental Protection Agency regulations and standards.

The Executive Director also should have been aware of what was contained in the CCC's bylaws. We found that the Executive Director of the CCC was also the Secretary and Treasurer which is a violation of the CCC's bylaws. Article VI indicates "any two or more offices may be held by the same person, except the office of Executive Director and Secretary."

Recommendation 4-1 We recommend that the Region III Administrator, in conjunction with the recommendations in Chapters 2 and 3 of this report, recover costs associated with the verbal agreement made between the CCC and Redman/Johnston Associates.

Region III Response

We will review the grantee's response, and defer any action on the recommendation in the interim.

CCC Response

The CCC was incorporated to address needs identified by the LGAC work group. Mr. Redman offered to act as agent for the incorporation to assure it would be in place to provide funding for services to local governments. Mr. Redman's involvement was never substantive in the operation of the Center and as the draft points out, he resigned shortly after incorporation.

The draft asserts Redman Johnston had detailed knowledge of RFQ requirements. LGAC and Bay Program procedures provide this knowledge be widely shared with LGAC members and Bay Program staff. This did not provide a competitive advantage since the same information is provided to all potential bidders. A conflict of interest did not exist because the Center awarded two contracts to Redman Johnston. The contractor was also the Executive Director of LGAC and as such was responsible for preparing budgets, developing work plans and securing LGAC approval of these proposals. Mr. Redman was also responsible for their presentation before the Bay Program's Budget Steering Committee. These roles involve full knowledge of the funds available and their purposes for future LGAC work. Interactions between CCC, Bay Program Staff and the contractor (representing LGAC) was therefore not only normal, it was expected by EPA.

EPA staff was fully aware that I intended to contract with Redman Johnston to provide technical assistance and organizational start-up support to initiate the activities of the Center. I regarded this work in many respects as an extension of the work already completed by Redman Johnston to evaluate the need for, and feasibility of using a non-profit organization to provide technical and financial assistance to local governments. The actual contract for \$9,894 was verbal. We believe 40 CFR 30 Parts 43 and 44 do not prohibit our verbal agreement to a contract in this amount since clear expectations existed, services were performed based on these expectations, an invoice was rendered and reviewed by CCC and EPA staff prior to payment, and full payment made based on the work completed.

The draft report asserts an application dated July 30, 1997 was submitted by CCC for services which covered incorporation and other services to create the Center. No such application was submitted. I have not seen such an application. I know these costs are not appropriate for a federal application. The application submitted in my name in early August, 1997 (I was in North Carolina and authorized Mr. Redman to sign my name) was the only application submitted.

I believe neither the facts nor the draft support the assertion that the second contract for \$155,000 was a "done deal." The Center used an RFQ process that was identical to the COG's in previous years, including as recently as 1996. We used the same contractor list and evaluation procedures. The draft indicated Mr. Redman preferred an RFQ process. It did not mention the RFQ process was the one used by COG, which is why the CCC used it. Redman Johnston was not the assured awardee.

Eighteen firms were sent the RFQ. I reasonably believed all eighteen firms received the RFQ since none were returned. Inspector General staff verified that at least six acknowledged receipt. Even this number is sufficient to assure competition. Had additional qualifying responses been received, they would have been fairly and objectively evaluated by parties other than myself. It is noted in the draft that the list of RFQ recipients was obtained from Redman Johnston. Mr. Redman's response indicated why this occurred.

I believe it was appropriate for Mr. Redman to review the draft budget titled Draft 2, dated September 11, 1997, in light of his role with LGAC and his responsibility to present the budget to the Budget Steering Committee. The draft notes the application for assistance was faxed from Redman Johnston's office on December 16, 1997. I was in New Orleans at an EPA meeting and asked a Redman Johnston staff member (without Mr. Redman's knowledge) to submit the application based on text I had reviewed and approved since the staff member had a copy of the application on disk and I did not have such materials. After keying in the text I had approved on the form, he forwarded it to EPA. During this period, late January and February, 1998, I was in the hospital recovering from surgery.

Redman/Johnston Associates Response

It is correct that I spearheaded the incorporation of the CCC. I agreed to do that at no cost to EPA. The EPA representatives indicated that if a nonprofit was formed, they would continue to fund LGAC activities through the CCC. My actions to create the nonprofit were designed to protect LGAC access to financial resources to support their ongoing activities. Your report should note that Mr. Allen expressly authorized and directed me to submit the grant application in his name.

There is nothing improper about me being personally aware of future grant availability. My job with LGAC was to prepare budgets based upon anticipated funding. Concerning the comment that Redman/Johnston benefitted from the grant made to the CCC, it is accurate that there was an addendum to an existing contract that resulted in additional work and revenue to Redman/Johnston, which was funded through a grant which I assisted the Center in preparing.

In investigating circumstances concerning the RFQ that was faxed from my office, I have learned that you requested this list from Mr. Allen, who requested a former employee of mine (the same one that now works for the Center) to obtain a copy on his behalf from the COG. Apparently, he obtained a copy and forwarded it to the Center without my knowledge. I recognize that he was an employee of my firm at that time. Nevertheless, I repeat, I have never seen such a list. In fact, it appears that the only reason such a list was ever in my office at all was because you requested it of the Center, and at Mr. Allen's request, my employee became a transmittal middle man, after the contract was awarded, I should add.

Work done to prepare the feasibility report was authorized in my contract with COG. Unfortunately the level of effort required to explore the feasibility of creating the Center, did not satisfy some LGAC members who expected to see a detailed report. The need for the detailed report and additional related work performed regarding start up for the Center was discussed with EPA staff and additional work was approved by EPA as an extra. At that time it was understood that the estimated cost to complete the work would be \$10,000. Rather than process a contract amendment through COG, EPA staff recommended that I receive compensation from the \$45,000 initial grant to be made to the Center. I accepted that arrangement and performed the work accordingly. Therefore it does not seem reasonable to disallow costs associated with preparation of the feasibility study since I was contractually obligated to complete this task within the scope of work.

OIG Evaluation

The ability of a Redman/Johnston Associates employee to obtain the RFQ list (before contract award and not after as Mr. Redman contends) and a disk copy of the CCC's grant application is a problem. Even more disturbing was the disclosure by the CCC's Executive Director, during our exit conference, that an employee of Redman/Johnston Associates mailed the RFQ to the 18 potential bidders for him. Although Mr. Redman's actions to create a nonprofit were purportedly to protect LGAC access to financial resources, by doing so he also protected the contract revenues his company received for LGAC support.

Although interaction between CCC, Chesapeake Bay Program Staff and the contractor (representing LGAC) was considered normal and expected, we believe

that there is an inherent conflict of interest between the contractor's position as the Executive Director of LGAC and his position as the President of Redman/Johnston Associates. For example, the contractor developed the LGAC workplan and budget that contained amounts estimated for the contract he eventually competed for. Subsequently, he presented this same budget that he developed to the Chesapeake Bay Program's Budget Steering Committee.

The responses from the CCC and Redman/Johnston Associates confirmed that the contractor "spearheaded" the CCC incorporation and submitted the CCC's grant application to EPA. Their responses also confirm that Redman/Johnston was privy to LGAC budget information. The budget document [Draft #2] we discussed in our report provided Redman/Johnston information about the future amendment to the cooperative agreement that EPA would award to the CCC, and the contract the CCC would award as a result of receiving the amendment.

Title 40 CFR 30.46 requires a recipient to have procurement records that include, at a minimum, the basis for contractor selection; justification for lack of competition when competitive bids or offers are not obtained; and the basis for award cost or price. Verbal contracts do not comply with this requirement nor are such contracts good business practice. Although the CCC Executive Director and the President of Redman/Johnston contend there were clear expectations about the verbal agreement, a transaction involving almost \$10,000 involves too many details that cannot be left to memory.

The CCC's Executive Director asserts that he neither saw or submitted a grant application dated July 30, 1997. However, we obtained this document from Region III files and it contains Mr. Allen's signature. A review of this application by the Region III Grants Office disclosed that it contained unallowable costs for items such as incorporating the CCC and fund raising. Annotations in Region III's files indicate that the results of the Region III review were sent to Redman/Johnston, which ultimately sent these same comments to the Executive Director of the CCC. Subsequently, the application was revised and the President of Redman/Johnston affixed Mr. Allen's signature to it before resubmitting it to EPA.

We disagree with the CCC's contention that all 18 firms received the RFQ. Personnel from two of these companies told us they did not receive the RFQ. We determined this occurred because the addresses on the CCC's list were incorrect. Four other companies did not exist; there were no telephone or Internet listings for them. We attempted to locate them through Dunn and Bradstreet, and EPA's Office of Criminal Enforcement, Forensics and Training, which searched Secretary of State Corporate Records and Uniform Commercial Code filings. The CCC's response indicates they used the COG's 1996 RFQ list. Attempting to obtain

competition with an RFQ list that was almost two years old, without verifying its accuracy, does not appear to be prudent.

EPA regulations prohibit Redman/Johnston Associates from competing for the contract awarded by the CCC. The contractor submitted the grant application containing provisions that identified how much money was budgeted for the contract it eventually received. The contractor and the CCC's Executive Director participated in the feasibility study that decided a new nonprofit was needed. The contractor incorporated this new nonprofit [the CCC] without compensation before it received a sole source verbal contract from the CCC. Subsequently, the contractor was the only bidder for a second contract awarded without the cost or price analysis required by EPA regulations. In our opinion, these events raised a real or apparent conflict of interest which 40 CFR Part 30 required the CCC to avoid.

CHAPTER 5

EPA MUST ENSURE THAT RECIPIENTS HAVE AN ADEQUATE FINANCIAL MANAGEMENT SYSTEM

The CCC did not properly account for Federal funds because it did not have an adequate financial management system. Moreover, the contractor did not have an adequate financial management system. According to EPA requirements, a recipient's accounting system must account for all costs incurred under a project and must consistently apply generally accepted accounting principles. As a result, the abilities of these organizations to record, process, summarize and report financial data were adversely affected. This condition affects all the cooperative agreements awarded to the CCC.

EPA's Assistance Administration Manual requires the Agency's program office, as part of the technical review of the application, to assess the applicant's overall capabilities to implement the intended activity efficiently and effectively. The manual indicates that reviews should cover such items as adequacy of financial management and accounting procedures. Title 40 CFR 30.21 requires the recipient's accounting system to provide the following:

- Accurate, current and complete disclosure of the financial results of each federally-sponsored project.
- Records that adequately identify the source and application of funds for federally-sponsored activities. These records will contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, outlays, and income.
- Effective control over and accountability for all funds, property and other assets. Recipients will adequately safeguard all such assets and assure they are used solely for authorized purposes.

- ❑ Comparison of outlays with budget amounts for each award. Whenever appropriate, financial information should be related to performance and unit cost data.
- ❑ Written procedures for determining the reasonableness, allocability and allowability of costs in accordance with the applicable Federal cost principles and the terms and conditions of the award.
- ❑ Accounting records including cost accounting records that are supported by source documentation.

CCC Disregarded Budget

At the time of our review, EPA was the sole source of the CCC's funding. As of May 1998, the CCC had drawn down \$139,000 from EPA and disbursed over \$73,000. The CCC was using the advanced payment method to obtain funds under the assistance agreement. According to 40 CFR 30.22(b), cash advances to a recipient organization will be limited to the amounts needed for the approved program or project. We reviewed these disbursements and found the CCC disregarded EPA requirements when it used funds for projects that were not part of the cooperative agreement.

EPA funds used to prepare assistance applications

Both the cooperative agreement and subsequent amendment contained detailed budgets for all costs. These budgets are required as part of the grant application process. However, the CCC's expenditures indicated that the Executive Director disregarded the detailed budgets when he expended funds. For example, the CCC paid one employee of Redman/Johnston Associates \$1,500, for preparing proposals in order to apply for other grants.⁴ Subsequently, the CCC received one of these assistance awards from EPA. Since preparing these applications is not covered by the cooperative agreement, Federal funds advanced to the CCC should not have been used to pay these costs. In accordance with EPA's

4. EPA selected the CCC for the 1997 Sustainable Development Challenge Grant Program. One of the partners listed on the CCC's project description was Redman/Johnston Associates. EPA also awarded the CCC \$391,000 under a cooperative agreement for the Small Watershed Grants Program. The employee that prepared the proposals is no longer employed by the contractor and is now employed by the CCC as the Director of Programs.

Assistance Administration Manual, a recipient's accounting system must include records that allow comparison of actual costs with budgeted costs for each project.

**CCC's Costs
Unsupported**

We also found the CCC did not maintain adequate support for its expenditures. The CCC's supporting documentation consisted of a haphazard collection of canceled checks, bank statements and invoices. However, we could neither link these documents to funds received under the cooperative agreement, nor could we determine if the expenditures were justified.

For example, the CCC's expenditures included \$184 for lunches for two CCC board meetings. These lunches were to be provided to board members on the day of the CCC's board meetings. However, the CCC did not maintain minutes of the board meetings or any other supporting documentation. Moreover, the CCC claimed the salaries of board members that attended the meetings as an in-kind expenditure chargeable to the cooperative agreement. In accordance with OMB Circular A-110, volunteer services may be counted as cost sharing or matching if the service is an integral and necessary part of an approved project. However, since there is no record of the board meetings, the CCC could not justify the basis for the in-kind services used as the recipient contribution to the cooperative agreement.

At the time of our review, the Executive Director received:

- \$42,252 for Salary
- \$2,474 for Health Insurance
- \$448 for Life Insurance
- \$5,128 for Retirement Benefit Contribution
- \$2,000 reimbursement to himself for miscellaneous items such as office supplies, phone, travel and office expense.

However, he did not maintain documentation, such as timesheets or a time distribution system, as required by OMB Circular A-122 to support his time charged to the cooperative agreement. Section L of OMB Circular A-122 titled, *Support of Salaries and Wages*, requires that reports reflecting the distribution of activity of each employee must

be maintained for all staff members whose compensation is charged, in whole or in part, directly to awards. These types of documents are needed to segregate the eligible work from ineligible work and to support the number of hours charged to the cooperative agreement. Because these documents were not maintained by the CCC, we were unable to determine if EPA funds were used in an effective and efficient manner, and only for eligible and allowable costs. Without this assurance, we considered these costs unsupported.

EPA should not have allowed the CCC to use the advanced payment method to obtain funds from EPA because it did not have an adequate financial management system. According to OMB Circular A-110, reimbursement is the preferred method when the recipient fails to meet the standards for fund control and accountability as established by EPA regulations.

In accordance with EPA's Assistance Administration Manual, supporting documentation must include everything needed to explain a transaction. Recipients must cross-reference supporting documentation so that a transaction can be traced from any document dealing with the transaction back to the initiating documents, and forward to entries in the accounting system. The CCC's record keeping did not satisfy this requirement.

**Contractor's Costs
Unsupported**

Contractor personnel also did not use timesheets or any mechanism to support actual hours charged to the contract. Moreover, the contractor did not segregate costs associated with non-government funded business from the costs chargeable to the contract funded by EPA.

From October 1, 1997 through December 15, 1997, Redman/Johnston Associates was simultaneously billing two contracts funded by EPA. One contract was with the COG for LGAC support and the other was the \$10,000 awarded by the CCC. One contractor employee charged a total of 521 hours to these contracts, but could not provide timesheets of the actual days he worked on each contract.

Redman/Johnston Associates was awarded time-and-materials contracts for the LGAC support. Payments under time-and-materials and labor-hour contracts must be substantiated by individual daily job timecards. However, the contractor did not keep daily timesheets and could not support actual costs or hours charged. Instead, the contractor divided the total amount of the contract over twelve months, and then billed the monthly amount. The contractor's method of billing was to submit a monthly invoice with an estimated number of hours that each employee worked under the contract. When the contract expired, the contractor had been reimbursed the total amount of the award. In effect, the contractor billed as if the contract was a fixed-price contract.

In accordance with 40 CFR 30.44 (c) and OMB Circular A-110, the type of procuring instrument used should be determined by the assistance recipient, but should be appropriate for promoting the best interest of the project. In our opinion, a time-and-materials contract is the least preferred contract type and should be used when no other type is suitable.

Conclusion

We found that neither the CCC nor Redman/Johnston Associates had financial management systems or internal control structures in place to properly account for Federal funds.

Recommendations

We recommend that the Region III Administrator:

- 5-1 Discontinue all payments to the CCC and review all costs already incurred under the cooperative agreements for allowability and reasonableness. To that end, labor amounts billed by Redman/Johnston Associates not supported by adequate timesheets should be disallowed.
- 5-2 Prior to awarding assistance agreements and before allowing advance payments, ensure that recipients have developed and implemented adequate internal controls and financial management systems that comply with OMB Circulars and EPA regulations.

- 5-3 Contact our office prior to grant closeout to afford us the option of performing a final audit of the cooperative agreement.

Region III Response

Region III concurs in-part with Recommendation 5-1. The Region discontinued payments on the cooperative agreement in a letter to the CCC dated November 19, 1998. Based upon a thorough on-site review of the financial management systems of the CCC, conducted on December 3-4, 1998, we have resumed payments in accordance with requirements of the grant agreement.

Region III concurs in part with Recommendation 5-2. At the time of application for cooperative agreements, grantees provide certifications that they will maintain adequate financial records. The Region will continue to require and review all grantee financial management system certifications as part of its review of applications. We cannot perform in-depth site reviews of all grantee records before authorizing payments. This would result in delays in payments and would be counter to the Prompt Payment Act provisions.

CCC Response

The Center for Chesapeake Communities was in the process of “starting up” during the period prior, during and after the review was carried out. Every one of the “systems” and much of the documentation noted in the report were in the process of being created and are now in place. I believe it is unreasonable to believe that any new organization would have all systems, policies, and manuals fully developed in the first eight months of its existence. The report fails to note why the creation of certain systems were delayed and why the Executive Director sought and received critical volunteer help from knowledgeable, skilled and trusted persons. During the period from December through March 1998 my attention to Center start-up was secondary to extraordinary health issues.

The Center's largest expenditure, fully consistent with the authorized grants and funds then received, was my salary. Until May, 1998, I was the only employee. It was easily verified then, and has since been reviewed and verified by EPA Grants and Audit Staff, that the salary and benefits paid to me were both appropriate and consistent with the budgets submitted to EPA. The percentages cited in the draft report concerning payments to me are accurate but easily misleading since during all but the last 30 days of the entire period of September, 1997 to April, 1998 the bulk of all the funds available were for my salary.

It is important to note that I had already initiated procedures to address the requirements of 40 CFR Part 30. The draft asserts that the Executive Director disregarded the detailed budget when funds were expended. This is not the case. Rather, close attention was paid to these budgets and EPA requirements when these expenditures were made. The CCC did employ a Redman Johnston employee on a consulting basis during late March and early April 1998 because help was needed to address critical grant and EPA requirements. The items cited in the draft footnote are in error and misleading. No funds were paid to anyone for the development of an application for a Sustainable Development Challenge Grant. This application was submitted in August 1997.

I did secure help to (1) develop a final draft of a training program required by our start-up grant, (2) provide copy of the small water shed grant required by EPA Bay Program Budget Steering Committee, (3) consult on a draft memo to the Governor of Maryland on the Summit required by our grant, (4) consult on the configuration of office equipment for a new Center office, (5) consult on the content of a draft brochure for the Center (again required by our grant), and (6) respond to certain technical questions from EPA Grants and audit staff on our budgets for ongoing and proposed work. All of these activities are authorized by our grant from EPA. The individual involved had knowledge and skills I believed were essential to our work and I had no other staff to draw on and could not, in good conscience, continue to constantly ask for such enormous time commitments for free.

Board meetings were documented, EPA Staff was present. IG Staff had access to copies of the agenda and other supporting materials in the files provided at the time of their visit. Minutes were not available.

Redman/Johnston Associates Response

The draft report indicated the CCC "paid one employee of Redman/Johnston Associates \$1,500 for preparing proposals in order to apply for two other grants". Redman/Johnston Associates provided some support in the preparation of the Sustainable Development Challenge Grant application. This assistance was limited since our contract at that time made no provision for compensation for such work. However, at no time was I aware of any arrangement between the Center and the employee to be compensated in the amount of \$1,500 for preparing these proposals. Such action was never sanctioned by Redman/Johnston Associates, nor did Redman/Johnston Associates receive any income for this work. This apparently was an arrangement between my about-to-be-former employee and his prospective employer. It was not an arrangement with Redman/Johnston Associates.

Redman/Johnston Associates has been a contractor with COG for more than three years. At no time was our record keeping and billing questioned. Redman/Johnston

Associates requested each payment on an invoice describing the work performed and the period of performance of the work. The contract does not mandate that Redman/Johnston Associates keep time records as a condition for payment. Although the phrase "time and materials" is used in the contract, it is not a typical "time and materials" contract as defined by the Federal Acquisition Regulation, but is more characteristic of a "fixed fee" contract. Specifically, the contract did not specify a fixed hourly rate, which is required for "time and materials" contracts under the Federal Acquisition Regulation. We viewed the contract as a fixed price contract, and understood that we would be paid the budgeted amount for the work performed.

It seems unreasonable for you to indicate that none of the costs are supportable since I provided the audit team copies of reports and documents reflecting completion of many of the tasks budgeted for in the contract. In most cases, the staff time needed to complete work assignments was greater than amounts budgeted. In those cases, I did not submit invoices for additional staff hours because it was our belief that we were committed to complete the assignments for the prices in the contract. We assumed any additional time it might take was not billable, and treated the contract as a fixed price contract. EPA staff who monitored my performance of contract responsibilities during the period March 1997 to March 1998 have never indicated any failure on the part of my firm to complete contract assignments and to do so within the price structure defined in the contract.

Please be advised that since April of 1998, we have adjusted our administrative procedures as a result of your audit team's visit. They provided me the first clear indication that our contract administrative procedures required us to maintain daily time records. Since that time, personnel at Redman/Johnston have been required to keep time sheets for all work related to LGAC assignments. These time sheets now accompany our monthly invoices to the CCC.

OIG Evaluation

During May 1998, we conducted an on-site review of the CCC's financial records. As a result of this review, Region III discontinued payments to the CCC in November 1998. Subsequently, the Region conducted its own review of the CCC's expenditures, and determined that the CCC had improved its financial system, and could show that its expenditures were supported by receipts. In their opinion, the CCC's financial management system properly documented the costs incurred under the three EPA cooperative agreements. Based on this review, Region III reinstated payments to the CCC in early December 1998.

Our analysis of the Region III review disclosed that Region III did not determine if the CCC's expenditures were reasonable and allowable under the grant, as we

recommended in our draft report. Without this determination, the Region's review was incomplete, and we disagree with Region III's action to reinstate payments before determining reasonableness and allowability of costs. In essence, the Region determined that the CCC now had receipts for its expenditures, but the Region did not evaluate whether or not the expenditures were reasonable and allowable under the grant.

Further analysis of the Region III financial review revealed that the CCC's accounting procedures still do not provide for the identification and segregation of unallowable costs. For example, the Region III report showed that the CCC charged the cooperative agreement \$6,500 for fund raising. The CCC was informed by Region III officials at the inception of the grant that fund raising costs were unallowable, and any reference to these activities should be deleted from the budget. The Region III review also revealed that the CCC had overdrawn funds on one cooperative agreement by more than \$82,000 and underdrawn another cooperative agreement by \$35,000. These examples represent additional occurrences where the CCC did not follow the budgets contained in the cooperative agreements with the EPA.

The CCC's response stated that no funds were paid to a Redman/Johnston Associates employee for preparing assistance agreements, but were paid for other activities authorized under the grant. Moreover, during the exit conference, the Executive Director indicated that he had a written consulting agreement with the employee, which he forwarded to us.

We disagree with the CCC Director's position that the \$1,500 paid to the Redman/Johnston Associates employee was only for eligible work. At the time of our site visit, we requested the Executive Director to clarify this expense and he indicated the check was for grant writing. In a later conversation, the Executive Director again told us he paid \$1,500 to the Redman/Johnston Associates employee to prepare the EPA grant application for the Small Watershed Grants Program. This grant writing is not eligible under the grant we reviewed. It is also noteworthy that we did not consider the document provided as a valid consulting agreement because it was not signed or dated by either party. As a result, our position regarding this cost remains unchanged.

We disagree with the CCC's comment that IG staff had access to copies of the board meeting agendas. This information was not available at the time of our site visit. We again requested copies of these agendas during our exit conference, but we have not received them to date.

Redman/Johnston Associates comments also indicated that they viewed the LGAC support contract as a fixed-fee contract, and not a time-and-materials contract. We

disagree with this conclusion because all of the Redman/Johnston invoices were prepared as time and material invoices. Each monthly invoice included the hourly labor rates multiplied by the number of hours each employee charged. It also itemizes materials and other miscellaneous expenses. These invoices indicate that the contract was administered as a time-and-materials contract.

Redman/Johnston Associates commented about EPA reviewing the contractors invoices, and that EPA monitored its performance; however, we believe EPA should not have any involvement with a contractor under an assistance agreement.

We disagree with the CCC's response regarding how long a new organization should be allowed to have its systems, policies and manuals in place. We are sympathetic to the Executive Director's health issues, but these health issues were not a factor during the first three months of the grant period. Moreover, the Executive Director knew many months before the initiation of the grant that the CCC would be formed. EPA regulations require recipients to have these systems in place before the grant starts, and Region III was responsible for ensuring they were in place and operational before awarding the grant.

Exhibit A - Analysis of Expenditures by the CCC

Auditor's Opinion

Funding Instrument	Period of Performance	Costs Expended as of May 1998	Costs Accepted	Costs Unsupported	Note
Cooperative Agreement CB993675-01 awarded to the CCC	November 1997 to May 1998	\$73,621	-0-	\$73,621	1, 2, 3

Note 1: At the time of our fieldwork, the CCC expended \$73,621. We considered the entire amount unsupported for the reasons discussed in this report.

Note 2: The \$10,000 verbal contract with Redman/Johnston Associates should not be charged to the cooperative agreement. These costs are unallowable because work on the feasibility study was not authorized under the cooperative agreement awarded to the CCC.

Note 3: The \$1,500 used for preparing assistance applications is also not included in the scope of work of the cooperative agreement and should be disallowed.

Region III Response

The Regional Grants and Audit Management Branch conducted a site review of the CCC's financial management system and financial records. From this review we have obtained supporting documentation for the \$73,261 which the audit cites as unsupported. A copy of our financial systems review is being forwarded under separate cover. We defer response on the two specific issues in Exhibit A to the grantee and contractor.

CCC Response

The CCC's comments to these issues are contained in Chapters 4 and 5.

Redman/Johnston Associates Response

The contractor's response to the verbal contract issue is contained in Chapter 4.

OIG Evaluation

Our evaluation of the responses are included in Chapters 4 and 5

Exhibit B - Costs Claimed by the Contractor

Auditor's Opinion

Funding Instrument	Period of Performance	Costs Expended as of May 1998	Costs Accepted	Costs Unsupported	Note
Contract Awarded by the COG under Cooperative Agreement CB003983-06-0	March 1997 to March 1998	\$204,000	-0-	\$204,000	1

Note 1: During our fieldwork, we reviewed the invoices associated with the last contract the COG awarded to Redman/Johnston Associates. The period of performance for this contract was March 1997 to March 1998. We considered the entire \$204,000 to be unsupported because the expenditures were not supported by adequate documentation. We did not review invoices applicable to the previous contracts the COG awarded to Redman/Johnston Associates. However, discussions with the contractor indicated the record keeping and billing methods used for these contracts were essentially the same as the contract we reviewed.

We did not review costs incurred by Redman/Johnston Associates under the contract awarded by the CCC for LGAC support. At the time of our review, Redman/Johnston Associates services under this contract were just beginning.

Region III Response

Defer to Grantee or contractor's Response.

Redman/Johnston Associates Response

Redman/Johnston Associates comments to this exhibit are included in Chapter 5.

OIG Evaluation

Our evaluation of the contractor's response is included in Chapter 5.

Exhibit C - Excerpt from Revised Application for EPA Assistance

APPLICATION FOR FEDERAL ASSISTANCE

OMB Approval No. 0348-0043

1. TYPE OF SUBMISSION: Application <input checked="" type="checkbox"/> Preapplication Construction <input type="checkbox"/> Construction Non-Construction <input type="checkbox"/> Non-Construction		2. DATE SUBMITTED July 31, 1997	Applicant Identifier																					
3. DATE RECEIVED BY STATE		State Application Identifier																						
4. DATE RECEIVED BY FEDERAL AGENCY		Federal Identifier																						
5. APPLICANT INFORMATION																								
Legal Name: Center for Chesapeake Communities		Organizational Unit:																						
Address (give city, county, state, and zip code): Center for Chesapeake Communities PO Box 1686 Annapolis Maryland 21401-1686		Name and telephone number of person to be contacted on matters involving this application: Tony Redman, Director, LGAC 410.822.9630																						
6. EMPLOYER IDENTIFICATION NUMBER (EIN): Not Yet Assigned 5 2 2 0 5 0 9 5 4		7. TYPE OF APPLICANT: (enter appropriate letter in box) <input checked="" type="checkbox"/> N A. State B. County C. Municipal D. Township E. Interstate F. Intermunicipal G. Special District H. Independent School Dist. I. State Controlled Institution of Higher Learning J. Private University K. Indian Tribe L. Individual M. Profit Organization N. Other (Specify) <u>Non-profit Corporation</u>																						
8. TYPE OF APPLICATION: <input checked="" type="checkbox"/> New <input type="checkbox"/> Continuation <input type="checkbox"/> Revision If Revision, enter appropriate letter(s) in box(es) <input type="checkbox"/> <input type="checkbox"/> A. Increase Award B. Decrease Award C. Increase Duration D. Decrease Duration Other (Specify):		9. NAME OF FEDERAL AGENCY: Environmental Protection Agency Region III Philadelphia, PA																						
10. CATALOG OF FEDERAL DOMESTIC ASSISTANCE NUMBER: 6 6 4 6 6 TITLE: Chesapeake Bay Program		11. DESCRIPTIVE TITLE OF APPLICANT'S PROJECT: Support start up funding for incorporation and provide assistance to support functions and operational needs for the Center for Chesapeake Communities.																						
12. AREAS AFFECTED BY PROJECT (Cities, Counties, States etc.): DC, MD, VA, PA																								
13. PROPOSED PROJECT Start Date: September 1, 1997 Ending Date: December 31, 1997		14. CONGRESSIONAL DISTRICTS OF: a. Applicant: DC, MD, VA, PA b. Project: DC, MD, VA, PA.																						
15. ESTIMATED FUNDING: <table border="1" style="width: 100%; border-collapse: collapse;"> <tr><td>a. Federal</td><td>\$45,000</td><td>.00</td></tr> <tr><td>b. Applicant (in-kind)</td><td>\$2,368</td><td>.00</td></tr> <tr><td>c. State</td><td>\$</td><td>.00</td></tr> <tr><td>d. Local</td><td>\$</td><td>.00</td></tr> <tr><td>e. Other</td><td>\$</td><td>.00</td></tr> <tr><td>f. Program Income</td><td>\$</td><td>.00</td></tr> <tr><td>g. TOTAL</td><td>\$47,368</td><td>.00</td></tr> </table>		a. Federal	\$45,000	.00	b. Applicant (in-kind)	\$2,368	.00	c. State	\$.00	d. Local	\$.00	e. Other	\$.00	f. Program Income	\$.00	g. TOTAL	\$47,368	.00	16. IS APPLICATION SUBJECT TO REVIEW BY STATE EXECUTIVE ORDER 12372 PROCESS? a. YES. THIS PREAPPLICATION/APPLICATION WAS MADE AVAILABLE TO THE STATE EXECUTIVE ORDER 12372 PROCESS FOR REVIEW ON: DATE <u>7-31-1997</u> b. NO. <input type="checkbox"/> PROGRAM IS NOT COVERED BY E.O. 12372 <input type="checkbox"/> OR PROGRAM HAS NOT BEEN SELECTED BY STATE FOR REVIEW	
a. Federal	\$45,000	.00																						
b. Applicant (in-kind)	\$2,368	.00																						
c. State	\$.00																						
d. Local	\$.00																						
e. Other	\$.00																						
f. Program Income	\$.00																						
g. TOTAL	\$47,368	.00																						
17. IS THE APPLICANT DELINQUENT ON ANY FEDERAL DEBT? <input type="checkbox"/> Yes If "Yes" attach an explanation <input checked="" type="checkbox"/> No																								
18. TO THE BEST OF MY KNOWLEDGE AND BELIEF, ALL DATA IN THIS APPLICATION/PREAPPLICATION ARE TRUE AND CORRECT, THE DOCUMENT HAS BEEN DULY AUTHORIZED BY THE GOVERNING BODY OF THE APPLICANT AND THE APPLICANT WILL COMPLY WITH THE ATTACHED ASSURANCES IF THE ASSISTANCE IS AWARDED.																								
a. Type Name of Authorized Representative G. Allen		b. Title Executive Director	c. Telephone Number: 301.262.4294 or 410.822.9630																					
Signature of Authorized Representative 		e. Date Signed: July 30, 1997																						

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Standard Form 424 (REV. 4-92)
 Prescribed by OMB Circular 41-02

Appendix 1 - Region III's Response to the Draft Report

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
REGION III
1650 Arch Street
Philadelphia, Pennsylvania 19103-2029

March 10, 1999

SUBJECT: Response to Draft Audit Report on the
Center for Chesapeake Communities
Report Number E6DEP8-03-0014

FROM: W. Michael McCabe 
Regional Administrator (3A100)

TO: Carl A. Jannetti
Divisional Inspector General for Audit (3AI00)

This responds to the Draft Audit Report on the formation of the nonprofit Center for Chesapeake Communities (CCC). This audit was requested by an Advisory Committee of the Chesapeake Bay Program with full support of the Region. We saw it as an opportunity to clarify and strengthen policies in a particularly confusing area of grants management related to awards to nonprofit organizations. The audit was so noted in our annual Assurance Letter under the Federal Managers Financial Integrity Act.

The Region concurs with virtually all the Recommendations outlined in the Draft Report, and in a number of instances has already taken actions which have the effect of carrying out the Recommendations in whole or in part. This includes a site review and evaluation of the Center's financial management and records systems; development of a management plan for competing nonprofit grants in the Chesapeake Bay Program Office; issuance of the first Request for Proposals under the new competitive procedures outlined in the management plan; and initiation of a vulnerability assessment for all Bay Program grants. Other actions will be taken in full response to the Recommendations made in the Final Report.

In retrospect, given the clarification of policies which will result from the Draft Report, as well as controversy within the Local Government Advisory Committee (LGAC) over the formation of the Center, it would have been better to have competed this grant. This would have eliminated any appearance of preferential treatment even where there was none, as in this case. The Bay Program is currently engaged in a process to do just that for a successor grant. At the same time, it is important to note that the Bay Program was following normal and customary practice, and that Agency policy provides a considerable degree of discretion to the Program Manager to make determinations of the need for formal competition. The Chesapeake Bay Program employs considerable competition in the selection of priority projects and tasks through an open Budget Steering Committee process involving dozens of organizations, and it was assumed that this provided ample competition to meet the intent of Agency policy. Given the concerns identified in the Draft Report, the Region will evaluate its procedures for competition and implement changes as may be necessary.

The Region further agrees that as the new nonprofit was formed, the Center and the
Customer Service Hotline 1-800-

contractor should have acted in ways which would have eliminated any appearance of a conflict and the complaints that resulted. Simple preventative measures should have been taken or used much earlier in the process: the LGAC Vice-Chair should have stepped down from the Workgroup Chairmanship when he first started considering launching a nonprofit; he should have informed the LGAC of the Center's creation in a timely manner and recused himself on all matters affecting the nonprofit decision; and a clearer separation should have been made between the work of the contractor and the Center's issuance of an RFQ used to employ the new LGAC support staff. We recognize the inherent difficulty of anyone conducting business with the LGAC without interacting with their official support staff, Redman/Johnston and Associates. However, greater efforts should have been employed to ensure separation of the roles and avoid any appearance of conflict in contracting. The Region took strong action in September 1997, prior to the award of the first Center grant, to seek written assurances from the CCC Director about avoiding even the appearance of a conflict of interest in future actions.

To provide further context and to correct misleading statements in the Draft Report, we recommend that the following issues be clarified:

First, it was not the practice of the Bay Program to compete such small grant awards in discretionary program areas. Project level competition is common in the Bay Program and grantee competition is common for national grant programs such as Environmental Education and Environmental Justice but not for smaller discretionary programs. It was common practice for the Region to accept a concise statement of justification for non-competition in grant awards. In fact, the file justification for this award far exceeded in level and detail what is typical for other similar grants. No extraordinary efforts were taken by the Region to streamline the award of this grant so as to deny others the opportunity to compete. In fact, at the time of initial grant award, no other eligible and interested organization was known to the Region.

Second, the Program was working under a clear mandate from the Chesapeake Executive Council to significantly enhance technical and financial assistance to local governments to meet Bay Program objectives. A critical recommendation of the Local Government Participation Action Plan, central to many other of the commitments being fulfilled, was investigating the feasibility of a new nonprofit since it had been established through extensive outreach that capacities to assist locals were needed throughout the watershed.

Third, a broad-based Workgroup was employed to develop the Feasibility Report which was essentially completed on schedule in June 1997, prior to the CCC's incorporation. This consensus report of the Workgroup, involving 12 participants in total and 5 existing nonprofit entities, made a clear recommendation that "there is currently not a non-profit organization that serves as a regional resource organization in the watershed with a local government focus." Significant efforts were also made by the Workgroup staff to contact existing service providers in the Region to see if the work could be done through existing means. Staff reported directly to the Workgroup, which included EPA, that they could not identify a willing nonprofit entity. Documentation of this search and of the Workgroup's serious concern for impacts on existing service providers is provided in the Feasibility Report.

Fourth, no objections to the formation of the nonprofit were heard from the Virginia state government or LGAC representatives on the Workgroup, or from the Washington Council of Governments, during the drafting of the Feasibility Report. Last minute objections from Virginia

representatives, after the report was essentially completed, evidenced a breakdown in communications between career civil servants and these appointees on this matter, which EPA could not have anticipated. This created confusion about the consensus reached in the Workgroup. Confusion was also evidenced in the change of position and the late expression of interest in this award by the Washington Council of Governments, whose staff cited suburban Virginia representatives as the source of the last minute change of position.

Finally, EPA has an obligation under the Clean Water Act to ensure adequate support to the operations of the Bay Program, which is comprised of over a dozen major committees and three advisory committees. The active grant in 1997 was scheduled to come to a close in early March 1998 and the current grantee (WASHCOG) had indicated for years its desire to terminate its role. The Region was therefore required to expeditiously identify an alternative, prospective grantee. Time urgency weighed heavily since the grant for LGAC services was expiring. Because of the impending expiration of the grant and the time required to process a new grant, the Bay Program could not wait an indefinite amount of time for final LGAC approval due to the need to support the Advisory Committee. LGAC's meeting schedule and a pattern of intentional delays were not conducive to providing input to this decision in a timely manner.

There are a number of other places in the Draft Report which are not clear, and where the material presented or analyzed could lead the reader to a misleading or incorrect conclusion. For example, extensive parts of the report are based on the erroneous assumption that the Region's motivation was to use the nonprofit grant recipient as a means to fund a profit-making contractor in violation of procurement regulations. In fact, the contracting out of some services to a profit-making organization by the nonprofit grantee is a practice that had a history predating the current grantee and is permissible under EPA rules. The selection of the contractor was within the full authority and discretion of both previous and current grantees.

Under these circumstances, it is misleading to include in the Introduction and Chapter 3 of the Draft Report allegations that the Region was trying to avoid procurement regulations. This is simply not the case. The Region sought out no contractors, instructed no grantee to contract, were not the direct beneficiary of the grant, and avoided no procurement regulations. This section of the Report and the relevant parts of the Introduction should therefore be deleted or corrected.

Other serious inaccuracies in the Draft Report relate to compliance with law and Agency policies. The Draft Report makes declarative statements that the Region did not comply with Agency Fact Sheets and the Federal Grant and Cooperative Agreement Law with respect to competition for grants. While we acknowledge above that, in retrospect, competing this grant could have averted any appearance of conflict, we do not concur with these statements and wish to point out the full context of these documents.

Agency policy, as articulated in the Grants Management Fact Sheet for Agency Leaders entitled Competition for Assistance Agreements, Number 9, states that "the Agency **encourages** fair and open competition in the award of **discretionary** assistance agreements." (Emphasis added.) This does not constitute a requirement to do so in the case of every grant awarded. In fact, the Fact Sheet clearly states that "Program Leaders **should determine up-front** if a competitive process **is appropriate** for your assistance program." (Emphasis added) Further, the Federal Grant and Cooperative Agreement Act of 1977 "encourages competition, **where**

appropriate, in the award of grants and cooperative agreements.” (Emphasis added.)

The Program Leader and the Project Officer in this case made a determination that there was adequate justification for non-competition of this award, based upon the extensive file documentation including the draft, 50-page Feasibility Report, many months of consultations and research, and two levels of management review within the Region. It was typical and customary for the Region to accept concise justifications for grants awarded without formal competition. This grant well exceeded the normal standard for such justifications. We therefore request that these statements in the report be modified to show the entire policy in its correct context, and not just selected portions of it. We further request that you modify these statements to reflect the discretionary nature of this determination and the degree of judgment involved..

Citing Executive Order 12674, Principles of Ethical Conduct, the report asserts that Region III did not act impartially and without preferential treatment to an organization or individual. At the time of grant award, the Region was not aware of any other eligible and interested prospective grantee, after months of extensive consultations and research conducted by the Feasibility Workgroup and by Region III independently. The Metropolitan Washington Council of Governments (COG) had not expressed interest in continuing this grant at that point. Therefore, EPA could not have acted in preference to one organization at the exclusion of a known, alternative option. There are no assertions of personal friendship or association in the report. Further, no one in EPA directly benefitted from any of these actions. Therefore, this assertion that Region III officials did not comply with the Principles of Ethical Conduct is incorrect and should be deleted in its entirety.

Response to Audit Recommendations

Based upon our reading of the Draft Report, we offer the following summary of EPA Region III responses to the recommendations:

Recommendation 2-1: Terminate the Existing Cooperative Agreement Awarded to the CCC

The Region agrees that the existing cooperative agreement should be brought to an end and be replaced by a new grant arrangement as determined by the outcome of a competitive Request for Proposals (RFP). It is critical to maintain LGAC and other project support, and a precipitous action to replace it could lead to the same issues of non-competition raised by the Inspector General. We will transition to the successful candidate(s) under the new RFP on or around August 1, 1999.

Recommendation 2-2: Award a New Cooperative Agreement Competitively

Concur: The Region has taken steps to compete the local government assistance functions consistent with an overall Bay Program management plan. By taking such action, the Region does not indicate concurrence that the initial justification for non-competition was inadequate.

Recommendation 3-1: EPA Should Obtain LGAC Services Directly

The Region has agreed to a future limit on the amount of contracting under Cooperative Agreements for this and similar Bay Program efforts. We have done this by specifying

evaluation criteria under the RFP which promote work being done in-house by prospective grantees.

Recommendation 4-1: Recover Costs Associated with a Verbal Agreement

This finding should be directed to the grantee. We will review the grantee's response, and defer any action on the Recommendation in the interim.

Recommendation 5-1: Discontinue Payments

Concur: The Region discontinued payments on the cooperative agreement in a letter of November 19, 1998. Based upon a thorough on-site review of the financial management systems of the CCC conducted on December 3-4, 1998, we have resumed payments in accordance with requirements of the Grant Agreement.

Recommendation 5-2: Pre-Award Review of Fiscal Accounting Systems

Concur in Part: At the time of application for cooperative agreements, grantees provide certifications that they will maintain adequate financial records. The Region will continue to require and review all grantee financial management system certifications as part of its review of applications. We can not perform in-depth site reviews of all grantee records before authorizing payments. This would result in delays in payments and would be counter to the Prompt Payment Act provisions.

Response to Exhibits A and B of the Draft Report

Exhibit A: Analysis of Expenditures by the CCC

The Regional Grants and Audit Management Branch conducted a site review of the CCC's financial management system and financial records. From this review we have obtained supporting documentation for the \$73, 261 which the audit cites as unsupported. A copy of our financial systems review is being forwarded under separate cover. We defer response on the two specific issues in Exhibit A to the grantee and contractor.

Exhibit B: Costs Claimed by the Contractor

Defer to Grantee or contractor's Response.

We request that you consider all the changes we have suggested in the final report so as to ensure a fair presentation of the facts and to provide the most useful response to the Local Government Advisory Committee. We also request an exit briefing before the issuance of the final report for the purposes of securing an explanation of how our comments have been addressed.

If you have any questions or need any additional information, please contact Robert G. Reed, Jr., Chief, Grants and Audit Management Branch, on 4-5410 or Robert J. Picollo of his staff on 4-5405.

cc: Nikki Tinsley

Appendix 2 - CCC's Response to the Draft Report



January 8, 1999

Mr. Carl A. Jannetti
Divisional Inspector General for Audit
United States Environmental Protection Agency
Office of the Inspector General, Mid-Atlantic Division
1650 Arch Street
Philadelphia, PA 19103-2029

Re: Draft audit report on the Center for Chesapeake Communities (CCC)

Dear Mr. Jannetti:

This letter is our response to chapters 4 and 5 of the Draft Report enclosed with your letter dated November 20, 1998. We trust that the comments and points made herein will be reflected in the final report when issued.

Before I make a number of substantive points about the Draft, I believe it is important to note several contextual circumstances which materially affect some of the judgments made in the Draft and which serve as background for the facts asserted as a result of the review on which the Draft Report is based. These contextual observations were not specifically highlighted in the Draft but are relevant to its interpretation.

Context

First, the Center for Chesapeake Communities (hereinafter the "Center" or "CCC") was in the process of "starting up" during the period prior, during and after the review was carried out. Every one of the "systems" and much of the documentation noted in the report were in the process of being created. As will be mentioned later, these systems are now in place, the documentation then being developed is now present. I believe it is unreasonable to believe that any new organization would have all systems, policies, manuals, etc. fully developed in the first eight months of its existence. The Report fails to note that the required systems were under development with a payroll system, tax reporting and payment, accounting system and policy manual all initiated prior to the review and now fully in place.

Second, the Report fails to note why the creation of certain systems were delayed and why the Executive Director sought and received critical volunteer help from knowledgeable, skilled and trusted persons.

Mail
209 West Street, Suite 201, Annapolis, MD 21401

Phone Numbers
410-267-8595, Fax: 410-267-8597

During early December, 1997, less than one (1) month after receipt of the first funds, I began to experience severe health problems, making it difficult to eat, and difficult to walk distances greater than 100 yards. Preliminary tests, as well as a visit to my doctor over the Christmas holiday indicated several possible problems. Immediately after the New Year (1998), I was in the emergency room for tests as a result of persistent chest pains and very high blood pressure. At the doctor's request, my activities were reduced, and a stress test ordered. The test, carried out over a little more than a week later, indicated a severe blockage of the blood supply to my heart and the necessity for a heart bypass operation as soon as it could be scheduled, in addition to an angioplasty. These were scheduled for early February, 1998 on consecutive days. I was advised not to resume activities for two to three weeks after the surgery, and then only gradually. Thus, during the period from December through March, 1998 my attention to Center start-up was secondary to these extraordinary health issues. During this period, in order to carry out the required development, preparation and distribution of documents and systems, I requested and received needed volunteer help where necessary and delayed as much as possible.

Third, the Draft Report fails to acknowledge that the Center Director provided complete access to all Center files, checks and records. When the review was carried out, fewer than 50 checks had been written, all receipts had been filed by month, and a payroll system fully implemented. Copies of these records were provided. The Center's largest expenditure, fully consistent with the authorized grants and funds then received, was my salary. Until May, 1998, I was the only employee. It was easily verified then, and has since been reviewed and verified by EPA Grants and Audit Staff, that the salary and benefits paid to me were both appropriate and consistent with the budgets submitted to EPA. The percentages cited in the Draft Report concerning payments to me are accurate but easily misleading since during all but the last 30 days of the entire period of September, 1997 to April, 1998 the bulk of all the funds available were for my salary.

Substantive Response - Actions taken prior to receipt of Draft Report.

In the context of these observations, I have always regarded the review undertaken by the EPA Inspector General's office with the utmost seriousness. While I was not aware of the issues identified until the Center received the Report on November 20, 1998, it is important to note that I had already initiated procedures to address the requirements of 40 CFR part 30. The review by EPA Grants and Audit Staff carried out in early December, 1998 in response to the assertion in chapter 5, indicated that Center documentation is fully satisfactory and responsive to those requirements. We believe that CCC is in full compliance with the Financial Management and Procurement systems in 40 CFR part 30.

The following management actions had already been taken prior to the receipt of the Draft Report:

1. Timesheets for all employees including time Distribution Systems by grant for all employees. Timesheets are also on file for Redman Johnston Associates, LTD ("Redman Johnston") for each month.
2. A financial management system was in place with appropriate coding of each expenditure.

3. Generally accepted accounting principles are now followed by the Center. We have current and complete disclosure of financial results for each activity within each grant.
4. We have records that adequately identify source and application of funds for all federally sponsored activities. These records contain awards, authorizations, obligations, unobligated balance and authorized income.
5. We have effectively segmented control and accounting for all funds, property and other assets.
6. All assets are used for authorized purposes.
7. We have written procedures for our work, our staff and our organization.
8. We have on-site full accounting records and source documentation for our work.
9. We have, where appropriate, fully implemented a computerized procedure for our grants and contract work.
10. We have staff in place, all substantive work underway, reported our progress and maintained frequent communication on program issues with EPA staff.
11. We have involved state and local governments in our work and responsibly carried out our agreed tasks.
12. We have a library of applicable federal regulations on site.
13. We have published a manual and distributed it to staff and our Board spelling out compliance requirements of applicable federal regulations and have created detailed employee policies and procedures.
14. All these records were reviewed by EPA Grants and Audit Staff during a two day site visit in December, 1998.

Comments on Draft Chapter 4

Point 1

The incorporation of the Center was undertaken to address needs identified by a work group of the Local Government Advisory Committee ("LGAC"). Mr. Redman offered to assist in this process and to act as agent for the incorporation to assure it would be in place to provide funding for services to local governments. Mr. Redman's involvement was never substantive in the operation of the Center and as the draft points out, he resigned shortly after incorporation. Mr. Redman's office was used as a point of contact because I was not immediately available and the Corporation did not set up a point of contact until early September, 1998.

Point 2

The Draft asserts that a real or apparent conflict of interest exists because the Center awarded two contracts to Redman Johnston. No such conflict existed. The Contractor was also the Executive Director of LGAC and as such was responsible for preparing budgets, developing work plans and securing LGAC approval of these proposals. Mr. Redman was also responsible for their presentation before the Bay Program's Budget Steering Committee. These roles involve full knowledge of the funds available and their purposes for future LGAC work. Interactions between CCC, Bay Program Staff and the Contractor (representing LGAC) was therefore not only normal, it was expected, as part of our responsibility by EPA.

The First Contract

EPA staff was fully aware that I intended to contract with Redman Johnston to provide technical assistance and organizational start-up support to initiate the activities of the Center. I regarded this work in many respects as an extension of the work already completed by Redman Johnston to evaluate the need for and feasibility of a non-profit organization to provide technical and financial assistance to local governments. The actual contract \$9,864 was verbal. However, real and substantive expectations were created, services were provided (EPA staff were fully familiar with this work) and full payment was made with one-third (1/3) paid in April, May and June of 1998. Note that at the time the Inspector General's review was carried out, these payments were not complete. As pointed out in my interview with Inspector General staff, they were delayed because of the grant processing and payment cycle of EPA and my attempt to maintain the continuation of my own salary when the delays occurred.

I was not aware I needed a written agreement for these services since clear expectations concerning the work were known by all concerned (myself, Mr. Redman and EPA staff). This work was fully authorized by the start-up grant awarded to the Center.

The Draft Report asserts an application dated July 30, 1997 was submitted by CCC for services which covered incorporation and other services to create the Center. No such application was submitted. I have not seen such an application. I know these costs are not appropriate for a federal application. The application submitted in my name in early August, 1997 (I was in North Carolina and authorized Mr. Redman to sign my name) was the only application submitted, and as mentioned above, it did seek assistance for only the following activities involving the formation of the Center. These activities included delegation meetings with LGAC members, development of information about the LGAC non-profit work group, identification of potential funding sources in part to address LGAC concerns that such sources existed, and development of informational materials on the new organization for LGAC members and Bay Program signatories.

This is the work that the first cooperative Agreement dated September 30, 1998 authorized. EPA staff were fully aware of our agreement with Redman Johnston to provide these services and I believe approved the agreement to secure them from Redman Johnston. We believe 40 CFR 30 parts 43 and 44 do not prohibit our verbal agreement to a contract in this amount since clear expectations existed, services were performed based on these expectations, an invoice was rendered and reviewed by CCC and EPA staff prior to payment and full payment made based on the work completed.

The Second Contract

The Draft Report asserts that a second contract for \$155,000 was a "done deal" based on the review carried out by Inspector General Staff. I believe neither the facts or the Draft support such a conclusion. The Center did use the Request for Qualification ("RFQ") process to select a contractor. This process was identical to that conducted by the metropolitan Council of Governments (COG) in previous years, including as recently as 1996. I consulted extensively with COG staff about their process and obtained complete copies of the documentation used. The CCC process was designed to copy that process. We used the RFQ process as COG did

and the same contractor list and evaluation procedures. EPA had found these procedures acceptable in the past and I saw no reason to change them, particularly in light of my health issue in January and February, 1998 when this process was being implemented. Redman Johnston was not the assured awardee.

Eighteen firms were sent the RFQ. I reasonably believed all eighteen firms received the RFQ since none were returned. Inspector General staff verified that at least six acknowledged receipt. Even this number is sufficient to assure competition. Two firms responded to CCC - Redman Johnston and the SoHo group. The SoHo group requested a meeting prior to their submission of a response to the RFQ. After a short delay because of my heart surgery, the meeting was held in my office in Annapolis on February 24, 1998. I outlined the evaluation procedure, including additional points for a minority-owned business (which SoHo was) and encouraged them to respond. At the time, they indicated they would. Up until the day the final submission was due, I fully expected at least two qualifying bids and was prepared to set up a review committee, consisting of a member from each of the signatory jurisdictions. Such a procedure was not used because the SoHo group called 2 hours before the deadline and indicated, based on their review of Redman Johnston's work, qualifications and experience, they did not believe they could be competitive. The CCC received only one (1) qualified response; that was from Redman Johnston. Their name was submitted to the LGAC Executive Committee, which approved the contract award in early March, 1998.

At no time did I regard the award as a "done deal". Had additional qualifying responses been received, they would have been fairly and objectively evaluated by parties other than myself.

It is noted in the Draft that the list of RFQ recipients was obtained from Redman Johnston. Mr. Redman's response indicated why this occurred.

The Draft Report indicated Mr. Redman preferred an RFQ process. The report does not mention the RFQ process was the one used by COG which is why the CCC used it. The draft report mentions a draft budget titled Draft 2, dated September 11, 1997 concerning the budget being developed for LGAC activities and CCC work. I believe it was entirely appropriate for Mr. Redman to review this documentation in light of his role with LGAC and his responsibility to present the budget to them and to the Budget Steering Committee as part of the process then being carried out by the Bay Program.

The Draft notes the application for assistance was faxed from Redman Johnston's office on December 16, 1997. I was in New Orleans at an EPA meeting and asked a Redman Johnston staff member (without Mr. Redman's knowledge) to submit the application based on text I had reviewed and approved since the staff member had a copy of the application form on disk and I did not have such materials. After keying in the text I had approved on the form, he forwarded it to EPA. During this period, late January and February, 1998, I was in the hospital recovering from surgery. Work needed to be done during this period to meet EPA deadlines and I asked a skilled and trusted person to volunteer and carry out these activities to assure the continuity of work and funding.

The Draft asserts that the Contractor, Redman Johnston, had detailed knowledge of the RFQ specifications and requirements, etc. The LGAC process and Bay Program procedures provide that this knowledge be widely shared with LGAC members and the Bay Program staff. This does not provide competitive advantage since the same information is provided to all potential bidders as part of the RFQ process. Redman Johnston's advantage is the excellent quality of their work and their reputation as a firm. CCC procurement records clearly indicate Redman Johnston was the only qualified bidder. The contract award amount was fixed by the RFQ. LGAC was informed that another bidder had dropped out for the reasons mentioned earlier. Therefore, only one bidder was recommended to LGAC. Our records are sufficient to show these were the facts. EPA staff were fully aware of these facts. These facts were sufficient for a contract award and no change was made to the cost of the contract since it was approved by the LGAC Executive Committee.

Much is made in the Draft about written statements of conduct for employees awarding or administering contracts. The Center now has such standards. We also now have more than one employee. At the time the award was made, I believe it was competitively done. There was no assurance Redman Johnston would prevail based on the Center's process, which was modeled after a process conducted by an organization which does have such standards.

Chapter 5

Point 1

Earlier I indicated that CCC does have an adequate financial management system. This has been verified by the review carried out by the EPA Staff in early December, 1998. I also indicated that a number of actions initiated prior to the Inspector General review were not concluded until after the Inspector General's review.

Point 2

The Draft asserts that the Executive Director disregarded the detailed budget when funds were expended. This is not the case. Rather, close attention was paid to these budgets and EPA requirements when these expenditures were made. The CCC did employ a Redman Johnston employee on a consulting basis during late March and early April, 1998 because help was needed to address critical grant and EPA requirements. The items cited in the Draft footnote are in error and misleading. No funds were paid to anyone for the development of an application for a Sustainable Development Challenge Grant. This application was submitted in August, 1997.

I did secure help to (1) develop a final draft of a training program required by our start-up grant, (2) provide copy of the small water shed grant required by EPA Bay Program Budget Steering Committee, (3) consult on a draft memo to the Governor of Maryland on the Summit required by our grant, (4) consult on the configuration of office equipment for a new Center office, (5) consult on the content of a draft brochure for the Center (again required by our grant), and (6)

respond to certain technical questions from EPA Grants and audit staff on our budgets for ongoing and proposed work.

All of these activities are authorized by our grant from EPA. The individual involved had knowledge and skills I believed were essential to our work and I had no other staff to draw on and could not, in good conscience, continue to constantly ask for such enormous time commitments for free.

Point 3

As indicated earlier in this response, the exact amounts cited in this chapter setting forth payments to me are not disputed. Rather they are entirely consistent with my authorized salary for the period cited and the health, life and retirement contributions are also consistent with the authorized budget. The reimbursements are consistent with actual costs documented for this same nine (9) month period. The \$9,000 in vendor costs reflecting the equipment ordered and now in use in our offices is fully consistent with our authorized budget for such costs as amended in March, 1998.

Point 4

Board meetings were documented, EPA Staff was present. IG Staff had access to copies of the agenda and other supporting materials in the files provided at the time of their visit. Minutes were not available.

Point 5

The Executive Director did maintain a detailed personal calendar. Timesheets for employees were not introduced until more than one employee was on staff. My time was, at the time of the review, covered by only one grant from one source. No distribution by activity seemed necessary. Copies of my calendar were not requested.

Point 6

The advance payment method is used and has been continued subsequent to the review by EPA Staff in December 1998. Our documentation is responsive to the EPA's Assistance Administration Manual.

Point 7

We fully believe our expenditures are supported based on the facts cited in our response and the review carried out by EPA Staff in December, 1998.

Point 8

We believe the verbal contract with Redman Johnston was valid, consistent with the cooperative

agreement, and approved by EPA.

Point 9

The Consulting Agreement referred to in footnote 2 of the Draft was fully consistent with the Cooperative Agreement. Note the actual activities addressed as identified in this response.

Point 10

Your Draft included 2 Exhibits, A & C. No Exhibit B was included.

Conclusion

Since the Center's incorporation, I have worked to build the independence, credibility and reputation of a new non-profit to serve the interest of local governments in the Bay Watershed. This organization was created to respond to real needs identified by these governments. EPA Staff are well aware of these facts. However, some individuals in the Region hold strong views concerning both the Federal Rules in clean water policy and any non-profit organization that seeks to partner with local governments to assist them in addressing Chesapeake Bay protection and restoration objectives. Their questions and suspicions led to the invitation which I supported for the review by your office. We have consistently tried to be cooperative with the review. I regret any shortcomings in our start-up which may have led to the assertions contained in the Draft. I hope you will agree these were not inconsistent with the start-up of many new enterprises.

I deeply hope the facts provided by Mr. Redman and myself go far in addressing your concerns. It would indeed be regrettable if the final report did not fully reflect these facts and on balance seemed to reinforce the prejudice of a few and undermine the credibility of our organization before it renders even the first full year of service. It is my hope the final report will fairly represent all the facts and not create a cloud of suspicion from which we cannot emerge.

It is important to note that at all times the Center and its employees acted in good faith with the intent to comply with relevant Federal regulations. No abuses occurred, and all funds received by the Center have been appropriately accounted for. All actions taken by the Center were taken in a manner which accomplished the stated objectives of the program without abusing procedures, and perhaps most important, EPA, the Federal agency responsible for the program, was constantly consulted by the Center's Executive Director to ensure that the Center was properly established, that the start-up obligations were accomplished and that the resources available to the Center were handled properly. If it is to be concluded that in some of these initial activities there may have been some lack of swift or strict adherence to Federal regulations, it is clear that there was no inappropriate activity and that any procedural or recordkeeping deficiencies have been corrected. We hope the Inspector General's report will concur with these observations.

Sincerely,

A handwritten signature in black ink, appearing to read "Guy C." followed by a stylized, cursive flourish.

Appendix 3 - Redman/Johnston Associates Response to the Draft Report



REDMAN/JOHNSTON ASSOCIATES, LTD.

Comprehensive Planning - Community Development - Environmental Resource Management

December 22, 1998

Mr. Carl A. Jannetti
Divisional Inspector General for Audit
United States Environmental Protection Agency
Office of the Inspector General, Mid-Atlantic Division
1650 Arch Street
Philadelphia, Pennsylvania 19103-2029

Re: Draft audit report on the Center for Chesapeake Communities (CCC), Report Number E6DEP8-03-0014

Dear Mr. Jannetti:

Please consider this letter as the draft written comments to the draft audit report you requested in your letter dated November 20, 1998. Please note that these comments are in response, only to the two pages of the draft audit report received from your office with the letter dated November 20, 1998. I will respond in a separate letter to the issues raised in Chapters 4 and 5 of your draft report, which were not provided with your November 20th transmittal. To the extent there is a final audit report which varies the draft report you provided, I reserve the right to make a further response.

One of the pages submitted to me (unnumbered), titled "Contractor's Costs Unsupported" suggests that RJA did not have an "adequate financial management system" because "our personnel did not use time sheets or any mechanism to support actual hours charged to the contract". As you know, RJA and the Metropolitan Washington Council of Governments ("COG") entered into a contract ("Contract") on April 28, 1997, which is the subject of your draft report. RJA fully complied with the terms of the Contract.

Point #1

As I indicated to your field investigation team during their visit at our offices, RJA has been a contractor with the Metropolitan Washington Council of Governments for three years prior to the subject contract. At no time during those contracts was our record keeping and billing procedure questioned. Throughout the period of our relationship with COG, and in conformance with the Contract between RJA and COG, Section 2.b., RJA requested each payment on an invoice form, upon the completion of each task, or a portion thereof, describing the work performed and the period of performance of the work being invoiced. RJA sent invoices in strict compliance with the language of the Contract. The Contract does not mandate that RJA

keep time records as a condition for payment. None of these invoices were ever questioned by COG or EPA administrative officials. Each invoice was prepared mindful of the need to complete all work identified in the contract scope of services and to do so within budget. RJA completed all tasks and assignments defined in our Contract work program on time and within the Budget set forth under Section 2.a. of the Contract. That was what COG expected, and that is what RJA accomplished. Time and materials billings were not contemplated.

Point #2

Although the phrase "time and materials" is used in Section 2.a. of the Contract, a review of the contractual language as a whole reveals that the Contract is not a typical "time and materials" contract as defined by the Federal Acquisition Regulations, but is more characteristic of a "fixed fee" contract. Specifically, the Contract did not specify a fixed hourly rate, which is required for "time and materials" contracts under the Federal Acquisition Regulations. 48 C.F.R. 16.601(a) provides that "[a] time and materials contract provides for acquiring supplies or services on the basis of (1) direct labor hours at specified hourly rates that include wages, overhead, general administrative expenses, and profit and (2) materials at cost, including, if appropriate, material handling costs as part of material costs." Reading the contract as a whole, including the 20 pages of the Contract which specifically define tasks, and the specific budgets allocated to the tasks, the payment schedule is more characteristic of a "fixed fee" contract, in which the contractor receives payment based on completion of each task, as opposed to a "time and materials" contract in which the contractor is paid at specified hourly rates.

The Federal Acquisition Regulations also provide that "[a] time-and-materials contract may be used only when it is not possible at the time of placing the contract to estimate accurately the extent or duration of the work or to anticipate the costs with any reasonable degree of certainty." 48 C.F.R. 16.601 (b). In this case, RJA and COG were able to estimate both the extent and duration of work. Section 3 of the Contract states that the "period of performance under this Contract is from March 16, 1997 through March 15, 1998." The Contract set forth specific and identifiable tasks to be performed in the one year time period, and assigned budgets for each task.

Although Section 2.a. of the Contract indicates that the contractor shall be paid on a time and materials basis an amount not to exceed \$204,000, it further indicates (in the same sentence) that payment shall be made in accordance with the scope of work and budget reflected in Contract Attachments A and B (Scope of work and budget). These two attachments represent over 20 pages of the contract that define our responsibilities for completion of tasks and assign a budget for each task. We viewed the Contract as a fixed price contract, and understood that we would be paid the budgeted amount for the work performed. At no time has anyone provided any indication that we did not complete all elements of the scope of services for which we were engaged during the period March 1997 to March 1998, or that we exceeded the budget established for the many tasks defined in the contract.

The draft audit report indicates that it is your opinion that "a time and materials contract is the least preferred contract type and should be used when no other type is suitable"..... since "according to 48 CFR 16.601, a time a materials contract provides no positive profit incentive to the contractor for cost control or labor efficiency and therefore, oversight of contractor performance is required". I agree.

Both RJA and COG considered the Contract a "fixed price" contract, or a lump sum contract which is reflected in both the monthly invoicing under the terms of the Contract and the manner in which our work was conducted. 48 C.F.R. 16.202-1 describes a "firm fixed price contract as a contract which:

...provides for a price that is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract. This contract type places upon the contractor the maximum risk and full responsibility for all costs and resulting profit or loss. It provides maximum incentive for the contractor to control costs and perform effectively and imposes a minimum administrative burden upon the contracting parties.

As I indicated to your review team, in many cases my invoices reflecting staff time committed to performance of services under this contract account for less than the actual time require to complete various aspects of work. In most cases, I found that staff time to complete many of the contract specific work assignments was greater than amounts budgeted. In those cases, when preparing invoices for our work, I did not submit invoices for additional staff hours devoted to these assignments because it was our belief that we were committed to complete the assignments and provide the products defined in the scope of work for the prices defined in the contract. We assumed that any additional time it might take to complete those elements was not billable. RJA did not bill for any costs or time over the agreed upon amounts, and treated the Contract as a fixed price contract.

Given the fact that only 3 words in the entire body of the contract and attachments references the fact that the contract was a "time and materials" contract and the fact that the contract does not specify hourly rates, and fully 25 pages of the document characterize work to be performed and budgets allocated to each work item, I have a great deal of trouble characterizing the contract as simply a "time and materials" contract. Both parties treated the Contract as a "fixed price" or lump sum contract, in which payment was made upon documentation of completion of specific tasks as defined under the Contract. It is undisputed that RJA in fact performed the tasks set forth in the Contract within the specified times. EPA administrative staff who monitored my performance of Contract responsibilities during the period March, 1997 to March 1998 have never indicated any failure on the part of my firm to complete Contract assignments and do so within the price structure defined in the contract.

Point #3

Your finding that all costs associated with this Contract are unsupported is quite surprising given the fact that I provided audit team members copies of products, (reports/documents) reflecting completion of many of the tasks which were budgeted in the Contract (see Contract attachments A and B). For example, the Contract provided for:

- preparation and distribution of four quarterly newsletters at a budget of \$12,250; and
- preparation of a pollution prevention toolkit (book publication and brochure) at a budget of \$25,000; and
- Preparation of a literature synthesis regarding the costs of sprawl and related pamphlets at a budget of \$5,000.

Each of these assignments was completed during the contract year and tangible work products in the form of reports, publications, or copies of the newsletters were made available for your review. It would therefore seem appropriate to credit these items as costs that are supportable in Exhibit B (the second and only other page of the report I received). Quite frankly, it seems unreasonable for you and your staff to indicate in your report that absolutely none of the costs during the year are supportable in the face of clearly visible products.

Point #4

Note #2 on Exhibit B of the draft report indicates that all costs associated with preparing the feasibility study for creation of a non-profit organization should be disallowed. The language in the note is confusing and may be a result of confusion on the part of the investigators. There is a distinct difference between "preparing the feasibility report" and "establishment of the nonprofit entity". Work done to prepare the feasibility report was authorized in attachment 2 to my contract with COG. (See page 2-1 attachment 2 to the contract scope of work) In fact, this work item was budgeted in the amount of \$6,500. Unfortunately the level of effort required to explore the feasibility of creating the Center, did not satisfy some LGAC members who expected to see a detailed report. The need for the detailed report and additional related work performed regarding start up for the Center was discussed with EPA staff and additional work was approved by EPA as an extra. At that time it was understood that the estimated cost to complete the work would be \$10,000. Rather than process a contract amendment through the Metropolitan Washington Council of Governments, EPA staff recommended that I receive compensation from the \$45,000 initial grant to be made to the Center. I accepted that arrangement and performed the work accordingly. Therefore it does not seem reasonable to disallow costs associated with preparation of the feasibility study since I was contractually obligated to complete this task within the scope of work. On the other hand, the action to establish the nonprofit entity was not within the scope of work and our firm has made no request, nor do we intend to request reimbursement of any expenses associated with the "establishment of the nonprofit entity."

Page 5

Point #5

In closing, please be advised that since April of 1998, we have adjusted our administrative procedures as a result of your audit team's visit to our offices. Their visit provided me with the first clear indication that our contract administrative procedures required us to maintain daily time records of our work. Since that time, personnel at RJA have been required to keep time sheets for all work related to LGAC assignments. These time sheets now accompany our monthly invoices to the Center for Chesapeake Communities.

Sincerely,

A handwritten signature in black ink, appearing to read "Anthony D. Redman". The signature is fluid and cursive, with the first name being the most prominent.

Anthony D. Redman
Redman/Johnston Associates, Ltd.



REDMAN/JOHNSTON ASSOCIATES, LTD.

Comprehensive Planning - Community Development - Environmental Resource Management

December 23, 1998

Mr. Carl A. Jannetti
Divisional Inspector General for Audit
United States Environmental Protection Agency
Office of the Inspector General, Mid-Atlantic Division
1650 Arch Street
Philadelphia, Pennsylvania 19103-2029

Re: Draft audit report on the Center for Chesapeake Communities (CCC), Report
Number E6DEP8-03-0014

Dear Mr. Jannetti,

I have been provided with copies of Chapter 4 and 5 of the above draft audit report. This letter is intended to address the matters set forth therein which relate to Redman/Johnston Associates, Ltd.

The first page of Chapter 4 in your report alleges that the Executive Director of the CCC "acted favorably toward Redman/Johnston Associates by awarding it, for all intents and purposes, two sole source contracts after Redman/Johnston Associates absorbed costs totaling \$2,300 for incorporating the CCC."

This conclusion is incorrect. There is a current contract with the Center for Chesapeake Communities (CCC) dated March 31, 1998, which was awarded to RJA after a bid process in which RJA was not involved, except as bidder.

It is correct that I spearheaded the incorporation of the CCC. I agreed to do that at no cost to the EPA, whose representatives advised that absent incorporation, they could not provide an initial grant to support the start-up activities of the Center. Please keep in mind that at that time the Metropolitan Washington Council of Governments (COG) staff had indicated they would withdraw future sponsorship of LGAC funding and that they supported the CCC assuming responsibility for future grants that would support the ongoing activities of the Local Government Advisory Committee (LGAC). The EPA representatives indicated that if a nonprofit corporation was formed, they would continue to fund LGAC activities through the CCC. My actions to create the non-profit were designed to protect LGAC access to financial resources to support

their ongoing activities. Since RJA's role as a contractor to the LGAC is subject to change each year based on a competitive selection process, there was never any assurance that incorporation of the Center would financially benefit RJA. In fact, RJA has sustained a substantial reduction in the dollar volume of services we provide on behalf of the LGAC since the Center now receives a portion of the LGAC's budget to provide many of these services.

As you indicated in your report, I signed Mr. Allen's name on certain application paperwork, and in so doing included my initials since I was signing requisite application forms on his behalf. Your report should note that Mr. Allen expressly authorized and directed me to submit the grant application in his name. My initials following his name were intended to make it perfectly clear that I had affixed a signature on his behalf as applicant.

You are correct that at the time CCC was incorporated, I was listed as a Director. Before there were any Board of Directors meetings or any Board action, I resigned as a Director on September 23, 1997. I never actually served as a Director, and was a Director in name only for purposes of the initial incorporation.

There is a comment in the draft audit report suggesting that it was somehow improper for me to be personally aware of future grant availability. That was my job with LGAC - to prepare budgets based upon anticipated grant funding. There is nothing improper about that process. With respect to the comment in Chapter 4 that RJA benefitted from the grant ultimately made to the CCC, it is accurate that there was an addendum to an existing contract which resulted in additional work, and additional revenue (\$9,894.00) to RJA, which was funded through a grant which I assisted the Center in preparing.

In Chapter 4/page 3 of the report you describe the actions taken to amend the cooperative agreement dated March 2, 1998 which awarded funding in the amount of \$314,000 to the Center of which \$155,000 was to fund the contract for services to the LGAC. You characterize this award of \$155,000 to my firm as "a done deal". In fact the report asserts "in our opinion, documentation in EPA's, the CCC's and Redman/Johnston Associates' files indicated the award of this contract was a done deal". While this is an interesting opinion, it is incorrect as far as I know. Although I had served for several years as contractor to provide support services to the LGAC, I received a request for qualifications and submitted a proposal to provide these services as part of what I understood to be a competitive contractor selection process. Please note that I had foreknowledge of the amount budgeted for LGAC activities for that year since I had prepared LGAC's budget request several months before the selection process took place. As I indicated earlier, I have prepared the LGAC's budget request on behalf of the Committee for the past five years as part of my contractual obligations to provide administrative support services to the organization. Without a budget they would be unable to function from year to year. Moreover, the budget request I prepare on their behalf each year is reviewed and approved by the LGAC members.

On page 4 in Chapter 4 you note that when you initially requested the list of firms that were mailed the RFQ, the list was faxed from my offices to the Executive Director of the CCC who in turn faxed it to you. I have never seen such a list. I can assure you it has never been in my personal possession.

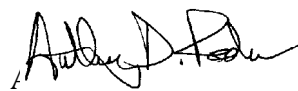
In investigating this circumstance, I have learned that you requested this list from Mr. Allen, who requested a former employee of mine (the same one that now works for the Center) to obtain a copy on his behalf from the Metropolitan Washington Council of Governments. Apparently, he obtained a copy for COG and forwarded it to the Center without my knowledge. I recognize that he was an employee of my firm at that time, nevertheless, I repeat, I never had any indication that such a list was ever in my offices and to this day have never seen such a list. In fact, it appears that the only reason such a list was ever in my office at all was because you requested it of the Center, and at Mr. Allen's request, my employee became a transmittal middle man, after the contract was awarded, I should add.

The second bullet located in Chapter 4 on page 5 of the report describes a proposed budget titled "Draft 2" that was faxed from my office to the CCC on September 11, 1997. You note that this was six months before the contract was awarded. The draft you saw was prepared at the request of the Director of the Center to assure funding would be set aside for LGAC activities during the coming year. As I have already indicated, preparing the LGAC's budget for the coming year is part of my contract administrative obligation to the LGAC.

Chapter 5/page 1/last paragraph of the report indicates the CCC "paid one employee of Redman/Johnston Associates \$1,500 for preparing proposals in order to apply for two other grants". Redman/Johnston Associates provided some support in the preparation of the Sustainable Development Challenge Grant application. This assistance was limited since our contract at that time made no provision for compensation for such work. However, at no time was I aware of any arrangement between the Center and the employee to be compensated in the amount of \$1,500 for preparing these proposals. Such action was never sanctioned by RJA, nor did RJA receive any income for this work. This apparently was an arrangement between my about-to-be-former employee and his prospective employer. It was not an arrangement with RJA.

Please advise if additional comment is necessary.

Very truly yours,



Redman/Johnston Associates, Ltd.

Appendix 4 - Distribution

Office of Inspector General (2410)

Regional Office

Regional Administrator (3RA00)

Director, Chesapeake Bay Program Office (3CB00)

Deputy Director, Chesapeake Bay Program Office (3CB00)

Office of Assistant Regional Administrator for Policy and Management (3PM00)

Audit Follow-up Coordinator (3PM70)

Office of Communication and Government Relations (3CG00)

Headquarters

Assistant Administrator for Administration and Resources Management (3101)

Assistant Administrator for Water (4101)

Comptroller (2731)

Director, Office of Grants and Debarment (3901R)

Director, Grants Administration Division (3903R)

Director, Office of Acquisition Management (3801R)

Director, Office of Regional Operations (1108)

Associate Administrator for Congressional and Intergovernmental
Relations (1301)

Associate Administrator for Communications, Education, and Media
Relations (1701)

Deputy Associate General Counsel, Finance and Operations Law Office (2377)

Agency Follow-up Official (2710)

Agency Follow-up Coordinator (2724)

External

Local Government Advisory Committee (LGAC)

Center for Chesapeake Communities

Redman/Johnston Associates

Landmark Legal Foundation

Metropolitan Washington Council of Governments (COG)