



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Special Review

Minnesota Grants Administration



Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota State government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

The division has a staff of approximately fifty auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

Consistent with OLA's mission, the Financial Audit Division works to:

- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

Through its Program Evaluation Division, OLA conducts several evaluations each year and one best practices review.

OLA is under the direction of the Legislative Auditor, who is appointed for a six-year term by the Legislative Audit Commission (LAC). The LAC is a bipartisan commission of Representatives and Senators. It annually selects topics for the Program Evaluation Division, but is generally not involved in scheduling financial audits.

All findings, conclusions, and recommendations in reports issued by the Office of the Legislative Auditor are solely the responsibility of the office and may not reflect the views of the LAC, its individual members, or other members of the Minnesota Legislature.

This document can be made available in alternative formats, such as large print, Braille, or audio tape, by calling 651-296-1727 (voice), or the Minnesota Relay Service at 651-297-5353 or 1-800-627-3529.

All OLA reports are available at our Web Site: <http://www.auditor.leg.state.mn.us>

If you have comments about our work, or you want to suggest an audit, investigation, evaluation, or best practices review, please contact us at 651-296-4708 or by e-mail at auditor@state.mn.us



OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Pamela Wheelock, Commissioner
Department of Finance

David Fisher, Commissioner
Department of Administration

We have conducted a special review of state grants. During the 2000–01 biennium, Minnesota spent over \$13.9 billion in state dollars through grants and aids to local governments, school districts, other governmental organizations, and non-governmental organizations. This review focused on approximately \$550 million of grants that state agencies paid to quasi-governmental and non-governmental organizations, including non-profit organizations. The special review addressed the following questions:

- Has the state developed an adequate system for managing grants?
- Did state agencies use appropriate methods for awarding and monitoring grants?
- Did state agencies comply with applicable legal requirements when expending grant funds?

We conducted this audit in accordance with *Government Auditing Standards*, as issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of management controls relevant to the audit. The standards require that we design the audit to provide reasonable assurance that the state's management complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. The state's management is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

This review was a joint project between the Financial Audit and the Program Evaluation Divisions of the Office of the Legislative Auditor. We received the full cooperation of numerous state agency heads, grant program staff, and grant recipients during the course of the review. This report is intended for the information of the Legislative Audit Commission. This restriction is not intended to limit the distribution of this report, which was released as a public document on January 31, 2002.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: August 31, 2001

Report Signed On: January 24, 2002

Special Review: Minnesota Grants Administration

Table of Contents

	Page
Report Summary	1
Chapter 1. Introduction	3
Chapter 2. Grant Awarding	9
Chapter 3. Grant Monitoring	19
Chapter 4. The Legislature's Role	29
Departments of Administration and Finance's Response	33

Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

James Nobles	Legislative Auditor
Roger Brooks	Deputy Legislative Auditor – Program Evaluation
Claudia Gudvangen, CPA	Deputy Legislative Auditor – Financial Audit
Jeanine Leifeld, CPA, CISA	Audit Manager
Marla Conroy, CPA, CISA	Director of Investigations
Joan Haskin, CPA, CISA	Auditor-in-Charge
Laura Peterson, CPA	Team Leader
Carrie Meyerhoff	Senior Program Evaluation Specialist

Numerous other Financial Audit Division staff participated in the audit of state agency grant sample items.

Exit Conference

We discussed the findings and recommendations in this report with the following staff of the Departments of Finance and Administration on January 9, 2002:

Department of Finance:

Anne Barry	Deputy Commissioner
Lori Mo	Assistant Commissioner
Mary Bogie	Agency Support Director
Stephanie Andrews	Finance Agency Coordinator
Heather Johnston	Executive Budget Officer

Department of Administration:

Kent Allin	Assistant Commissioner
Paul Stembler	Assistant Director, Materials Management
Julie Poser	Accounting Director
Judy Hunt	Internal Auditor

Special Review: Minnesota Grants Administration

Report Summary

We have conducted a special review of state grants. During the 2000–01 biennium, Minnesota spent over \$13.9 billion in state dollars through grants and aids to local governments, school districts, other governmental organizations, and non-governmental organizations. This review focused on approximately \$550 million of grants that state agencies paid to quasi-governmental and non-governmental organizations, including non-profit organizations. The special review addressed the following questions:

- Has the state developed an adequate system for managing grants?
- Did state agencies use appropriate methods for awarding and monitoring grants?
- Did state agencies comply with applicable legal requirements when expending grant funds?

Key Findings:

- As a general rule, we found that state agencies have attempted to establish open and impartial processes when selecting grant recipients. However, state agencies did not always clearly specify grant objectives and work products. In certain instances, grant contracts were unclear or incomplete. The state should establish general guidelines or requirements for the grant award process, especially in the areas of conflict of interest and cash management. We recommend that the departments of Administration and Finance coordinate these efforts.
- State agencies did not consistently or adequately monitor grantee activity throughout the grant period. In numerous cases, agencies did not independently verify information they obtained from grantees, did not ensure that grantees complied with grant reporting requirements, and did not verify matching funds claimed by grantees. The Department of Finance should work with state agencies to coordinate grantee monitoring and auditing, to provide a mechanism for state agencies to obtain information necessary to assess a grantee's financial environment, as well as its compliance with individual grant requirements.
- Agencies did not always comply with applicable legal requirements when expending grant funds. In some cases, agencies did not pay grantees in accordance with applicable payment terms. In addition, there were inconsistent interpretations of the period of availability for grant funds. The Department of Finance should seek legislation to clarify statutory provisions regarding the availability of grant balances.
- The Legislature can have a significant impact on state grants. Some grant administrative problems could be avoided by more carefully crafted legislation. Many of these problems are unique to individual grant programs and could be resolved by more consultation between legislators and agency staff when drafting new grant legislation.

Special Review: Minnesota Grants Administration

This page intentionally left blank.

Special Review: Minnesota Grants Administration

Chapter 1. Introduction

Each year, the State of Minnesota grants money to a variety of organizations to achieve a wide range of objectives. For example, the state makes grants to support Minnesota theater companies, gambling addiction counseling, snowmobile trail maintenance, and tourism promotion. During the 2000–01 biennium, Minnesota made approximately \$1.1 billion in grants to various types of private and governmental organizations.

In several recent audit reports, we have criticized the way particular grants were administered. In March 2001, for example, we reported serious findings related to a grant administered by the Department of Children, Families, and Learning. That report raised concern among legislators and, in response, we made a commitment to conduct a broader review of state grant management. By reviewing a sample of grants across state agencies and examining the state’s general approach to making and monitoring grants, we hoped to determine whether the state has an adequate system for managing grants. We examined grants made in fiscal years 2000 and 2001.

Simply identifying grants made in those two years proved difficult because the state does not maintain a central list or catalog of grants. In fact, the state accounting system combines grants with aids under a general category called “local assistance.” Further complicating our efforts, we found that state agencies are not consistent in coding grants. As a result, we had to work with agency financial offices and program personnel in an effort to achieve a complete, unduplicated list of grants for fiscal years 2000 and 2001.

We focused on grants the state accounting system categorized as going to either a “non-governmental” or “other-governmental” organization.¹ These grants accounted for approximately \$550 million of the \$1.1 billion in total grants. Generally, these two categories include private non-profit and “quasi-governmental”² organizations. We focused on these grants because, for the most part, the recipient organizations are not subject to all of the control and accountability measures that state agencies and local units of government are required to follow.

¹ However, see our concerns related to recording grant information on the state’s accounting system as discussed in Chapter 3, Finding 8.

² *Minnesota Statutes* do not define “quasi-governmental” organization and the term is subject to some variation in use. Nevertheless, quasi-governmental organizations exist at every level of government. At the state level, the term usually refers to an organization that has a close association with the state and may even have some attributes of a state agency, but is not considered a state agency. In some cases, the state created the organization, but exempts it from certain legal and administrative requirements imposed on state agencies (e.g. Minnesota Technology, Inc.). In other cases, the organization was not created by the state, but it performs a public purpose and is significantly supported financially by the state (e.g. Minnesota Historical Society). There are a variety of organizations at the local level that are often called “quasi-governmental.” Some are created by local governments (e.g. Southwestern Minnesota Opportunity Council, Inc.) and some are created by state law (e.g. Lake Superior Center Authority). They are called “quasi” because they are not a department or division of local government and, in fact, some are structured as corporations. A report by the State Auditor, *Corporations Created by Public Entities* (January 1999) is a good source of information on this type of “quasi-governmental” organization at the local level.

Special Review: Minnesota Grants Administration

To conduct this review, we researched current legal requirements concerning state grants and the guidance provided to state agencies by the departments of Finance and Administration. We surveyed 26 state agency heads concerning their agencies' grant awarding, monitoring, and evaluation processes. We asked agency program managers questions about the nature of their grants and the characteristics of grant recipients. We examined a sample of 50 grants to determine whether the agency and the grantee complied with applicable legal requirements, including any legislative stipulations and the terms of the grant contract. We sent surveys to a sample of the grantees, asking them about their experiences with state agencies. We conducted two roundtable discussions with agency staff and one with legislative staff to gain their perspectives on a variety of topics relating to how the state awards and monitors grants. Finally, we researched grant audit practices in other states and reviewed the literature on grant management.

Audit Limitations

We did not audit individual grantee records, nor did we verify the accuracy or completeness of reports submitted by grantees to state agencies. Instead, we assessed state agency processes for ensuring the accuracy of grantee information.

We also did not assess the effectiveness of the grant programs we reviewed. For example, we did not apply performance measures to the programs to determine how well grants served state goals. Likewise, we did not assess whether granting money to non-governmental organizations was the most efficient and effective way for agencies to provide the desired goods or services. We did not examine the requirements of agency grant application processes for economy and efficiency. We did not assess the costs and benefits of the various methods agencies used, or the burden on grantees to create grant proposals. Nor did we evaluate the state's role as a recipient of grant money from the federal government and private foundations.

Finally, we designed our audit work to provide reasonable assurance about compliance with laws and regulations significant to the special review. However, this review was not intended to, nor would it necessarily, discover all instances of noncompliance with grant laws and contracts. Within this report, we have reported all material instances of noncompliance we found during the review. We also sent closure letters, in which we communicated all detailed instances of noncompliance uncovered during our testing, to individual agency heads.

Background

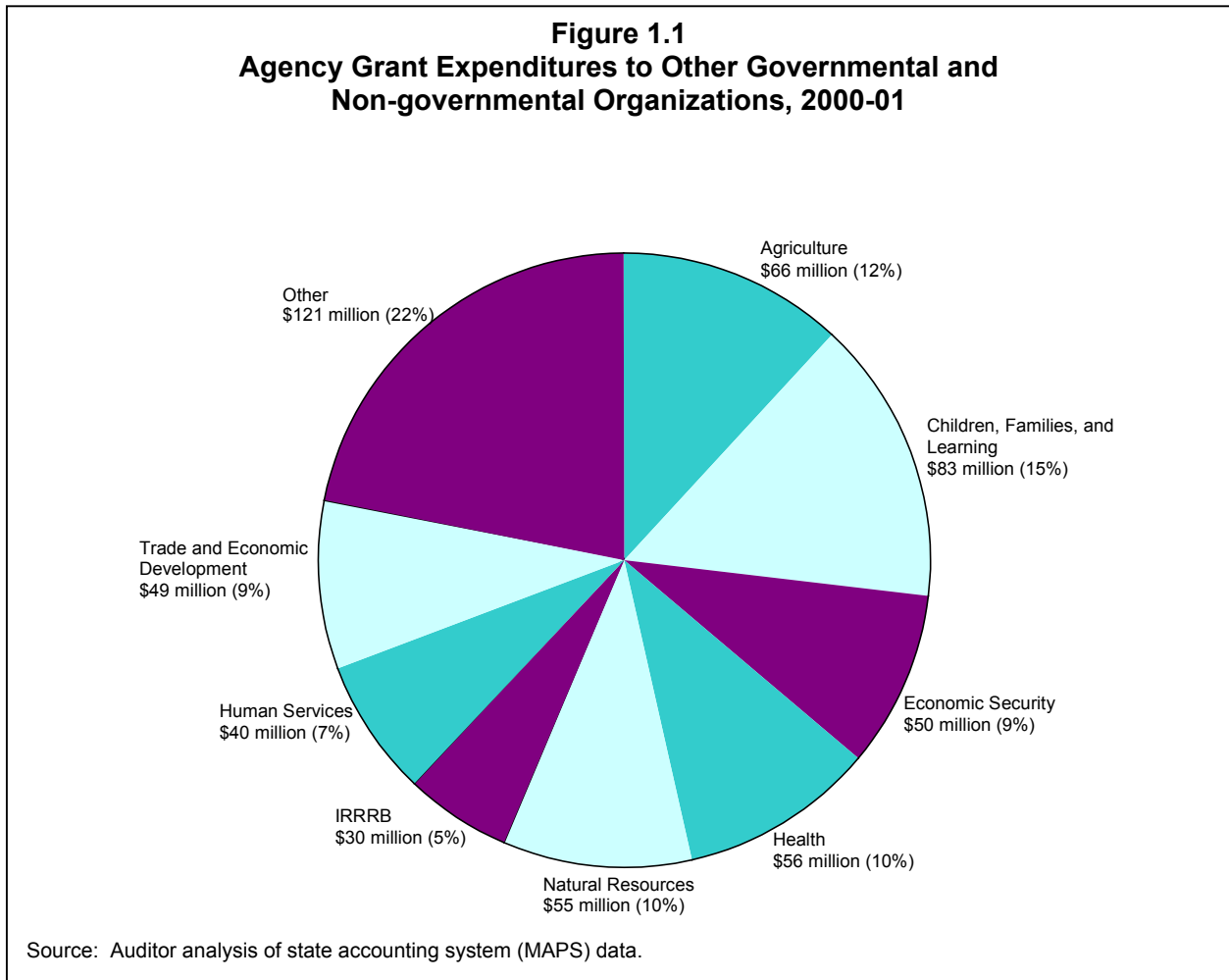
In the Minnesota Accounting and Procurement System (MAPS) Operations Manual, a grant is defined as "financial assistance paid or services furnished by a state agency via a third party to an eligible recipient.... The state agency is buying something for someone else...."³ Of the approximately \$550 million in grants we addressed in this review, we estimate that 87 percent

³ Minnesota Departments of Finance and Administration, Operating Policy and Procedure, Grants Contracts, #0707-02, June 21, 1995.

Special Review: Minnesota Grants Administration

was related to on-going agency programs and approximately 13 percent was for one-time projects.

The level of grant activity, measured by dollars granted, varied greatly across agencies. Figure 1.1 shows that the Department of Children, Families, and Learning accounted for 15 percent of dollars granted to quasi-governmental and non-governmental organizations. The departments of Agriculture, Health, and Natural Resources each accounted for at least 10 percent.



While most of the money (approximately 73 percent) granted to organizations in the 2000-01 biennium supported specific programs or projects, the state did support the general operations of some recipient organizations. For example, the Minnesota State Arts Board awarded over \$13 million in grants to provide “general operating support to high-quality, established arts organizations that produce or exhibit works of art or provide a broad range of services to artists.”⁴ In another example, the Legislature directed the Department of Commerce to transfer

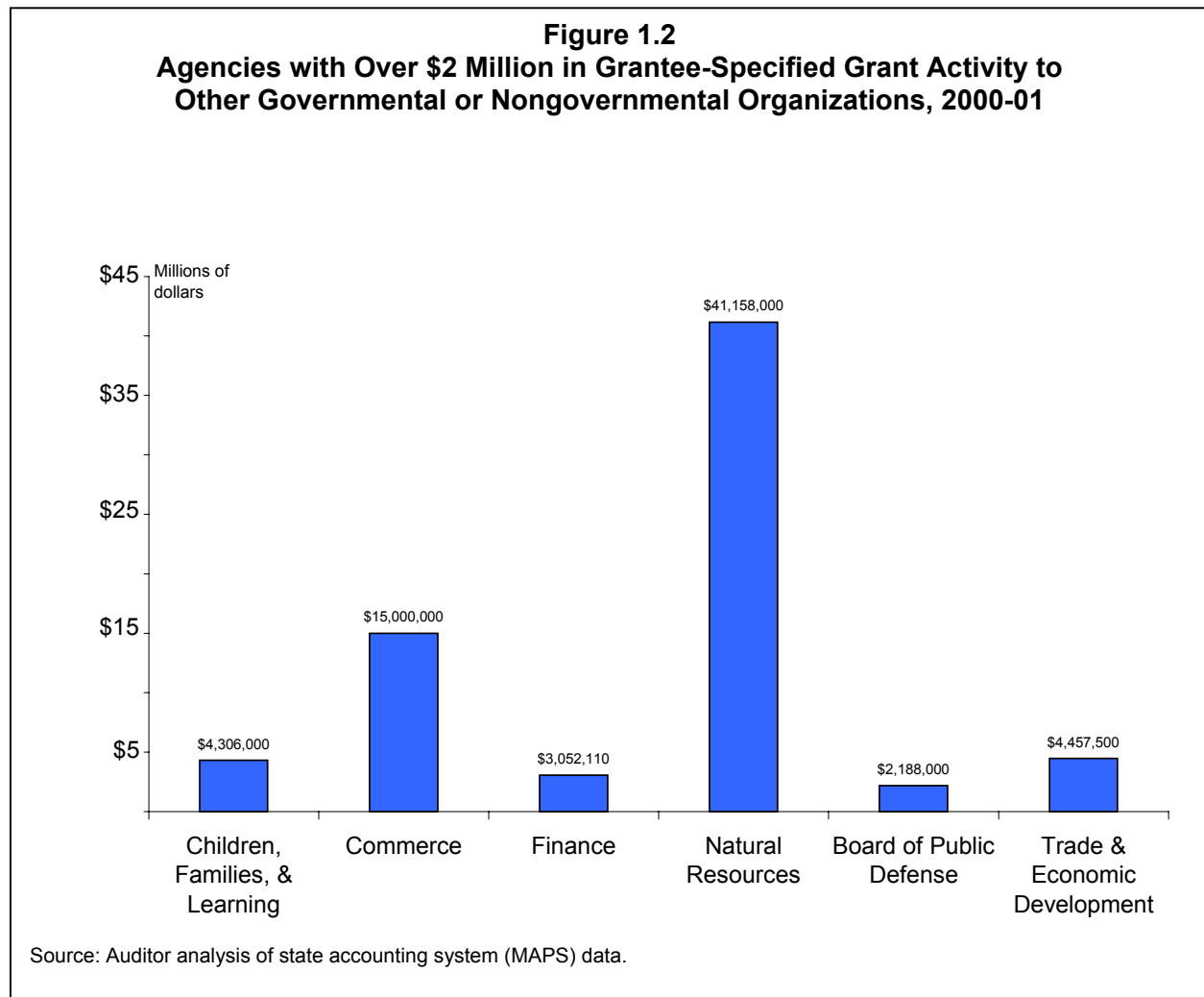
⁴ Minnesota State Arts Board, “Applications for Arts Organizations: Institutional Support and Arts in Education (AIE) Organizational Support, Fiscal Years 2002 & 2003,” page 1.

Special Review: Minnesota Grants Administration

\$15 million to the Minnesota Comprehensive Health Association “for the exclusive purpose of reducing the association’s operating deficit assessment for calendar year 2001.”⁵

For about 14 percent of 2000-01 grant money—almost \$79 million—the Legislature identified the intended grant recipient in law, either directly or through narrow eligibility criteria.⁶

Figure 1.2 shows the state agencies that administered over \$2 million in grants to organizations that were named in law. The Department of Natural Resources administered 52 percent of the money for which the grantee was specified in law.⁷



When a recipient is named in law, some agency officials question calling the transaction a grant, especially when the money can be used to support the organization generally rather than to

⁵ *Minn. Laws* (2000), Chapter 488, Article 13, Section 1.

⁶ This is a conservative estimate because we counted only those appropriations in which all of the money went to the specified grantee(s) and limited it further to those programs that managers told us awarded fewer than seven grants.

⁷ During 2000-01, DNR administered several pass-through grants for which the grant recipient was specified by the Legislative Commission on Minnesota Resources (LCMR). Although LCMR grant recipients are specified in law, we were told that over 95 percent of the dollars awarded by the LCMR are to recipients who participated in a competitive process.

Special Review: Minnesota Grants Administration

achieve a specific program purpose. Some officials see this kind of transaction as a “pass through” appropriation to the organization that is named in law. However, based on the MAPS Operations Manual definition, we think it is appropriate to call these transfers “grants.” We also think it is useful since the term implies that certain accountability and control measures should be used (such as a contract, monitoring by the state, and reporting by the organization).

Our findings and recommendations are in Chapters 2 and 3. In addition, in Chapter 4, we offer comments and suggestions about the Legislature’s role in grant making.

Special Review: Minnesota Grants Administration

This page intentionally left blank.

Chapter 2. Grant Awarding

Chapter Conclusions

State agencies used various practices to select grant recipients and award competitive grants. For the items tested, in all material respects, agencies complied with the applicable legal requirements for awarding grants. As a general rule, we found that state agencies have attempted to establish open and impartial processes when selecting grant recipients. However, state agencies did not always clearly specify grant objectives and work products. We noted certain instances where grant contracts were unclear or incomplete.

We think the state should establish general guidelines or requirements for the grant award process, especially in the areas of conflict of interest and cash management. We recommend that the departments of Administration and Finance coordinate these efforts.

The grant award process normally begins when the Legislature appropriates money to an agency for a certain purpose. The Legislature can be quite general or very specific in its appropriation language. For example, some agencies award grants through their regular operating appropriations, and the Legislature does not establish specific requirements or limitations on the grants, other than those that relate to any appropriation. At the other extreme, the Legislature may name the grant recipient and specify the exact grant amount.

When the Legislature does not specify the grant recipient, agencies use various processes to award grants. There are no centralized rules and only limited guidelines relating to the award process, although statutory provisions or administrative rules for individual programs may establish certain requirements. Some state agencies have developed written policies and procedures for grant making, at either an agency-wide or program level. However, there are wide variations in the procedures agencies use to select grantees and make grant payments.

Objectives and Methodology

This chapter addresses the following questions:

- Did state agencies comply with applicable legal requirements when awarding grant funds and establishing grant contracts?
- Did state agencies use an open and impartial process when awarding grant funds?
- Did state agencies clearly specify grant objectives and work products?

Special Review: Minnesota Grants Administration

To answer these questions, we reviewed grant files for a statewide sample of 50 grants, analyzing documentation for the award process and discussing procedures with program personnel. In addition, we asked questions about the grant award process in roundtable discussions with agency staff and in questionnaires we sent to state agency heads and to grant recipients. We also reviewed Minnesota's policy on contract administration and applicable Minnesota Statutes. Finally, we relied on professional judgment and our experience in auditing state agency grant programs. In the next section, we describe the practices state agencies used to publicize the availability of grant funds and the criteria they used when selecting individual grantees.

State Agency Grant Award Practices

State agencies use a variety of methods to inform citizens and organizations about grant programs. In response to our questionnaire, agency heads identified agency web sites and mailings to interested organizations as the primary methods used to publicize the availability of competitive grant funds. Of the 19 state agency heads whose agencies had competitive grant programs during the 2000-01 biennium, 12 said they always or usually publicized the availability of grants through agency web sites, and 12 said they used mailings to interested organizations to publicize grants. Publishing a notice in the *State Register* was a close third, with 11 agency heads saying they always or usually publicized the availability of competitive funds this way. Some agency staff told us that the *State Register* was not necessarily the best vehicle for publicizing the availability of grants, depending on the eligible population. Niche publications and targeted mailings were mentioned as ways agencies could provide grant information to a narrower eligible population.

In the 2000 Session, the Legislature passed a law that requires agencies to use their web sites to publicize grant availability. We verified agency compliance with the new law through a review of 26 state agency web sites. Some agencies have created web sites that offer grant information and the sites were user-friendly. For example, the Department of Natural Resources has a "Financial Assistance Directory" link on its home page.⁸ This directory includes a Financial Assistance Program Matrix, which gives information on programs, eligible applicants, and eligible projects. The Minnesota State Arts Board web site provides interested parties with a list of its programs and a schedule of upcoming grant application workshops.⁹ The Department of Health has a link to an "Available Grants Funds Notice" which provides grant descriptions and outlines grant application procedures.¹⁰ However, we found other agencies that did not have all grants listed on their sites, or the agencies' grant information was difficult to find.

The 41 grantees that responded to our questionnaire said they learned about available grant funds from the following sources:

- mailings from a state agency (11);
- contact with state agency staff (10);

⁸ <http://www.dnr.state.mn.us/>, accessed 9/11/01.

⁹ <http://www.arts.state.mn.us/>, accessed 9/11/01.

¹⁰ <http://www.health.state.mn.us/>, accessed 9/11/01.

Special Review: Minnesota Grants Administration

- the *State Register* (2);
- a peer organization (3); and
- other sources or a combination of sources (8).

None of the respondents said they first became aware of the grants through other publications or the agency's web site.¹¹ However, many grant recipients had received grants for several years, some since the 1970s or 1980s. Even though agency web sites did not play a role with these grantees, the sites may be a useful tool in the future.

Agencies also used various methods to provide information on the grant application process. Staff from one agency said they produced lists of commonly asked questions about the application process and posted them on the Internet. Other staff said their agencies held grant information workshops or open houses around the state to discuss grant programs and the application process. One agency recently piloted video conferencing as a way of informing potential applicants about grant funds.

In our sample of 50 grants, 31 grants were *not* awarded as a result of a competitive process. In eight of these cases, the Legislature either named the grantee or provided strict criteria for determining the grant recipient(s). Another eight grants provided continuation funding for prior year grants. The remaining noncompetitive grants went to certain specified types of organizations, such as area aging agencies.

Table 2.1 shows the techniques and processes used by agencies for the 19 sample grants that were subject to a competitive process.

Table 2.1
Agency Grant Awarding Practices
For 19 Competitively Awarded Grants

Practices Followed	Number Using Practice
The agency used a request for proposal.	16
The agency used a public notice of availability of grant funds.	16
The agency used an independent evaluation process.	12
The evaluation process was conducted in open meetings.	9
The agency used rejection letters.	12
The rejection letter listed the rejection criteria.	9
The agency held conferences for potential grantees.	8
The agency published questions and answers relating to the grant proposal.	8

Source: Auditor testing based on 19 sample grants that were subject to competitive awarding out of 50 total grant sample items.

In responding to a question about the adequacy of information on grant availability, 28 grantees thought no improvement was needed, while 8 recipients thought some improvement was

¹¹ Four recipients did not know how they first heard of the grant and three did not answer the question.

Special Review: Minnesota Grants Administration

needed.¹² For 29 grants, recipients thought that information about the grant application process did not need improvement, while 6 grant recipients thought some improvement was needed in this area.¹³ It should be noted that over half of the grantees we surveyed had received grants previously, so they may not be representative of first-time grant applicants.

We also asked grantees what they thought of the information they received about the criteria upon which individual grant applications would be judged. For 23 of the grants, recipients thought no improvement was needed, but 10 thought some improvement was needed and 2 thought much improvement was needed.¹⁴ One grantee said she did not receive information about selection criteria, and she thought it would have been helpful. Another recipient thought the criteria needed to be clearer and more concise, because it was hard for her to determine whether her organization met the requirements. In reviewing these results, one must recognize that questionnaires were sent only to organizations that were successful grant applicants; the opinions of unsuccessful applicants might differ.

Agency staff told us that, after grant applications were received, they used a number of different tools to assess an applicant's capacity to meet grant objectives. For example, 21 agency heads told us they conducted site visits, 18 used some form of expert review, and 16 used the organizations' annual reports. Seventeen agency heads told us that they looked at financial statements to help assess a grant applicant's capacity. Thirteen agency heads said they conducted interviews with grant applicants. And while 21 agency heads considered their own agency's prior experience with the applicant when assessing capacity, only 9 indicated that they considered the experiences of other state agencies.

Conclusions

As a general rule, we think state agencies have attempted to establish open and impartial processes when selecting grant recipients. For the items tested, in all material respects, agencies complied with the applicable legal requirements for awarding grants. However, we noted certain instances where grant contracts were unclear or incomplete. The state should establish general guidelines or requirements for the grant award process, especially in the areas of conflict of interest and cash management. We recommend that the departments of Administration and Finance coordinate these efforts. We identified certain issues or concerns about the grant award process, as discussed in Findings 1 through 4.

1. Some grant contracts were unclear or incomplete.

We identified five grant programs where state agencies did not use grant contracts or, if used, the contract terms were vague or ambiguous. One agency used purchase orders rather than grant contracts to document its arrangements with the grantee organizations. The purchase orders did not contain standard contract provisions, such as the grantee's duties and payment terms.

¹² Three recipients responded that the question did not apply and two responded "don't know."

¹³ Four recipients responded that the question did not apply and two responded "don't know."

¹⁴ Four recipients responded that the question did not apply and two responded "don't know."

Special Review: Minnesota Grants Administration

Although state agency personnel approved the purchase orders, the grantee was not required to sign the document. During our survey work, we also identified an agency that did not initiate a contract with the recipient organization, even though the general fund appropriation law for the grant had a specified match requirement. It could be very difficult for agencies to enforce expectations without a contract document. A written contract is also critical in resolving potential disputes over grantee performance.

In three other cases, state agency contracts were incomplete or contained incorrect or ambiguous terms and conditions. For one grant, the state agency used a contract that did not contain certain standard contract provisions such as terms of payment and data practices requirements. Instead, the agency relied on a broad statement requiring the grantee to comply with all applicable provisions of law. Another state agency executed a grant contract that contained confusing reporting requirements. The agency subsequently sent letters to grantee organizations clarifying and changing the reporting requirements. In another case, a state agency transposed the total grant dollar amount on the grant contract. Although the error did not result in an overpayment to the grantee, the agency did not detect the error.

In our survey of grantees, 11 recipients responded that they believed some improvement was needed concerning the information they received on the laws, regulations, and conditions that applied to their particular grant.¹⁵ Fifteen recipients stated that the clarity of the state agency's expectations needed "some" or "much" improvement.¹⁶ Clear and complete contracts are the beginning of good communication between state agencies and recipients.

Minnesota Statutes (2000), Chapter 16C, provides guidance concerning the procedures needed to make a state contract valid. Section 16C.05 provides, in part, that a contract is not valid unless it is signed or executed by the appropriate parties and that the accounting system reflects an obligation for the amount of the contract liability. The statute specifically provides that grant contracts do not have to be signed by the Commissioner of Administration and/or the Attorney General, at their discretion. In addition, statutes require that contracts have an audit clause providing that the contracting agency and either the legislative auditor or state auditor, as appropriate, have access to relevant books and records for a minimum of six years.¹⁷

The departments of Finance and Administration have encouraged state agencies to prepare contracts when entering into grant agreements.¹⁸ In 1994, the Department of Administration published an example of a grant contract for state agencies to use. When the Department of Administration reissued its contract manual in April 2000, it excluded the grant management section. However, in September 2001, the department reissued the section of its contract manual relating to grant and loan contracts. The section discusses public notice for grants and includes the sample grant contract and a procedure checklist for agencies to consider when awarding grants. The contract template includes provisions such as grantee's duties, consideration and

¹⁵ Twenty-eight recipients responded that no improvement was needed, and two responded that either the question did not apply or they did not know the answer.

¹⁶ Twenty-five recipients responded that no improvement was needed and one responded that the question did not apply.

¹⁷ *Minnesota Statutes* (2000), 16C.05, Subd. 5, Subject to Audit.

¹⁸ Minnesota Departments of Finance and Administration Operating Policy and Procedure, Grants Contracts, #0707-02, June 21, 1995.

Special Review: Minnesota Grants Administration

terms of payment, contract period, cancellation clauses, assignment, liability, audits, data practices, and ownership of material. If grants are funded from federal monies, state agencies also have to consider any federal contract requirements.

We think that comprehensive and clear contracts are important for both competitive and noncompetitive grants. They provide a way to document duties and responsibilities of both the grantor and the grantee. It is particularly important when there are specific legal requirements or when the grant is expected to pay for specific services.

Recommendation

- *When awarding grants, agencies should execute standardized grant contracts that contain all required provisions, as well as clear and specific information on the quantities and types of services to be performed. Agencies should follow the Department of Administration's Contract Manual when drafting grant contracts.*

2. Uncertainty exists about how the statutory conflict of interest provisions apply to individuals involved in the grant process.

The state's procurement conflict of interest statutes do not clearly extend to agency staff members and others who may be involved in reviewing state grant proposals. *Minnesota Statutes* (2000), Chapter 16C, discusses conflicts of interest "in the acquisition process." It requires the Commissioner of Administration to "develop policies regarding code of ethics and conflict of interest designed to prevent conflicts of interest for employees involved in the *acquisition of goods, services, and utilities* [emphasis added]." ¹⁹ In its April 2000 contract manual, the Department of Administration included a sample policy agencies can use to build their conflict of interest policies. However, the statute is not clearly applicable to grant contracts.

Agencies handled conflict of interest in different ways, based upon comments of state agency roundtable participants and the written policies we reviewed. For example, one agency's enabling legislation and administrative rules have an explicit policy on conflict of interest. ²⁰ These are repeated in its advisory panel members' guide, in which *apparent* conflicts of interest are also discussed. ²¹ Other state agencies did not have agency-wide written policies relating to conflict of interest.

In various financial audits, we have identified instances where state agencies did not adequately address potential conflicts of interest when awarding grants. Conflicts of interest may arise during grant awarding because of the unique nature of certain grants. In some cases, the number of people interested or involved in certain social issues may be small. Therefore, it is more likely that agency personnel, or others responsible for recommending recipients, may know or

¹⁹ *Minnesota Statutes* (2000), 16C.04, Subd. 2.

²⁰ *Minnesota Statutes* (2000), 129D.04, Subd. 1, Clause h; and *Minnesota Rules* (2000), 1900.0410, Subps. 5 and 6, pertaining to the Minnesota State Arts Board.

²¹ Minnesota State Arts Board, *Panel Handbook*, 9th Edition, November 1998.

Special Review: Minnesota Grants Administration

have personal or professional relationships with members of the grantee community. Because of this, it is important for an agency to clearly state its conflict of interest policy. In addition, agencies should have a process for making employees and others involved in reviewing grant applications aware of the policy, and should train employees on how to avoid or deal with potential conflicts.

Recommendations

- *The Department of Administration should seek legislation to clarify that procurement conflict of interest statutes apply to grant contracts.*
- *Agencies should establish formal policies and procedures that deal with potential conflicts of interest in the grant award process. They should ensure that the policy clearly extends to non-state employees involved in the agencies' grant awarding processes.*

3. State agencies did not consistently follow cash management practices that were in the state's best financial interest.

We found that, for 32 of the 50 sample grants, agencies gave the grantee all or a portion of the grant amount in advance of the services being provided. In a few cases, agencies paid large operating grants as a lump sum at the beginning of the grant period, making no attempt to prorate the funding over the entire grant period. This certainly helps the grantee's cash flow, but is less beneficial to the state. In recent financial audits, we have also identified problems with grant cash flow procedures.

Agencies use a variety of methods and timeframes to distribute funds to grant recipients. Some of these methods are more favorable to the state, while some provide more benefit to grantees. A key cash management consideration when disbursing funds is who should earn investment earnings on idle cash not immediately needed for program purposes. There are no statewide policies governing the distribution of funds to grantees. Of the 50 sample grants we reviewed, 14 recipients were paid solely through reimbursements based on the performance of certain measurable tasks. Obviously, this method of cash management is most beneficial to the state. It follows the state's general payment philosophy, which is to pay only for goods or services it has already received. However, this method requires the grantee to provide and pay for services and wait for state reimbursement. Some agencies told us that grantees do not always have available cash that would allow them to wait for payment until after they have provided the services.

There are policy arguments to be made concerning the state's role in providing cash flow assistance to nonprofit organizations. In some cases, agency staff told us that, due to the lack of potential qualified service providers, the agency felt obligated to support its grantees by providing funding in advance of actual program disbursements. However, providing cash in advance limits an agency's influence over nonperforming or underperforming grantees.

Special Review: Minnesota Grants Administration

If state agencies are disbursing grants from federal funds, they must also consider federal guidelines, as addressed in the Cash Management Improvement Act. In that act, the federal government attempted to balance the grantees' financial burden while maximizing federal interest earnings. The act emphasized "just in time" funding and, generally, does not allow grantees to draw federal funds until the monies are actually disbursed. In our sample of 50 grants, 26 involved federal funds and were subject to federal cash management requirements.

The state needs to establish a clear cash management policy for grant programs. It should consider the cash flow needs of grantees, while maximizing the state's cash flow. As technology has changed, the state is able to provide more timely cash reimbursements to grantees. Other techniques, such as withholding a percentage of the final grant payment until all services are provided, may also be effective.

Recommendation

- *After consulting with state agencies, the Department of Finance should establish appropriate cash management policies for disbursement of grant funds.*

4. The state does not have a formal mechanism for agencies to share information about grantee performance.

The state currently has no established process for sharing information among state agencies about nonperformance or noncompliance by grantees. Although 21 agency heads told us that they consider their own agency's past experience with applicants when assessing capacity, only 9 said they consider experiences of other state agencies. Staff from one agency said inter-agency checking occurs informally or in situations where several agencies administer similar programs.

In its rules, the federal government has dealt with the issue of grantee nonperformance. Non-federal entities are "prohibited from contracting with, or making subawards under covered transactions to parties that are suspended or debarred or whose principals are suspended or debarred. Covered transactions include procurement contracts for goods and services equal to or in excess of \$100,000 and all nonprocurement transactions (e.g. subawards to subrecipients)."²² Based on this language, it is clear that the federal government will not allow states to subgrant federal funds to parties who have been suspended or debarred.

The Department of Administration's Materials Management Division has a vendor performance reporting process. Agencies are encouraged to complete a report on vendor performance and send it to Administration to be included as part of the vendor's performance history. Materials Management cites its goal for this process as acknowledging excellent vendors, identifying poor performance, resolving problems, and removing poor quality vendors.²³ We were told that state agencies have not used this process to report on performance of grantees.

²² Office of Management and Budget A-133 Compliance Supplement Section I, Procurement and Suspension and Debarment.

²³ <http://www.mmd.admin.state.mn.us/mn02005.htm>, accessed 9/12/01.

Special Review: Minnesota Grants Administration

We think it is important for agencies to have a mechanism to determine whether potential grantees have had serious nonperformance or noncompliance issues. Although some performance issues might not be relevant, an agency could learn whether an applicant has had serious compliance concerns or financial management problems. The state agency could then work with the potential grantee to determine whether the issues had been appropriately resolved.

Recommendations

- *The Departments of Finance and Administration should work with state agencies to require potential grantees to report, as part of the grant application process, other grants received from the state.*
- *State agencies should seek information concerning potential grantee past performance from other state agencies when making grant awarding decisions.*

Special Review: Minnesota Grants Administration

This page intentionally left blank.

Chapter 3. Grant Monitoring

Chapter Conclusions

State agencies did not consistently or adequately monitor grantee activity throughout the grant period. We found numerous cases where agencies did not independently verify information they obtained from grantees, did not ensure that grantees complied with grant reporting requirements, and did not verify matching funds claimed by grantees. We think the Department of Finance should work with state agencies to coordinate grantee monitoring and auditing, to provide a mechanism for state agencies to obtain information necessary to assess a grantee's financial environment, as well as its compliance with individual grant requirements.

Agencies did not always comply with applicable legal requirements when expending grant funds. In some cases, agencies did not pay grantees in accordance with applicable payment terms. In addition, there were inconsistent interpretations of the period of availability for grant funds. We recommend the Department of Finance seek legislation to clarify statutory provisions regarding the availability of grant balances.

Once grants are awarded, agencies have an ongoing responsibility to monitor grantee performance. Monitoring can be an effective tool to identify potential problems before they escalate, and it can provide opportunities for state agencies to provide technical assistance to grant recipients. Ultimately, it provides a structure to ensure that state funds are used as originally intended by the Legislature.

Objectives and Methodology

This chapter addresses the following questions:

- Did state agencies adequately monitor grantees to ensure that grant funds were expended in accordance with legal requirements and grant contract provisions?
- Did state agencies have an appropriate process to ensure compliance with state laws or policies and procedures relating to the close of grants?

To answer these questions, we reviewed state agency policies and procedures relating to grant administration, when available, and also tested the actual practices followed by state agency staff for a sample of 50 grants. We included questions about grant monitoring at agency roundtables

Special Review: Minnesota Grants Administration

and in questionnaires. We also considered the results of previous audits that addressed concerns relating to grant management.

State Agency Grant Monitoring Practices

When monitoring the use of grant funds, state agencies follow various procedures. When we asked state agency heads about support they provided to grant recipients, most said they provided grantees with a contact person at their agency. Most also said they offered written information on laws, rules, policies, and procedures. Over half of the agency heads said they provided grantees with training on compliance issues. Some agency heads listed other types of support they provided, including site visits, orientation for new grantees, and training sessions.

The tools that the greatest number of agency heads told us they used to monitor grantees during the grant period²⁴ include:

- site visits (23);
- other communication, such as phone calls and faxes (22);
- periodic financial reports (21); and
- periodic performance reports (20).

Agency staff at our roundtables gave examples of how monitoring and technical assistance are often linked. They indicated that periodic performance and financial reports could alert them to problems that a particular grantee was having and staff could then increase the level of technical assistance to that organization. Some said that a financial staff member might accompany program staff on site visits, particularly if program staff had identified financial concerns. A staff member from one agency said that, because of past compliance problems with grantees, the agency plans to provide more information on agency expectations, with the hope that it will reduce subsequent incidents of noncompliance.

We asked agency heads whether they were able to assess overall grantee performance, detect problems in performance, propose corrective action for unacceptable performance, and take timely corrective action for unacceptable performance. In each case, between 21 and 23 state agency heads responded that they were able to do these things “very well” or “well.”²⁵ Although indicating the occurrence is rare, some agency staff told us that there have been instances of terminating a grant relationship or requiring repayment of grant funds when grantees have not performed well or have not complied with grant terms.

Grantees were mostly positive in response to our questions about technical assistance and monitoring requirements. For 28 of 41 grants, recipient organizations responded that no improvement was needed in the quality of technical assistance provided by state agencies.²⁶ Some grantees that said some or much improvement was needed mentioned difficulty reaching

²⁴ Based on the survey responses of 24 agency heads. Of the original 26 agency heads to whom we sent questionnaires, one did not respond and one response was eliminated because the agency’s grant activity was limited to interagency grants.

²⁵ One agency head responded “don’t know” to these questions.

²⁶ Two grant recipients answered “not applicable” and one answered “don’t know.”

Special Review: Minnesota Grants Administration

state agency staff and getting questions answered as their main concerns. Grantees characterized financial reporting requirements for 35 of the grants as reasonable²⁷ and thought the performance reporting requirements were reasonable for 32 grants.²⁸ Recipients thought the financial reporting requirements were excessive for five of the grants and the performance reporting requirements were excessive for seven grants.

Conclusions

State agencies did not consistently or adequately monitor grantee activity throughout the grant period. In addition, agencies did not always comply with applicable legal requirements when expending grant funds. We believe the Department of Finance should work with state agencies to coordinate grantee monitoring and auditing, to provide a mechanism for state agencies to obtain information necessary to assess a grantee's financial environment, as well as its compliance with individual grant requirements. We also recommend the Department of Finance seek legislation to clarify statutory provisions regarding the availability of grant balances. We discuss these issues related to grant monitoring and close out in Findings 5 through 8.

5. State agencies did not adequately or consistently monitor grantees to ensure that funds were used as intended.

In many cases, agencies were doing an inadequate job of assessing the validity of information they obtained from grantees throughout the course of the grant project. In our sampling of 50 grants, we found 17 instances where agencies did not independently verify the financial and program information submitted by grantees. In some cases, the agencies merely collected and filed the required reports. Although some agencies said that they rely on site visits to verify submitted information, we noted examples where site visits had not been performed for a number of years, or the conclusions from the visits were not documented.

Some of the instances of inadequate monitoring involved agency verification that recipients had met matching requirements. Match requirements may include cash contributions for a percentage of the grant amount or "in kind" services. For 17 of the 50 grants we sampled, matching funds were required. The state agencies did not request or verify supporting documentation for the match amounts claimed by four grantees. In the four programs, the grant agreement cited specific match amounts the grantee had to provide in order to qualify for the grant. In addition, as a result of our survey work, we identified an agency that did not have a formal agreement with the grantee, despite a match requirement imposed by the Legislature. In their reports to the state agencies, the grantees indicated that they had provided the required matching amounts. However, without independent verification, there is a risk that the match was not met and that the state's share of project costs exceeded legislative intentions.

We also found 16 instances where grantees either did not submit required reports or submitted them after the stated deadlines. These included financial status reports, as well as statistical and program results information. In four cases, we found no evidence that the state agencies ever

²⁷ One grant recipient answered "no opinion."

²⁸ One grant recipient answered "no opinion" and one answered "don't know."

Special Review: Minnesota Grants Administration

received the reports required by program rules or the grant contract. In 12 other cases, agencies received grantee reports, including final evaluations, anywhere from a few weeks to over a year late. In these cases, the agencies did not withhold final payments pending the receipt of required reports.

State agencies, and sometimes individual grant program managers, have developed some inconsistent approaches for monitoring grantee performance. For example, the level or method of monitoring often varies for “pass-through” grants, where the Legislature names the grantee in the appropriation law. Some of these grants are for a particular service; others are used to support the general operations of an organization. Agencies that administer these grants took different approaches to monitoring. In some cases, the agency acted primarily as a fiscal agent disbursing money to the recipient organization with no follow up on the use of funds. At least one agency that administers pass-through grants responded that it does not monitor grantees at all during the grant period. Other agencies told us they treated these pass-through recipients the same as other grantees. The agencies required an application, work plan, and proposed budget so that they had criteria against which to measure the organization's performance. Some staff said that they felt a responsibility to provide a level of oversight for public funds, but that grants seldom come with any money for agency administrative costs.²⁹

Although we recognize that the type of monitoring performed for pass-through grants may differ from other grants, we think there still is a need for accountability in the use of these grant funds. For example, where there are established legal requirements or expectations, such as matching funds or specific services to be provided, state agencies should ensure that these requirements are met. This may be accomplished through review of supporting documentation or site visits, as appropriate. In addition, even when grant funds are going to support the general operations of an organization, it may be valuable to review audited financial statements and audit management letters for the organization to ensure that the auditor did not identify major concerns relating to the entity's financial operations.

We think that validating grantee information is an important way for agencies to ensure that grantees are spending their awards appropriately. It is not enough for an agency to simply award grant funds based on a good proposal. By not establishing some process to verify supporting documentation for grantee reports, agencies run the risk that grant funds are used for unallowable costs, or the program's purposes are not being achieved. We are concerned that the state does not have a coordinated approach to grant monitoring. While some state agencies may require grantees to have individual grant audits, even for very small grants, other agencies may not do any independent verification of expenditures for much larger programs. These inconsistencies in the monitoring process do not provide the most effective grant management process.

The federal government faced the problem of inconsistent grant management in the early 1980s. It found that, “lacking time, experience, or executive branch guidance, each [federal] agency, and in many instances different bureaus within the same agency, developed their own administrative

²⁹ However, the 2001 Legislature appropriated \$150,000 to the Department of Natural Resources (DNR) to administer Legislative Commission on Minnesota Resources grants passed through DNR. Minn. Laws (2001), Chapter 2, Section 14, Subd. 3(b).

Special Review: Minnesota Grants Administration

requirements with which state and local governments were required to comply.”³⁰ For some programs, federal agencies conducted or required annual audits of program expenditures for all grant recipients. Other programs received no audit coverage at all. Some grant recipients may have had audits each year by several different federal agencies.

The federal government addressed this inconsistent, and possibly duplicative, monitoring by implementing the Single Audit Act in 1984. The general purposes of the act included promoting sound financial management by recipients of federal funds, establishing uniform and effective requirements for audits of these funds, and reducing the administrative burden on grant recipients. The act established financial thresholds for audits of federal grantees, as well as priorities for conducting detailed financial and compliance reviews of individual grant programs. It also provided for “compliance supplements” that identified information or compliance features that grantee auditors were to verify.

In the years since the federal Single Audit was established, several states have passed their own state Single Audit acts. At least 12 states require some coordinated audits of state financial assistance recipients. Many of these states have published audit guides, compliance supplements, or other guidelines to assist auditors of state grantees. The results of these audits are intended to provide state agencies and program managers with both general and specific information about their grantees. In Minnesota, the Office of the State Auditor has published a legal compliance guide for audits of local government entities.

We think the concept of a state Single Audit merits consideration by the State of Minnesota. It is sometimes difficult for agencies and program managers to know how much information to require from grantees and to evaluate the adequacy of information they receive. In addition, state agencies do not have a basis for assessing the overall capacities and financial health of their grantees based only on program-specific information. There is a potential to decrease the burden on individual state agencies if they are able to obtain assurances about the financial structure and control environment of grantees through annual audits of grantee organizations. Thirty-six of the 40 grantee organizations we surveyed stated that an independent auditor had reviewed their finances during our scope period. Thirty-two of these reviews were audits designed to express an opinion on the entity’s financial statements, and 15 of the audits were designed to meet federal Single Audit requirements.³¹ These audits could be expanded to include testing of selected compliance features deemed important by state agency program managers.

When we asked state agency heads if they would favor a requirement that state grants be audited at the grantee level on a periodic basis, 14 said yes, 4 said no, and 6 did not have an opinion. A number of agency heads who favored an audit requirement qualified their response by noting that criteria should be developed to determine which entities would be subject to the requirement. For example, a Single Audit could be required if an organization received at least an established

³⁰ Dettmar, Richard P. Grants Management by State and Local Governments: A Systematic Approach, *GAO Review*, Spring 1981.

³¹ Of the 36 who said their organization’s finances had been reviewed between July 1, 1999, and June 30, 2001, 2 did not specify the type of review. Other audit efforts included compilations or reviews (13 grantees) and cash-basis audits (2). (Grantees could indicate more than one level of audit.) Three grantees said their organization’s finances had not been reviewed by an independent auditor between July 1, 1999, and June 30, 2001. One grantee did not know.

Special Review: Minnesota Grants Administration

minimum amount of state grant funds each year. Agency heads were split over who they thought should be responsible for the audit. Of the 14 favoring an audit requirement, 6 thought the grantor should be responsible, 4 thought the Legislative or State Auditor should be responsible, 1 thought the grantee should be responsible, and 3 thought either the grantee or the Legislative or State Auditor should be responsible for the audit.

Lack of funding for administrative positions is one of the primary reasons why state agencies said their monitoring efforts were limited. During roundtables, staff pointed out that site monitoring requires staff resources. In addition, even when site visits were performed, staff may not have had the background or skills to assess both financial concerns and performance results. If an agency can rely on a grantee Single Audit that focuses on the organization's overall financial management, as well as testing selected program criteria, the agency's detailed monitoring responsibilities may decrease or become more effective.

However, designing and implementing a state Single Audit is not necessarily an easy task. Criteria and requirements for the audits would have to be established. In addition, agency program staff would have to identify the critical compliance features to be reviewed as a part of the audit. There is a risk that this process could result in an excessive number of features to be tested, making the cost-benefit of the audit process questionable. We think such an effort would have to be coordinated by the Department of Finance to provide an objective and consistent approach to establishing the audit requirements.

Recommendation

- *The Department of Finance should ensure there is appropriate accountability for the use of grant funds by working with state agencies to:*
 - *coordinate grantee monitoring and auditing among agencies; or*
 - *refine agency reporting requirements and determine the monitoring necessary to ensure the validity of submitted grantee information.*

6. Some state agencies did not make grant payments in compliance with applicable legal or contract requirements.

In our testing of 50 grants, we found 3 grants where state agencies did not pay grantees in accordance with applicable payment terms. Two agencies did not comply with the payment terms of the related grant agreements. For one agency, the grant agreements stated that grantees were to receive the lesser of 25 percent of the grant award or the grantee's actual expenditures, after an initial 25 percent advance in the first quarter. Despite this, the agency automatically gave all grantees 25 percent of the funding each quarter, regardless of the grantee's actual expenditure amounts. Another agency paid a grantee 100 percent of the grant award before the grantee met all contract provisions. The grant agreement stated that the agency would retain ten percent of the total award "until receipt and approval of final completion report." The agency paid the final ten percent of funding to the grantee, even though it did not receive the grantee's final report until approximately three months later.

Special Review: Minnesota Grants Administration

In three cases, agencies made payment errors. For two grants, agencies made duplicate payments totaling approximately \$2,000. In another instance, an agency transposed an invoice amount, resulting in an overpayment of \$450. The agencies' monitoring procedures did not detect these errors.

In four other cases, agencies paid for expenses grantees incurred before the grant contract was signed and effective. In one of these cases, the grant contract stated, in part, "Grantee understands that no work should begin under this grant contract until all required signatures have been obtained, and grantee is notified to begin work by the state's authorized representative."

Recommendation

- *Agencies should pay grantees in accordance with applicable contract and other legal provisions.*

7. Often, state statutes do not clearly establish the time period during which grant money may be spent.

State statutes often do not clearly define the period of availability for grant appropriations, resulting in inconsistent interpretations and possible noncompliance with statutory requirements. When reviewing the close of grant awards, a key concern is the time period during which services can be provided and grant funds can be expended. In various recent audits, we have questioned whether state agencies have ensured that grants were timely closed and that grant recipients expended funds within allowable time frames. In some cases, we have questioned whether the agencies themselves have spent grant funds in accordance with established legal or contract requirements.

As a general rule, state agency appropriations are available only for the biennium in which the appropriations were made. *Minnesota Statutes* (2001), Section 16A.28, Subd. 3, provides, in part:

Any appropriation amounts not carried forward and remaining unexpended and unencumbered at the close of a biennium lapse to the fund from which the appropriation was made.

Section 16A.28, Subd. 6, provides, in part:

On October 15 all allotments and encumbrances for the last fiscal year shall be canceled unless an agency head certifies to the commissioner that there is an encumbrance for services rendered or goods ordered in the last fiscal year, or certifies that funds will be carried forward under subdivision 1.

Subdivision 6 applies to all appropriations except those from a fund derived from special taxes, fees, earnings, fines, federal grants, or other sources that are by law appropriated for special purposes by standing, continuing, or revolving appropriations.

Special Review: Minnesota Grants Administration

These legal requirements are reasonably clear if applied to a state agency's direct purchase of goods or services. But they may not be clear when applied to grants. For example, do grant funds only have to be disbursed or encumbered by the state agency as of the end of the biennium, or do they also have to be disbursed or encumbered by the grant recipient within that time frame? In other words, is the appropriation available only for those services provided by the grant recipient during the biennium in which the appropriation was made?

In this review, as well as in many prior audits of state agencies that administer grant funds, we have noted that agencies follow varying interpretations of the "availability" criterion. Some state agencies follow a practice of disbursing grant funds during the biennium in which the appropriation was made, but then establish a longer period for the grantee to actually incur costs in performance of the prescribed duties. For other programs, the agency may require the grantee to provide the required services during the biennium for which the funds were appropriated.

State agency grant administrators raise some valid concerns about their ability to appropriately manage grant funds within the strict time frame of the biennium in which monies are appropriated. The process to award competitive grants may take an extended period of time as proposals are solicited and reviewed and formal contracts are awarded. If an appropriation is made during the second year of the biennium, there may be only a few months to distribute the grant funds. Depending on the complexity of the program, it may not be realistic to expect the grant recipient to fulfill all of its responsibilities by the June 30 fiscal year end date. Some staff also said that the biennium end date is not appropriate for certain types of program services, such as providing funding for a growing season that runs from spring to fall.

Recognizing there was a problem in this area, in April 2001, the Department of Finance issued budget and accounting instructions regarding grant funds and their period of availability. The instructions provided guidance for state agencies when setting up fiscal year 2002 and 2003 spending plans and stated that grant agreements may not extend beyond June 30, 2003, unless there was specific legislative authority to do so. The instructions also said that the department would continue to study the issue and evaluate the need for changes in legal requirements. In September 2001, the department developed a draft operating policy and procedure relating to grants management and the availability of funds. The draft policy provided that grant monies should be disbursed on a reimbursement basis, based on evidence of performing contracts. It also stated that for grants awarded by June 30, encumbrances could be certified for one year after the end of the year in which the funds were appropriated. This would allow the grantee to provide services for one year following the appropriation end date.

We think the action taken by the Department of Finance was an appropriate starting point to clarify legal requirements regarding availability of funds. Whether one year beyond the end of the biennium is the appropriate definition of the grant availability period is a matter for debate between the Legislature and state agencies. It is important to come to a common understanding of the legal criteria and establish clear guidance for agencies that administer grant funds.

Special Review: Minnesota Grants Administration

Recommendation

- *The Department of Finance should seek legislation to clarify statutory provisions regarding the availability of grant appropriation balances. The department should continue to work with state agencies to address concerns on the availability of funds related to specific grant programs.*

8. The state's accounting system does not readily provide comprehensive information on grant program expenditures.

There is currently no way to identify the number of grant programs and the amount expended by state agencies for these programs. Three factors contribute to this issue. First, the current accounting system structure does not differentiate between grants and other types of financial assistance. The accounting system combines what we refer to as “grants” with aid payments to local government and transfers to other organizations. Second, although the Department of Finance has established some broad guidelines for coding information in MAPS, it has allowed state agencies to establish their own account structures, which may not relate to individual grant programs. Third, there is not a clear definition of what constitutes a grant. For example, the difference between grants and professional technical services is not always clear.

We originally chose a sample of 60 disbursements coded as grants on the state's accounting system. After our review, we decided to exclude ten of the disbursements in our sample because we concluded they were not grant payments. For example, one disbursement was a reimbursement to a telephone company for telephone services to low income customers. Another disbursement was for professional technical services. Still another was a loan payment. We had many other questions that came up concerning the definition of grants during our survey work.

The state does not maintain a comprehensive listing or catalog of grant programs. Understanding the variety of arrangements that are considered “grants” is important because different kinds of financial arrangements may suggest different administrative expectations. The type and amount of monitoring to be performed by state agencies could vary depending on the nature of the program.

Recommendations

- *The Department of Finance should establish a common definition of grant programs and revise accounting system coding, if necessary.*
- *The department should work with state agencies to ensure there is a clear understanding of the required coding structures relating to the recording of grant expenditures.*

Special Review: Minnesota Grants Administration

This page intentionally left blank.

Chapter 4. The Legislature's Role

Chapter Conclusions

The Legislature can have a significant impact on state grants. Therefore, we asked agencies about the Legislature's role and their responses suggest some opportunity for change. Some administrative problems could be avoided by more carefully crafted legislation. Many of these problems are unique to individual grant programs and could be resolved by more consultation between legislators and agency staff when drafting new grant legislation.

The Legislature's role in grant making varies widely. Table 4.1 shows this variety with a continuum of "legislative involvement," by which we mean the degree to which laws and statutes determine to whom a grant should be given or how it should be structured.

At one end of the continuum, reflecting more legislative involvement, are direct appropriations. These are grants through which the Legislature appropriates money to nonstate organizations through state agencies. Direct appropriation laws may stipulate the purpose of the funding or conditions of receiving the funds, such as matching requirements. At the other end of the continuum are competitive grant programs in which a state agency is responsible for selecting grant recipients. For competitive programs, the Legislature varies in how much discretion it leaves to state agencies to select grantees and design program components. We asked agencies specific questions about the Legislature's role in grant management and, in this chapter, provide a more complete account of what we learned.

Period of Availability of Funds

In Chapter 3, Finding 7, we discussed administrative issues relating to the period of availability of funds. In addition, we asked agency officials whether legislative grant requirements "unnecessarily limit flexibility in use of grant funds," and we received a mixed response. Ten agency heads said "do not limit," nine said "somewhat limit," one said "severely limit," and four said "don't know."

One problem agency heads pointed to was the limited time for which grant funds are sometimes available. But the responses to a specific question about that problem also brought a mixed result. Ten agency heads said there are "no problems" with working in the time limits set by the Legislature for grant money, nine said there are "some problems," and five said there are "many problems."

Special Review: Minnesota Grants Administration

**Table 4.1
Legislative Involvement in Grant Making**

	More Legislative Involvement	
Direct appropriations		The 1999 Legislature appropriated \$606,000 the first year and \$348,000 the second year of the 2000-01 biennium to the Historical Society to act as a fiscal agent in disbursing money to various organizations. ¹
Grantee named by Legislature		The Legislature appropriated \$70,000 each year of the 2000-01 biennium to Minnesota Technology, Inc. for grants to the Minnesota Inventors Congress. ²
Grantee implied by Legislature		The 2000 Legislature appropriated \$135,000 to the Department of Health for a grant to “a Minnesota organ procurement organization that is certified by the federal Health Care Financing Administration or to an entity that is a charitable entity under section 501(c)(3) of the Internal Revenue Code of 1986 and is created by an organ procurement organization that is certified by the federal Health Care Financing Administration.” ³
Competitive program with more statutory guidance		The statute creating the learn and earn graduation achievement program includes grantee eligibility criteria for participating students, components that must be part of each program, and program outcome measures. ⁴
Competitive program with less statutory guidance		The Department of Corrections administers the juvenile restitution grant program. The agency was charged with developing criteria for judging applications and working with other agencies to design suitable programs that provide services to communities. ⁵
		Less Legislative Involvement

¹ *Minn. Laws* (1999), Chapter 223, Article 1, Section 17, Subd. 5.

² *Minn. Laws* (1999), Chapter 223, Article 1, Section 3.

³ *Minn. Laws* (2000), Chapter 492, Article 1, Section 18, Subd. 2.

⁴ *Minn. Statutes* (2000), 124D.32.

⁵ *Minn. Statutes* (2000), 242.39.

Special Review: Minnesota Grants Administration

The fund availability problems mentioned by agency staff referred to either (1) the length of time for which grant funds are appropriated or (2) grant beginning and end dates coinciding with the state fiscal year. According to agency staff, there are factors beyond grantee performance issues that could affect the ability of a grantee to complete work within certain time periods. For example, if a competitive process takes months to complete, the grant recipients will end up with a comparatively short time in which to accomplish the grant objectives. The competitive process aside, some agency staff said that one- or two-year grant periods are not always long enough to accomplish the objectives of the grants. And if fund availability is tied to the state fiscal year, but the grants fund programs, such as agricultural programs or summer recreation programs, that operate on another cycle, grant-funded activities might not be completed by June 30, the end of the state's fiscal year.

Naming Grantees in Law

As mentioned in Chapter 1, we estimated that 14 percent of grant dollars were directed by the Legislature to specific recipients. We asked agency heads whether their agency's approach to grant management changed if the grant recipient is specified in statute. Seven said "yes," twelve said "no," and five said the question was "not applicable." The most common change in approach indicated by agencies was that agencies consider these kinds of grants to be "non-competitive" and do not, therefore, advertise their availability or have any kind of selection process.

In our roundtable discussion with agency staff, we asked about oversight of grants where the recipient is specified in law. While some staff said they felt that their agencies were just being used as a "conduit" to pass money through to another organization, most felt they still had a responsibility to provide some oversight. As one person said:

Lots of times we may not fully understand what the motivation is behind certain grant recipients being specified, but ... [legislators] are the policy makers for the state.... At the same time, we do feel like we have to provide a responsible level of oversight....

Another said:

We're very concerned about how the [the grant recipients are] going to spend the money. Just because the Legislature said they were going to have the money ... it's like, Okay, [but] we have to answer to the Legislature, so what are you going to do with the money? Are you going to complete something, get it done?

Some staff said that even if the recipient is named in law, they still require the recipient to have a grant application and may require the recipient to provide some documentation of performance. Determining performance objectives in these cases can pose a challenge. One grant manager noted:

Special Review: Minnesota Grants Administration

This grant was created from legislative desires and directed to a specific grantee for disbursement. It would have been beneficial if specific performance measures had been provided by the Legislature or staff to determine if these funds met their objectives as they intended.

But agencies also said that the Legislature generally does not provide their agencies with money to support oversight of grant recipients. As one staff person said:

The pass through has gotten pretty intensive. So much so that we had to go in and request money because they were just loading us up with so many of these pass-throughs going to specific individuals or specific organizations or entities that we just couldn't administer them.

In addition, some agency staff noted that at times their agencies had been used as a conduit for grants even though the agency did not have the necessary expertise to oversee them. According to an agency official:

You have many of these [pass-through grants] that have a very tenuous connection with anything to do with [the department]. To have proper oversight, you would need to have people in those functions.... We don't have those [people] in many cases.

Conclusions

As indicated in the responses and comments highlighted above, some administrative problems could be avoided by more carefully crafted legislation. Many of these problems are unique to individual grant programs and could be resolved by more consultation between legislators and agency staff when drafting new grant legislation.



January 23, 2002

Office of the Commissioner
200 Administration Building
50 Sherburne Avenue
St. Paul, MN 55155
Voice: 651.296.1424
Fax: 651.297.7909

James R. Nobles, Legislative Auditor
Office of the Legislative Auditor
1st Floor South – Centennial Building
658 Cedar Street
Saint Paul, MN 55155

Dear Mr. Nobles:

Thank you for the opportunity to discuss and comment on the recommendations arising from your special review of state grants administration. We appreciate the efforts of your office in completing this review and highlighting the variation and complexity of state grant programs.

Recommendation

- 1. When awarding grants, agencies should execute standardized contracts that contain all required provisions, as well as clear and specific information on the quantities and types of services to be performed. Agencies should follow the Department of Administration's Contract Manual when drafting grant contracts.*

Response

The Department of Administration agrees with the recommendations that agencies should (1) "execute standard grant contracts that contain all required provisions" and (2) "follow the Department of Administration's Contract Manual when drafting grant contracts."

To further enhance the value of the Contract Manual, Admin will review the Office of the Legislative Auditor's closure letters to agency heads citing the specific instances of noncompliance identified during the audit. If it appears that clarification or other fine-tuning of the Manual might help prevent future noncompliance, we will make those changes. Admin also will take additional steps to advise agencies to refer to the Contract Manual, and to use the standardized contract template it contains.

Person Responsible:
Kent Allin

Estimated Completion Date:
90 days from receipt of closure letters

Recommendation

2. *The Department of Administration should seek legislation to clarify that procurement conflicts of interest statutes apply to grant contracts.*

Agencies should establish formal policies and procedures that deal with potential conflicts of interest in the grant award process. They should ensure that the policy clearly extends to non-state employees involved in the agencies' grant awarding process.

Response

The Department of Administration agrees that the conflict of interest laws that apply to procurement activities should also apply to grants. Consistent with the OLA's recommendation, Admin has proposed language in its housekeeping bill that would do so.

We also agree that agencies should adopt policies and procedures dealing with conflicts of interest that cover both employees and non-state employees involved in the evaluation and awarding of grants. We believe that Administration's existing policies will provide a good template for agencies to adopt or modify as appropriate

Person Responsible:
Kent Allin

Estimated Completion Date:
Subject to legislative action

Recommendation

3. *After consulting with state agencies, the Department of Finance should establish appropriate cash management policies for disbursement of grant funds.*

Response

The Department of Finance agrees with this recommendation and will continue to meet with state agencies to address cash management policies for the disbursement of grant funds. Our draft revision of the grants management operating policy and procedure released for agency comment in November, instructs agencies to disburse grant monies on a reimbursement basis, based on evidence of contract performance. The department does however, recognize that certain grantee relationships may justify another payment method and will continue efforts to address and establish a clear cash management policy for such circumstances.

Person Responsible:
Barb Ruckheim

Estimated Completion Date:
Subject to legislative action

Recommendation

- 4. The Departments of Finance and Administration should work with state agencies to require potential grantees to report, as part of the grant application process, other grants received from the state.*

State agencies should seek information concerning potential grantee past performance from other state agencies when making grant awarding decisions.

Response

The Departments of Finance and Administration agree that we “should work with state agencies to require grantees to report, as part of the application process, other grants received from the state” and that “state agencies should seek information concerning potential grantee past performance from other state agencies.” That second recommendation is most applicable in instances where the awarding agency has no previous history with the potential grantee but could “check references” with other state entities.

Our departments will implement the recommendation by adding language to our instructional materials. More specifically, Admin will revise the grants chapter of its Contract Manual at the same time it makes the modifications proposed in response to recommendation #1.

Person Responsible:
Kent Allin

Estimated Completion Date:
90 days from receipt of closure letters

Recommendation

- 5. The Department of Finance should ensure there is appropriate accountability for the use of grant funds by working with state agencies to: coordinate grantee monitoring and auditing among agencies; or refine agency reporting requirements and determine the monitoring necessary to ensure the validity of submitted grantee information.*

Response

The Department of Finance agrees there is a need for accountability in the use of state grant funds. The diverse nature of grantees and the limited resources available to state agencies for monitoring makes this a complex issue. The department will work with state agencies to evaluate the costs and benefits of different monitoring strategies and develop guidelines/benchmarks for agency use in monitoring different types of grants.

Person Responsible:
Peggy Ingison/Lori Mo

Estimated Completion Date:
October, 2002

Recommendation

6. *Agencies should pay grantees in accordance with applicable contract and other legal provisions.*

Response

Finance and Administration certainly agree with the recommendation that “agencies should pay grantees in accordance with applicable contract and other legal provisions.”

Administration’s Contract Manual specifically advises agencies to carefully consider appropriate payment terms and cautions against advance payments for anything beyond startup costs. Our grant contract boilerplate emphasizes in bold type that work under a grant must not begin until the grant contract is fully executed and the state’s representative has given the go-ahead.

The problem described is compliance with the terms and conditions of a signed grant contract. Only the agency administering the grant can correct the identified errors. However, our departments will continue to provide instructional materials (e.g. Contract Manual) and informal guidance to agencies on this topic.

Recommendation

7. *The Department of Finance should seek legislation to clarify statutory provisions regarding the availability of grant appropriation balances. The department should continue to work with state agencies to address concerns on the availability of funds related to specific grant programs.*

Response

Finance agrees with this recommendation and has submitted language to clarify the period of availability for grant funds and revised the grants management policy and procedure accordingly. State agencies with grant activity that require funds to be available longer than the policy permits, have been instructed to work with their executive budget officer to develop statutory exceptions with a specific end date.

Person Responsible:
Peggy Ingison/Lori Mo

Estimated Completion Date:
Subject to legislative action

Recommendation

8. *The Department of Finance should establish a common definition of grant programs and revise accounting system coding, if necessary.*

The department should work with state agencies to ensure there is a clear understanding of the required coding structures relating to the recording of grant expenditures.

Response

Operating policies and procedures issued by the department define grants as, “financial assistance paid or services furnished by a state agency via a third party to an eligible recipient.” Still, the difference between a grant and a professional technical contract is not always clear. The department relies heavily upon whether the law specifies the money to be a grant.

The accounting system contains standardized coding as well as agency specific account codes. Agencies are given the flexibility to establish account structures in the accounting system to meet their unique needs. Object codes are standard across state agencies and agencies are instructed to code grants in the accounting system according to the following object categories/classes:

40 Payments to Individuals

4A0 Payments to Individuals – Medical/Rehab

4B0 Payments to Individuals – Other than Medical/Rehab

50 Local Assistance

5A0 Aid to Counties

5B0 Aid to Cities and Towns

5C0 Aid to School Districts

5D0 Aid to Higher Education Institutions

5E0 Aid to Other Governments

5F0 Interagency Grants

5G0 Aid to Non-government Organizations

Object codes provide a further breakdown of the categories/classes shown above. Finance will meet with the Office of the Legislative Auditor to review specific examples of coding issues and will revise definitions to clarify proper coding where necessary.

Person Responsible:
Mary Bogie/Peggy Ingison

Estimated Completion Date:
July, 2002

Very truly yours,

/s/ David Fisher

/s/ Pam Wheelock

David Fisher, Commissioner
Department of Administration

Pam Wheelock, Commissioner
Department of Finance