DECISION AND ORDER - AUDIT RESOLUTION


As the result of an audit (No. 17-93-001-03-315) of the Unemployment Insurance Automation Support Account (UIASA) covering a 1988 grant to the Virginia Employment Commission (VEC State) certain expenditures of grant monies were disallowed by the Department of Labor (DOL). Initially, the audit report questioned $1,207,572.00 charged as costs to the grant. A final determination allowed $881,555.00, and disallowed $326,117.00 in costs for which DOL demanded reimbursement. VEC requested a hearing.

A pretrial conference with the parties was conducted by telephone conference call. The parties agreed that facts were not in dispute. Moreover, they agreed on the legal questions presented. Accordingly, they submitted a stipulation of facts, and briefs on the legal questions.

The following is the stipulation of facts submitted by the parties:

STIPULATION OF FACTS

1. Between April 15, 1987, and September 23, 1987, the Virginia Employment Commission ("VEC" or "Virginia") obligated $291,345.50 in fiscal year 1987 Unemployment Insurance ("UI") grant funds, received from the United States Department of Labor ("DOL"), for automation equipment as follows:
   a. $262,656 for a laser printing system on April 15, 1987;
   b. $6,792.50 for a control unit on September 11, 1987;
2. Between October 7, 1987, and March 18, 1988, Virginia Obligated $34,672 in fiscal year 1988 UI grant funds, received from DOL, for automation equipment as follows:

   a. $4,790 for five cathode ray tubes, and $3,615 for a printer on October 7, 1987;

   b. $19,160 for twenty cathode ray tubes on February 23, 1988; and

   c. $3,832 for four cathode ray tubes, and $3,275 for a printer on March 18, 1988.

3. On July 28, 1987, ETA's Philadelphia Regional Office issued Regional Field Memorandum UI No. 18-87 to the state employment security agencies ("SESAs"). This field memorandum solicited applications for fiscal year 1988 Unemployment Insurance Automation Support Account ("UIASA") grant awards.

4. The UIASA is used to help SESAs upgrade their UI automation systems, and thereby improve customer service through enhanced efficiency and decreased delays due to system failures. [DOL Office of Inspector General ("OIG"), Audit Report No. 17-93-001-03 --315 on VEC UIASA ("the Audit Report") at 3 (Nov. 12, 1992)]. AF 54.1 ETA awards UIASA grants to SESAs based on the criteria set forth in the applicable field memorandum. Id. at 3, AF 54. Regional Field Memorandum UI No. 18-87, which set the criteria for the 1988 awards, stated that UIASA funds would be given only to state agencies that demonstrated that other available funds were not sufficient to accomplish their proposed projects. Regional Field Memorandum UI No. 18-87 at 2, 5 (July 28, 1987) AF 138, 141.

5. In September 1987, Virginia applied for a fiscal year 1988 UIASA grant. The Commonwealth's grant application stated that no existing funds were available to carry out its UIASA proposals and that all its current funds were obligated for existing operations. VEC's Proposal for Data Entry Equipment Replacement at 1 (Sept. 1987), AF 113; VEC's Proposal for Purchase of UI Laser Printing System at 2 (Sept. 1987), AF 119;
VEC's Proposal for Local Office Equipment Replacement at 1 (Sept. 1987), AF 132.


7. On receipt of this April 13, 1988 notice, Virginia transferred obligate UI grant cost of $262,656 for its laser printer its just-awarded UIASA grant. VEC's Response to the Audit Report at 1 (Jan. 15, 1993), AF 45. Subsequently, between July and December 1988, Virginia transferred an additional $63,361 in obligated UI grant costs for other automation equipment, see supra. paras. lb-c and 2, to its UIASA grant.

VEC's May 5, 1993 letter at Attachment I, AF 27. The Commonwealth paid the costs for the laser printer and November 9, 1988. Id. at Attachment I, AF 27.

8. On November 12, 1992, the OIG issued its audit report on Virginia% UIASA grant. The OIG recommended that ETA disallow grant costs of $1,181,305 for pre-award and post-funding-period equipment purchases and unauthorized equipment and service purchases. Audit, Report, AF 51-89.

9. During the informal resolution period, ETA's Grant Officer allowed questioned costs of $881,555 for post-funding-period and unauthorized purchases. Initial Determination (Mar. 8, 1993) at 10-14, AF 39-43. The Grant Officer also disallowed additional costs of $26,267 for pre-award procurement obligations, based on information that Virginia provided in response to the Initial Determination. Final Determination at 8 (May 21, 1993), AF 15.

10. On May 21, 1993, the Grant Officer issued his Final Determination, disallowing costs of $326,017 for pre-award procurements. Final Determination at 9-12, AF 16-19.

ISSUES

DOL contends that the Grant Officer properly disallowed the costs of $326,017 occurred in 1987 for the pre-award procurement of computer equipment: Virginia improperly charged costs of equipment in 1987 to the grant before it was awarded 1988. The procurement funds were taken from other Unemployment Insurance sources prior to the application for the award, and charged to the 1988 award.

This procedure violated the conditions of funding. UIASA grants are for the use of state agencies that have no other available source of funds. In effect, the state obtained the
UIASA grant under false pretenses since it represented to DOL that it had no existing funds to buy this equipment.

VEC ARGUMENTS

VEC contends that it complied with the spirit of the UIASA grant: the laser printing system VEC purchased comported with its proposal and the purposes of the UIASA grant. VEC sees the issue explicated in two paragraphs from the Final Determination:

In the May 5th response, the VEC explains that the procurement of the laser printer, which was in addition to an existing unit, was necessitated by the circumstances of early 1987 when the agency's workload had exceeded the capacity of the existing printer and there was no backup to that unit upon which the agency had grown to depend. The VEC's letter emphasized that the Commonwealth's protracted procurement procedures served as the impetus to begin the process early, thus allowing time to locate a source of funds in the 1988 fiscal year when it was anticipated the bill would become payable. The obligation of FY 1987 funds notwithstanding, VEC contends that there were insufficient 1987 funds available and that the excess obligations would be carried forward into 1988. When the obligation became payable in FY 1988, VEC contends that had the UIASA grant not become available, reductions in expenditures for service delivery staff would have had to have occurred. The response relies heavily on the opinion that it is not "the intent of the UIASA . . . to fund state automation enhancements jointly after a state reduces all other expenditures, at the expense of service delivery, in an effort to make non-UIASA funds available. If one were to accept the interpretation of the Grant Officer, no SESA could accurately state that other funds are not 'available'." Thus the VEC's argument implies that the ETA's position would produce unwarranted interference into the management of the UI administrative grant.

However, the circumstances VEC describes should not occur because the provisions of ETA's memorandums required that funds already committed to automation be expended for that purpose, not reduced through substitution of UIASA grant funds as was done by VEC. Furthermore, ETA's criteria do not require concomitant reductions to other budget categories as VEC's argument asserts. In this instance, the VEC retained authority over the agency's own budget, wherein the VEC had committed itself--through the obligation of funds--to the laser printer procurement prior to ETA's July 28, 1987 announcement seeking proposals for 1988 UIASA grants. Thus, the proposals submitted were for procurements that had already been determined necessary under VEC's internal procedures as evidenced by the commitment of other
funds; and in the instance of the laser printer, the
commitment had been consummated by final payment. Such
commitments were by necessity, independent of the outcome
of the UIASA grant applications.

VEC argues that the DOL position does not take into
consideration the realities of running the program faced with
urgent needs, slow government procurement, and not having the
funds within the existing grant to meet those needs. As the
State sees it, the program could not continue without the
printers in 1987. Given that need, it employed a practical
solution, and bought the printers on expectation of funds in the
1988 grant. Further, requiring State Employment Security (SESA)
to wait until the grant money is in hand to purchase needed
equipment works a great hardship on the procurement process, and
on the employees of VEC and its clients.

VEC contends that, these problems were recognized by DOL.
On December 16, 1993, ETA Regional Field Memorandum, UI No. 7-94
(FM 9-94) "seemed" to have corrected the problem of timing for
fiscal year 1994,

a. UIASA projects must demonstrate a focus on customer
service.
b. The UIASA criterion relating to funds of last resort has
been eliminated.
c. The funding of proposals on the basis of urgency has
been eliminated.
d. SESAs have additional time, through September 30, 1996,
to obligate FY 1994 UIASA funds. There can be no extensions
of this date.
e. The National Office (NO) is no longer required to delay
granting UIASA funds until April 1.

VEC concludes that it was aware of the timing problems on
the front and back ends of the grant period: "VEC should not be
penalized for anticipating and trying to work around those
difficulties even if VEC figured them out five or six years
before DOL was able to correct them/"

VEC argues that its actions were within its "bottom line"
authority. Documentation of this authority it claims is found in
the Federal Register, Vol. 51, No. 94, May 16, 1986, which
eliminated detailed fiscal oversight and reporting of SESAs in
favor of SESA self monitoring. Further, the budget guidelines
announced in Regional Field Memorandum, UI NO. 1-87, which
provides, in part:

[T]he bottom line authority vested in each State through the
short term Administrative Finance Initiative (AFI) changes
now in effect gives each State full flexibility to shift
dollar resources among program areas (except claims activities) to meet State management needs as long as specified performance objectives and outcomes are achieved.

This means that all resources, including those for State Integrity, will be distributed to the States in a form similar to a block grant.

And, it continues, Regional Field Memorandum, UI NO 8-88 gave SESAS full authority to shift resources among all program categories deemed appropriate to manage programs without DOL approval.

Finally, VEC points out that over five years since the subject audit, it has clean audits. This record, coupled with the fact that repayment of the disallowed funds would work a hardship on the VEC and affect its ability to provide services, should be grounds for relieving VEC of repayment. In the alternative, VEC requests that repayment be made through a reduction in one or more annual UI allocations.

DOL ARGUMENTS

Virginia improperly charged costs to its UIASA Grant that were incurred before the Grant was awarded. The grant was not available for expenditures before it was awarded.

In essence, Virginia obligated and spent the costs in question from other accounts and gambled that it could reimburse these accounts by winning a UIASA award. Federal grant funds, however, cannot be used in such a freewheeling way but are restricted to the purpose and period for which they are granted. Virginia was given its 1988 UIASA grant to buy specified automation equipment in that fiscal year, not to transfer previously obligated costs to an alternative source of funding. By charging these pre-award costs to its UIASA grant, Virginia used that grant for an unauthorized period.

Grant awards may be given only to "state agencies which demonstrate in their applications that other available sources are not sufficient to accomplish the automation objective for which funds are sought." Regional Field Memorandum UI No. 18-87 at 2 (July 28, 1987), AF 138, and [s]tate agencies must consider using other UI and non-UE resources before requesting resources from the UIASA." Id. at 5, AF 141. Virginia had already purchased the equipment from existing funds in 1987 when it applied for the 1988 grant of UIASA funds. DOL maintains that Virginia misrepresented the facts in obtaining the 1988 grant.

To the argument that failure to purchase the equipment would have been detrimental to staff and services, DOL responds that
was not designed to finance ordinary staff costs, which are customarily covered by base grants, but only "one-time capital outlays (including hardware, software, site preparation, etc.)."

Regional Field Memorandum UI No. 18-87 at 3, AF 139.

DOL asks that the Final Determination be affirmed, and that Virginia be ordered to pay DOL the total disallowed costs of $326,017 from nonfederal funds.

DISCUSSION

There are no serious legal questions involved in this case. The regulations and policy relating to grants are clear. The cost of automation equipment purchased in 1987 was not authorized by the grant under which Virginia was operating at the time. And, the 1988 grant did not authorize payment for equipment purchased in the previous year. The defenses of VEC are equitable: VEC complied with the spirit of the UIASA grant; and, the actions of VEC were within it "Bottom Line Authority". Moreover, VEC finds that the regulations prohibiting procurement until the funds are in hand is unrealistic: the urgent needs of the program cannot be deferred pending receipt of the funds.

These defenses are appealing, but they lack support in law. VEC cites no law, or any reasonable interpretation of the law and regulations to support its position. In the absence of some authority, it is not within my power to forgive the disallowed funds.

As described by VEC, its needs were urgent at the time it purchased the automation equipment. There was no money in the existing grant. Again, according to VEC, it could not provide the services essential to the program without the equipment. Interpreting all of this in favor of VEC, there are no exculpating rules of law.

On the other hand, VEC had a simple expedient available to it at the time of its extra legal-purchase: it could have presented the problem to the Grant Officer, and asked either for permission to make the purchase, or for a legal opinion on the validity of the planned purchase. It failed to take this option. In going ahead with the purchase without prior approval, it took a calculated risk that its action would not be approved. It lost.

Regional Field Memorandum U NO 7-94 (FM 9-94), cited by VEC supports the position of DOL. The memorandum is instructive on the use of UIASA funds:

Funds granted under the authority of the UIASA are for the express purpose presented in the SESA's proposal as approved including any clarifications or stipulations made by the
Department. SESAs which need to redirect an approved project **MUST** submit a written request through the Regional Office (RO) and receive advance written approval from the NO. A redirection is a change in the **goals and objectives** of the project from those outline in the State's original proposal for which the grant was awarded. **Funds redirected without written approval are subject to recapture and/or audit exceptions.**

id. 3, UIASA Funding Policies and Guidelines.

These same operating conditions prevailed in 1987 and 1988. VEC had an obligation under the provisions of the guidelines to seek guidance on its planned purchase of automation equipment. Having failed in that duty, it incurred this disallowance, and rightly so. The Final Determination of the Grant Officer must be affirmed.

In its brief, Virginia requested that any repayment be made through a reduction in one or more annual UI allocations. I view this request to be outside the relief required by this case. In the first place, there is no guarantee that the UI program will continue in its present form. Secondly, determining the entitlement of Virginia to funds from the program calls for speculation. If the payback is to be less painful, the method of repayment is a matter between the U. S. Department of Labor, as judgment creditor, and the State of Virginia, as judgment debtor.

**ORDER**

It is ADJUDGED and ORDERED that the Final Determination of the Grant Officer, dated May 21, 1993, be, and is hereby affirmed, and the State of Virginia is ordered to pay the disallowed costs of $326,017 to the United States Department of Labor from nonfederal funds.

[Signature]
APPEAL NOTICE: The decision of the administrative law judge shall constitute the final action by the Secretary unless, within 20 days after receipt of the decision of the administrative law judge, a dissatisfied party files exceptions with the Secretary specifically identifying the procedure, fact, law, or policy to which exception is taken. Thereafter, the decision of the administrative law judge shall become the final decision of the Secretary unless the Secretary, within 30 days of such filing, has notified the parties that the case has been accepted for review. 29 U.S.C. §1576(b).
Service Sheet

Case Name: Commonwealth of Virginia

Case No. : 93-JTP-24

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