

**Agreed-Upon Procedures on the
State of California,
Employment Development Department's
Year 2000 Grant Expenditures**

FINAL REPORT

This Agreed Upon Procedures Report was performed by the Accounting Firm of Harper, Rains, Stokes & Knight, P.A. under contract to the U.S. Department of Labor - Office of Inspector General, and, by acceptance, it becomes a report of the Office of Inspector General.

Assistant Inspector General for Audit

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ACRONYMS

DOL	U.S. Department of Labor
ES	Employment Service
ETA	Employment and Training Administration
FM	Unemployment Insurance Field Memoranda
FY	Fiscal Year
IV & V	Independent Verification and Validation
JS	Job Service Branch of California Employment Development Department
JTPA	Job Training Partnership Act
CAEDD	California Employment Development Department
OIG	Office of Inspector General
RA	Regional Administrator
SBR	Supplemental Budget Request
SESA	State Employment Security Agency
SOF	Statement of Facts
UI	Unemployment Insurance
UIPL	Unemployment Insurance Program Letters
Y2K	Year 2000

EXECUTIVE SUMMARY

During Fiscal Years (FYs) 1998 and 1999, Congress appropriated funds to help State Employment Security Agencies (SESAs) make their automated Unemployment Insurance (UI) and Employment Service (ES) systems Year 2000 (Y2K) compliant. The U.S. Department of Labor (DOL), Employment and Training Administration (ETA), awarded the California Employment Development Department (CAEDD) grants totaling \$11,266,110 from funds available for Y2K readiness. Qualifying Y2K-readiness costs incurred by all of CAEDD's branches were \$15,151,343.¹

As part of this engagement, we examined direct and allocated charges of \$15,097,542 the Y2K grants that occurred from their inception through September 30, 2000, and found CAEDD did not always comply with requirements governing use of the funds. We have questioned \$848,643² consisting of:

- \$603,963 of staff salary and fringe benefit costs that did not satisfy criteria for reimbursement as Y2K expenditures;
- \$151,516 of hardware costs incurred by CAEDD that were unsupported with regard to their being Y2K necessary in accordance with the terms of the grants;
- \$73,376 of miscellaneous costs charged to the grants that were incurred prior to October 1, 1997 (\$93,676 of expenditures less \$24,300 of hardware costs included in the finding on unsupported hardware costs above);
- \$18,545 of expenditures for unidentified and unreconcilable amounts which were charged to the grants; and
- \$ 1,243 of tuition and book costs that were not Y2K related.

¹ Although additional costs were incurred for the project, this amount represent costs from the inception of the project until March of 1999, when ETA-provided funding was exhausted.

² In the draft report, we questioned \$1,068,626 which has been reduced by a total of \$224,983 because of additional documentation provided in CAEDD's response to the draft report.

We recommend the Assistant Secretary for Employment and Training recover grant expenditures, totaling \$848,643 related to the findings identified.

INTRODUCTION AND PRINCIPAL CRITERIA

ORIGIN AND PURPOSE OF Y2K FUNDS

In FY 1998, concerns with the approach of Y2K and the potential for problems with automated systems prompted Congress to provide SESAs with grants that totaled \$200 million. The funds were to help ensure SESAs' automated UI and ES systems were Y2K compliant.

ETA distributed base funding of \$1 million to each of the 53 SESAs. In addition to base funding of \$53 million, ETA awarded \$9,540,000 (\$180,000 to each SESA) to develop business continuity or contingency plans, in the event of Y2K-related shutdowns of critical UI and ES systems, or for independent verification and validation (IV & V) of Y2K compliance measures. During FY 1998, each SESA was also afforded the opportunity to request additional funds for specific Y2K needs, through Supplemental Budget Requests (SBRs). The SBRs detailed specific Y2K-related needs for which the funds were requested. The SBRs were evaluated by a panel consisting of ETA staff, and the funds were awarded based upon what the panel judged were "reasonable and allowable" costs.

In Fiscal Year 1999, ETA reprogrammed an additional \$50 million of UI contingency funds to address the SESAs' Y2K needs. The funds were awarded to the SESAs through SBRs. ETA required the SESAs to demonstrate a "compelling need" for the funds to be considered for the FY 1999 awards.

CAEDD received a total of \$11,266,110 in Y2K grant funds from ETA. In FY 1998, ETA distributed Y2K base and IV & V funds of \$1,180,000 to CAEDD. Also, in FY 1998, CAEDD received additional Y2K grants of \$8,969,737 through two separate SBRs. During FY 1999, ETA awarded an additional \$1,296,373 in Y2K funds which CAEDD had requested in two separate SBRs.

PRINCIPAL CRITERIA

ETA Field Memorandum 50-97, dated August 4, 1997, provided the following guidance for the use of FY 1998 Y2K funds:

The Y2K Compliance projects for which funds are received must focus on activities relating to Year 2000 conversion efforts, the replacement or upgrading of systems, systems interfaces, and/or software products necessary to ensure Y2K

compliance, or replacing or upgrading computer hardware that is not Y2K compliant and that will adversely impact system or program performance if not replaced or upgraded.

Costs incurred by SESA base funded staff assigned to the project on a temporary basis cannot be funded by the Y2K grant; however, overtime costs are allowable. Any staff costs must be for additional staff, not previously funded by the SESAs base grant, or for overtime applied to Y2K activities performed by the technical staff or program personnel.

. . . SESAs are required to include a separate entry for Y2K expenditures in the SF 269 comment section and to maintain documentation supporting all charges to Y2K automation efforts as part of the regular reporting process for Base Expenditures.

SESAs which receive a supplemental Y2K conversion grant and subsequently determine that other hardware or software is more suitable may elect to substitute the more suitable product contingent upon adequately documenting the appropriateness of the substituted purchase and obtaining the agreement of the Regional and National Offices.

Guidance on the use of FY 1999 Y2K supplemental funding was included in ETA Field Memorandum 3-99, dated October 13, 1998:

The Y2K funds received must be used only for activities relating to Y2K compliance efforts, including replacement or upgrading of systems, systems interfaces, and/or software products which will adversely impact system or program performance if not replaced or upgraded. . . .

FY 1999 Y2K funds are intended to meet those identified immediate requirements of those SESAs which, in the absence of these additional funds, are unlikely to achieve Y2K compliance of their employment security automated systems. Thus, compelling need is the primary criterion which will be used in evaluating SBRs. Additionally, the SESA must demonstrate that the funds will materially assist the SESA in achieving its Y2K compliance goals.

Costs incurred by SESA base funded staff assigned to the project on a temporary basis cannot be funded by the Y2K grant; however, overtime costs are allowable. Any staff costs must be for additional staff, not previously funded by the SESAs

base grant, or for overtime applied to Y2K activities performed by the technical staff or program personnel.

. . . SESAs are required to include a separate entry for Y2K expenditures in the SF 269 comment section and to maintain documentation supporting all charges to Y2K automation efforts as part of the regular reporting process for Base Expenditures.

Additional guidance on the use of FY 1999 Y2K supplemental funding was included in ETA Field Memorandum 47-99, dated July 14, 1999:

These funds may not be applied to base staff positions or to support staffing positions otherwise covered by base grants, or to on-going maintenance activities or to on-going communications.

Funds allocated for Y2K can only be used for activities or purchases relating to Y2K compliance efforts, including replacement or upgrading of systems, systems interfaces, and/or software products that, if not repaired or replaced, would adversely impact the UI program.

These funds cannot be applied to purchases of personal computers (PCS), peripheral devices (printers, modems, monitors, etc.) or PC-based office support applications such as electronic mail, spreadsheets, or word processors.

These Y2K funds are intended to meet those identified immediate requirements of SESAs which, in the absence of these funds, are unlikely to achieve Y2K compliance of their UI automated systems.

Funds granted through this process must be applied expressly to those cost items presented within the SBR including any clarifications or stipulations made by the review panel. State agencies that wish to redirect funds from an approved cost item must request such changes through the Regional Office and must receive advance written approval from the National Office. Funds redirected without such approval are subject to recapture or audit exception.

The "Executive Summary" of ETA's "Year 2000 SBR Review Panel's Briefing Package" stated that SESAs should prioritize their spending to best meet their own critical needs, and that ETA Regional Offices should:

. . .strongly encourage the SESAs to initially concentrate their efforts and resources on making UI Benefits systems compliant, as they are mission critical and will be the first to fail. Before funds are spent on PC upgrades and replacements, mission critical systems need to be converted and tested for compliance.

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**INDEPENDENT ACCOUNTANTS' REPORT
ON APPLYING AGREED-UPON PROCEDURES**

We have performed the procedures described in the engagement program provided by the U.S. Department of Labor, Office of Inspector General (OIG), which were agreed to by the OIG, solely to assist in evaluating the State of California Employment Development Department's (CAEDD) compliance with the terms and provisions of the Y2K grants as noted in the Unemployment Insurance Field Memoranda (FM) and Program Letters (UIPL).

This agreed-upon procedures engagement was performed in accordance with attestation standards established by the American Institute of Certified Public Accountants and Government Auditing Standards, issued by the Comptroller General of the United States.

The sufficiency of these procedures is solely the responsibility of the OIG. Consequently, we make no representations regarding the sufficiency of the procedures described in the engagement program, either for the purpose for which this report has been requested or for any other purpose.

The results of our procedures are enumerated in the section titled "Results of Agreed-Upon Procedures, within this report.

We were not engaged to, and did not perform an examination, the objective of which would be the expression of an opinion on CAEDD's compliance assertion on its utilization of the funds granted by ETA. Accordingly, we do not express such an opinion. Had we performed additional

procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the use of the OIG and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of the procedures for their purposes.

Harper, Rains, Stokes & Knight, P.A.
Ridgeland, Mississippi
September 20, 2001

OBJECTIVE, SCOPE AND METHODOLOGY

The primary objective of this engagement was to determine whether funds designated for Y2K compliance were spent for intended purposes, in compliance with grant provisions and other applicable Federal criteria.

We examined Y2K grant funds received and the corresponding expenditures of the funds by CAEDD during the period October 1, 1997 through September 30, 2000. We reviewed the SBRs and financial status reports, interviewed state officials and reviewed financial records and other documentation related to Y2K conversion expenditures.

CAEDD received a total of \$11,266,110 from ETA for Y2K compliance activities, all of which was expended as of September 30, 2000. The population of qualifying costs incurred by CAEDD for Y2K readiness for all branches was \$15,151,343.

This total amount of cost was partially allocated to the Job Service (JS)³ and UI branches within CAEDD using an internally-derived allocation percentage based on historical data as detailed in the accompanying Exhibit A. CAEDD officials stated that the reason an allocation percentage was used to charge costs to the grants was that the Y2K project addressed compliance for systems used by all branches of CAEDD. These common systems were not specifically identifiable with any particular branch of CAEDD and so the allocation to JS and UI was determined on another basis.

The \$15,151,343 was the entire amount of cost incurred for all branches over the period which CAEDD received funding. Subsequent to a periodic accumulation of these costs in specific ledger accounts, portions of these costs were isolated, allocated to JS and UI and charged to the grants. The methodology used to accomplish this, however, was inconsistent⁴ over the course of the grant period. It is for this reason that simple application of the allocation percentage derived in Exhibit A to the entire population of costs and addition of the costs of personnel and benefits, which were charged wholly without allocation, will not result in the \$11,266,110 which was charged to the grants.

³ "JS" or Job Service is synonymous with Employment Service (ES).

⁴ Initially, charges were specifically isolated and charged to the grants. Subsequently, charges were isolated wholly from the pool of costs accumulated as mentioned above and then the application percentage was applied. The third and most consistently applied method for charging the grants was the straight application of the allocation percentage to the entire amount of costs accumulated in the pool from the point of the prior transfer.

We examined expenditures for personnel and benefits of \$876,423 which were charged to the grants without allocation, as well as expenditures for contract services, hardware, software and other items totaling \$14,221,119. The costs were allocated by CAEDD in the aforementioned ratio, from the inception of the grant through September 30, 2000.

Our engagement objective was to determine whether Y2K funds were spent for intended purposes, in conformity with the grant agreements and applicable Federal requirements. Our engagement was conducted in accordance with agreed-upon procedures developed by the U.S. Department of Labor, Office of the Inspector General and found in the *DOL-OIG Engagement Guide–Y2K SESA Spending* and included such tests as OIG to satisfy the objectives of the engagement. The agreed-upon procedures engagement was also performed in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States.

Our review of internal controls was limited to those controls related to the FY 1998 and FY 1999 Y2K funds. We did not evaluate CAEDD's general operational internal controls over non-Y2K funds. Our agreed-upon procedures engagement was conducted for the sole purpose of determining if ETA's requirements for the use of Y2K funds had been followed. The expenditures reported by CAEDD as included in the attachment of this report were the sole source of transactions selected for compliance testing. Fieldwork began April 2001 and continued through June 2001.

A Statement of Facts (SOF) containing data collected during our engagement was issued to CAEDD at the conclusion of fieldwork. CAEDD's response to the SOF was considered in preparing both the draft and this final report. The results of our agreed-upon procedures engagement is presented in the "Results of Agreed-Upon Procedures" section of this report.

RESULTS OF AGREED-UPON PROCEDURES

Although CAEDD avoided interruption of ES and UI services, it did not always adhere to ETA's requirements governing the use of Y2K funds. We identified grant expenditures, totaling \$848,643 that were not in accordance with Y2K grant requirements. For purposes of discussion, we have classified those expenditures into the following categories:

- \$603,963 of "base-funded" staff salary and benefit charges;
- \$151,516 of hardware costs charged to the Y2K grants;
- \$73,376 of expenditures retroactively charged to the grants (\$97,676 of expenditures less \$24,300 of hardware costs included in the finding on unsupported hardware costs above);
- \$18,545 that was charged to the grant yet was unsupported and unreconcilable to Y2K expenditures; and
- \$1,243 of expenditures for tuition and books that were unrelated to Y2K but charged to the grants.

**BASE-FUNDED STAFF COSTS OF \$603,963 WERE
IMPROPERLY CHARGED TO THE Y2K GRANTS**

CAEDD improperly charged \$603,963 of staff salary and fringe benefit costs to the Y2K grants.

The DOL provides all SESAs annual appropriations to pay the costs of administering ES and UI activities. Annual appropriations include monies for "base-funded" personal service and benefit costs. ETA established restrictions on how Y2K funds could be spent, to ensure Y2K grant funds were used to pay the additional costs of staff working on Y2K-related problems, and to prevent Y2K funds from being used to supplant the cost of base-funded activities.

To that end, ETA required that personnel costs charged to the Y2K grants be only for the overtime costs of base-funded staff, or for the salaries of additional staff (in excess of base-funded levels) hired to work on critical Y2K-related problems. However, CAEDD did not comply with this requirement resulting in improper charges of \$603,963 of base-funded staff salaries and benefit costs to the Y2K grants.

ETA Field Memorandum Number 50-97, dated August 4, 1997, discusses SESA's compliance activities related to Y2K funding. Under Staff Needs, at Section 6, SBR Proposal Format and Instructions, ETA states:

Costs incurred by SESA base funded staff assigned to the project on a temporary basis cannot be funded by the Y2K grant; however, overtime costs are allowable. Any staff costs must be for additional staff, not previously funded by the SESA's base grant, or for overtime applied to Y2K activities performed by technical staff or program personnel.

ETA reiterated an identical requirement in Field Memorandum 3-99, dated October 13, 1998, concerning staff charging time to FY 1999 Y2K grants funded through SBRs. Also, ETA Field Memorandum 47-99, dated July 14, 1999, provided additional guidance on staff charges to FY 1999 SBRs:

These funds may not be applied to base staff positions or to support staffing positions otherwise covered by base grants, or to on-going maintenance activities or to on-going communications.

CAEDD designated six full-time, base-funded employees along with a single retired annuitant as "dedicated" to the Y2K compliance efforts for the JS and UI programs. In order to satisfy the terms of the grants and qualify their salary and benefits costs as legitimate Y2K grant charges, the seven employees should have spent their effort on, and charged their time solely to, JS and UI Y2K program activities. We found that each of the seven employees charged time to programs other than the JS and UI, indicating their efforts were not entirely dedicated to the JS and UI programs' Y2K compliance efforts. In fact, \$423,680 of the salaries questioned in this finding were charged to programs other than JS or UI.

Moreover, we did not find evidence that the dedicated Y2K employees' positions were backfilled. We concluded that a portion of staff salaries and benefits already being funded by base grants were also being funded with Y2K grant monies. We noted that CAEDD was denied funding in their SBR request for FY 1998 and 1999 because it had not substantiated staff costs. As annotated in a letter dated January 13, 1998, from the Region IX ETA office to the Director of CAEDD:

California's budget plan. . .does not indicate whether staff costs are for new positions, back-filled positions, base staff, or for overtime. Because the costs were so difficult to decipher, the panel added up. . .Personnel and Fringe Benefits (\$2,012,850) and then subtracted half of the total of these costs as not allowed.

CAEDD'S COMMENTS ON THE DRAFT REPORT

In response to our draft report, CAEDD provided additional information regarding the \$705,224 of questioned staff salary and fringe benefit costs. (The entire text of CAEDD's response to this and other findings is included as Exhibit C to this report). The response indicates one of the base-funded staff positions was appropriately back filled. Moreover, the response contests the entire \$705,224 of questioned costs based on Region VII Letter No. 97-33. CAEDD's response provides:

[Individual 1] worked as a manager on the Y2K project in a limited-term position. In January 1998 [Individual 1's] prior position was filled by [Individual 2], recruited from the California Department of Social Services and therefore not a baseline Unemployment Insurance (UI) or Job Service (JS) employee. Information supplied to the auditors by the EDD incorrectly stated that [Individual 2] left that position March 1, 1998, and consequently all charges for in-scope Y2K work by [Individual 1] after February 1998 were disallowed. EDD, on examination of the details of the audit findings, caught their error. [Individual 2] actually remained in [Individual 1's] prior position through May 4, 2001; therefore, charges to the grant for [Individual 1's] services from January 1998 through February 2000 totaling \$101,261, should be allowed.

In addition, we believe the \$705,224 in questioned base-funded staff costs should be allowed per Region VII Letter No. 97-33, Change 1. Letter No. 97-33, Change 1 states that "As soon as the funds become available, a \$1 million base grant will be allocated to each SESA, to be applied to Y2K compliance activities or for the purchase of Y2K related products. The base grant funds may be applied to base staff if the base staff is assigned to work on Y2K activities. Once appropriated, Y2K funds may be applied to allowable costs incurred anytime during FY 1998." Since the Y2K funds were available for a three-year period, the \$1 million more than covers all the base-funded staff costs questioned.

OUR CONCLUSION

Having reviewed this additional information and the accompanying support for its position, the auditors agree that \$101,261 of staff salary and fringe benefit costs, associated with the backfilled position, were spent in compliance with the terms and provisions of the Y2K grants. However, we do not agree that the balance of \$603,963 spent on salary and benefit costs conformed with the Y2K grants' requirements.

The intention of the formal governing criteria for funding staff and fringe benefit costs outlined in Field Memorandum 50-97 was to ensure that grant funds were used to pay the additional costs of staff working on Y2K-related problems. DOL provides all SESAs annual appropriations to pay the costs of administering ES and UI activities. The appropriations, include monies for base-funded personal service and benefit costs. In consideration of this, restrictions were imposed by the Field Memoranda to prevent grant funds from being used to supplant appropriations for the cost of base-funded activities. The Region VII Letter No. 97-33, Change 1, cited by CAEDD as their basis for charging the base funded staff to the cost of the grants is silent to the restrictions imposed by the formal governing criteria, that being the Field Memoranda identified by the auditors in the body of the above finding.

The letter cited in EDD's response was written by ETA regional staff. We have since learned, that its content was taken from an electronic mail message sent by ETA's Office of Regional Management (ORM) to its regional administrators (RAs), on October 7, 1997. Its purpose was "to provide clarification to the funding requirements provided in FM 50-97. . . ."

Both the e-mail and the RA's letter required that regular base positions redirected to Y2K activities funded by the SBR were to be backfilled. However, the correspondence was silent concerning whether regular base positions redirected to Y2K base grant activities needed to be backfilled. Further, both the ORM e-mail and the letter from the RA were disseminated outside of ETA's formal policy-making procedures.

As interpreted by the State, the RA's letter may conflict with the formal governing criteria provided in FM 50-97, which was disseminated nationally, with respect to limitations on the use of the Y2K base grant to fund regular base staff positions. However, as the original e-mail was distributed as a clarification, rather than a change to existing policy, and because it was silent on the issue of the need to backfill regular base positions funded with the Y2K base grant, its meaning was ambiguous at best.

The State's interpretation also contravenes the purpose for which Y2K funds were appropriated and the intent of the restrictions. Y2K grant funds were expected to be spent on Y2K-readiness activities. DOL provides all SESAs annual appropriations to pay the costs of administering ES and UI activities, and the appropriations include monies for base-funded personal service and benefit costs. Restrictions on how Y2K funds could be spent helped ensure the grant funds were used to pay the additional costs of staff working on Y2K-related problems, and prevent Y2K funds from being used to supplant the cost of base-funded activities.

Also, CAEDD's stewardship of its Y2K grants causes us to question whether the State relied on the interpretation and recognized a distinction between restrictions affecting Y2K base grants and SBRs. CAEDD commingled financial activities related to the Y2K base grant and SBR in Y2K

fund ledger accounts. We are unable to determine what activities were paid for by each of the grants, and CAEDD's accounting practices indicate the State did not segregate each of the awards, which should have been done to ensure unallowable base funded salary costs were not charged to the SBR.

Finally, as we previously discussed, the employees in question charged \$423,680 in personnel costs to the Y2K grants even though their time charges indicate they spent the time on activities other than ES or UI, indicating they were not working on ES or UI Y2K-readiness projects. This concern was not addressed in CAEDD's response. We note that no guidance provided by ETA, either formal or as might have been interpreted by CAEDD in the Regional Letter, suggest it was appropriate to use Y2K funds for other activities. Consequently, we continue to recommend recovery of \$603,963.

**UNSUPPORTED HARDWARE COSTS OF \$151,516
WERE IMPROPERLY CHARGED TO THE Y2K GRANTS**

ETA's guidance requires that all SESAs receiving grant funds maintain adequate documentation for all costs which are charged to the grants.

Field Memoranda 50-97, dated August 4, 1997, and 3-99, dated October 13, 1998, each state:

. . . SESAs are required to . . . maintain documentation supporting all charges to Y2K automation efforts as part of the regular reporting process. . . .

Additionally, Field Memorandum No. 50-97 states:

The Y2K Compliance projects for which funds are received must focus on activities relating to Year 2000 Conversion efforts, the replacement or upgrading of systems, systems interfaces, and/or software products necessary to ensure Y2K compliance, or replacing or upgrading computer hardware that is not Y2K compliant and that will adversely impact system or program performance if not replaced or upgraded.

CAEDD charged hardware costs of \$151,516 to the grant but did not provide adequate documentation to support their relevance to Y2K. As a result, we could not determine the necessity of these purchases for Y2K readiness. Furthermore, there was no discernible relationship between the items purchased with grant funds and those items that might have been replaced due to their nonconformity with Y2K standards. (See Exhibit B, Part 1.)

CAEDD'S COMMENTS ON THE DRAFT REPORT

In response to our draft report, CAEDD argued that \$62,057 of the \$213,573 in hardware costs questioned in our draft report were allowable. CAEDD's argument centered on the necessity of purchasing desktop computers for Y2K contractors and the need to acquire hardware for a "command center".

The response indicated:

The EDD requests consideration for allowance of \$62,057 in questioned costs as follows:

The EDD's contract with International Business Machines Corporation (IBM) Global Services for consulting staff to supplement our Y2K project team required EDD to provide workstations for IBM consultants. The Y2K project is identified in EDD records as cost center 3461. This cost center was exclusively for Y2K project staff, and all consulting staff reported to this cost center. The number of consultants provided by IBM under the contract varied, with the peak being 29 consultants in February 1999. Included in the hardware purchases identified in the audit as disallowed charges were purchases of 19 desktops and monitors, plus 10 printers and related equipment used to provide workstations for IBM consultants to the Y2K projects. These charges, totaling \$52,663 should be allowable under the terms of the grant.

Hardware costs totaling \$9,394 were incurred to set up a command center to continue primary Department functions in the even that Y2K problems caused power and communication outages. Our primary focus for continuity of operations was UI check processing.

OUR CONCLUSION

Having reviewed this additional information and the support CAEDD provided for their position, the auditors agree that \$62,057 of the \$213,573 in hardware costs complied with the terms and provisions of the Y2K grants. However we continue to question \$151,516 as unallowable Y2K grant costs.

**RETROACTIVE CHARGES OF \$97,676
WERE MADE TO THE Y2K GRANTS**

We identified \$97,676 of items purchased prior to October 1, 1997, from Y2K grant funds.

ETA Field Memoranda No.'s 50-97, 3-99, and 47-99 all require that funds appropriated to the SESAs be made available for use

in the fiscal year issued and not be retroactively applied to any work performed or to any products purchased prior to October 1, 1997.

Field Memorandum 50-97 dated August 4, 1997, provides:

. . . funds cannot be applied retroactively to work performed or products already purchased prior to October 1, 1997.

In isolating charges from the pool of Y2K costs for their application to the first transfer of funds related to the Y2K grants, CAEDD included several items of software and hardware that were purchased prior to October 1, 1997. Included in these costs are \$24,300 of hardware costs included in the finding on unsupported hardware costs above. Exhibit B, Part 2 provides the details of purchases prior to October 1, 1997.

CAEDD'S COMMENTS ON THE DRAFT REPORT

CAEDD did not comment on this finding.

OUR CONCLUSION

We continue to recommend recovery of \$73,376 in retroactive charges to the Y2K grants. This amount is net of the \$24,300 in hardware charges already questioned in the previous finding.

**UNRECONCILED AMOUNTS TOTALING
\$18,545 WERE CHARGED TO THE Y2K GRANTS**

In determining the means by which costs were charged to the grants, we reconciled the amount of each specific transfer of Y2K grant funding from CAEDD's

ledgers to the underlying detail of the associated costs. Thus, the supporting detail of the qualifying costs was evaluated and tested. However, we were unable to reconcile the amounts of the transfers to the underlying detail, in some instances.

Field Memoranda 50-97, dated August 4, 1997, and 3-99, dated October 13, 1998, each provide:

. . . SESAs are required to . . . maintain documentation supporting all charges to Y2K automation efforts as part of the regular reporting process. . . .

As a result of our reconciliations, we identified \$18,545 of costs that were charged to the grant, in excess of supporting detail for these costs. A listing of unreconcilable amounts can be found in Exhibit B, Part 4.

CAEDD'S COMMENTS ON THE DRAFT REPORT

CAEDD did not comment on this finding.

OUR CONCLUSION

We recommend recovery of \$18,545 of Y2K grant costs.

**TUITION AND BOOKS CHARGES OF \$1,243
WERE NOT Y2K RELATED**

CAEDD charged the Y2K grant \$1,243 for tuition and books that were not related to Y2K compliance efforts .

Guidance on the use of FY 1999 Y2K supplemental funding was included in ETA Field Memorandum 3-99, dated October 13, 1998:

The Y2K funds received must be used only for activities relating to Y2K compliance efforts, including replacement or upgrading of systems, systems interfaces, and/or software products which will adversely impact system or program performance if not replaced or upgraded. . . .

The above amount of cost for tuition and books charged to the grants reflects expenditures for ordinary staff development and not for activities relating specifically to Y2K compliance efforts. Further examination of the detail of these transactions revealed that several employees (beyond the dedicated seven) received the same training and education. This suggests that the costs were ordinary in nature and would have been incurred in the absence of any Y2K remediation efforts. Exhibit B, Part 5 provides the details of purchases of tuition and books with Y2K grant funds that were not related to the Y2K effort.

CAEDD'S COMMENTS ON THE DRAFT REPORT

CAEDD's response contained additional information regarding the cost of tuition and books totaling \$15,079 . The response indicates:

The Mercury Interactive software testing tools were newly acquired by EDD for use by EDD and Y2K contractor project staff. EDD had no prior experience with the tools, and staff had no training in their use. Training for staff in the use of the tools was purchased, and \$13,836 was charged to the grant to cover the cost of training. The audit results incorrectly disallow these charges.

OUR CONCLUSION

After considering the additional information and the support CAEDD provided for their position, we believe \$13,836 of the total \$15,079 spent for tuition and books was used to train staff working on Y2K readiness efforts and complied with the terms and provisions of the Y2K grants. However, we continue to question the remaining of \$1,243 spent on training which was provided for staff not directly involved in Y2K efforts.

RECOMMENDATIONS

We recommend the Assistant Secretary for Employment and Training recover grant expenditures, totaling \$848,643 based on the results of the agreed-upon procedures. Such grant expenditures include:

- \$603,963 of “base-funded” staff salary and benefit charges;
- \$151,516 of hardware costs charged to the Y2K grants;
- \$73,376 (97,676 of expenditures retroactively charged to the grants less \$24,300 of hardware costs included in the finding on unsupported hardware costs above);
- \$18,545 that was charged to the grant yet was unsupported and unreconcilable to Y2K expenditures.
- \$1,243 of expenditures for tuition and books that were unrelated to Y2K but charged to the grants.

ATTACHMENT

CALIFORNIA Y2K EXPENDITURES*
AS OF SEPTEMBER 30, 2000

	<u>SBR</u> <u>FY 1998</u>	<u>SBR</u> <u>FY 1999</u>	<u>TOTAL</u>
EXPENDITURES:			
PERSONAL SERVICES	\$ 494,908	\$ 67,207	\$ 562,115
PERSONNEL BENEFITS	<u>294,452</u>	<u>19,856</u>	<u>314,308</u>
TOTAL PERSONNEL COSTS	<u>789,360</u>	<u>87,063</u>	<u>876,423</u>
TRAVEL	7,930	1,621	9,551
EQUIPMENT RENT	156,154	-	156,154
EQUIPMENT EXPENSES	208,883	3,960	212,843
SERVICES	8,743,856	1,196,716	9,940,572
OTHER	<u>45,267</u>	<u>7,013</u>	<u>52,280</u>
TOTAL NONPERSONAL SERVICES	<u>9,162,090</u>	<u>1,209,310</u>	<u>10,371,400</u>
TOTAL CAPITAL EXPENDITURES	<u>18,287</u>	<u>-</u>	<u>18,287</u>
TOTAL OPERATING EXPENSE	<u>\$ 9,969,737</u>	<u>\$ 1,296,373</u>	<u>\$ 11,266,110</u>

* As represented in Status of Obligational Authority Report No. 61 as of September 30, 2000 by CAEDD

EXHIBIT A

**CALIFORNIA EMPLOYMENT DEVELOPMENT DEPARTMENT
CALCULATION OF ALLOCATION PERCENTAGE
FOR JS AND UI PROGRAMS**

<u>Project Code(Branch)</u>	<u>1997 Person Years*</u>	<u>Branch Percentage</u>	
210 (UI)	4,366.0	54.91 % **	
637 (DI) 1,662.2	20.91 %		
205 (JS)	1,135.3	14.28 % **	640 (PIT)
347.3 4.37 %			
803 (JTPA) 255.7 3.22 %			
622 (ETF) 66.0 .83 %			
623 (ETP) <u>118.2 1.48 %</u>			
	<u>7,950.7</u>	<u>100.00 %</u>	

* Person years denotes the number of person hours per year for each branch within CAEDD. The above values are for Fiscal Year 1997 which was used as the base year to establish the relative percentages for each branch; these percentages were then applied in each sequential year in which the project occurred.

** 54.91% UI + 14.28% JS = 69.18% Allocation Percentage

EXHIBIT B

**DETAIL OF RESULTS OF
 AGREED-UPON PROCEDURES**

<u>Expense Code</u>	<u>Doc Number</u>	<u>Vendor</u>	<u>Before Allocation</u>	<u>After Allocation</u>
<i>Part 1 - Hardware charges:</i>				
645	CM810775	Dell Marketing	\$ 3,329.49	\$ 2,303.34
645	CM810773	Dell Marketing	19,976.85	13,819.98
645	CM810794	Government Stores	8,975.58	6,209.31
645	CM813396	Government Stores	18,037.35	12,478.24
645	CM813399	Dell Marketing	3,417.32	2,364.10
645	CM813399	Dell Marketing	42,716.40	29,551.21
645	CM814662	Quest Media	223.04	154.30
645	CM814747	Dell Marketing	9,849.45	6,813.85
645	CM815452	Quest Marketing	3,986.75	2,758.03
645	CM819221	Dell Marketing	8,423.89	5,827.65
645	CM819221	Dell Marketing	3,161.39	2,187.05
645	C820861	GE Capital	6,975.37	4,813.00
645	CM911252	CCS/Entex	10,148.46	7,020.71
645	C930666	GE Capital	3,702.06	2,561.08
645	C930666	GE Capital	148.55	102.77
645	CM931918	Dell Computers	1,341.50	928.05
645	CM931918	Dell Computers	1,479.44	1,023.48
645	CM931918	Dell Computers	20,711.73	14,328.37
645	CM931918	Dell Computers	14,862.75	10,282.05
645	CM931918	Dell Computers	1,390.03	961.62
645	CM931918	Dell Computers	273.87	189.46
645	CM931918	Dell Computers	273.87	189.46
645	CM931918	Dell Computers	1,396.47	966.08
645	CM931918	Dell Computers	49.57	34.29
645	CM931918	Dell Computers	24.79	17.15
645	CM931918	Dell Computers	2,958.82	2,046.91
645	CM931918	Dell Computers	2,958.82	2,046.91
645	CM931918	Dell Computers	14,862.75	10,282.05
645	CM931918	Dell Computers	1,396.47	966.08
645	CM931918	Dell Computers	14,862.75	10,282.05
645	CM931918	Dell Computers	1,390.03	961.62
645	CM931918	Dell Computers	1,399.70	968.31
645	CM931918	Dell Computers	1,486.29	1,028.22
645	CM931918	Dell Computers	2,958.82	2,046.91
645	CM931918	Dell Computers	5,917.65	4,093.83
645	CM931918	Dell Computers	1,390.03	961.62
645	CM931918	Dell Computers	14,794.11	10,234.57
645	CM931918	Dell Computers	16,273.51	11,258.01

EXHIBIT B (Cont.)

**DETAIL OF RESULTS OF
 AGREED-UPON PROCEDURES (Cont.)**

<u>Expense Code</u>	<u>Doc Number</u>	<u>Vendor</u>	<u>Before Allocation</u>	<u>After Allocation</u>
<i>Part 1 - Hardware charges - continued:</i>				
645	CM933461	Dell Computers	\$ 4,816.43	\$ 3,332.01
645	CM931918	Dell Computers	1,396.47	966.08
645	C035322	Dell Computers	2,900.05	2,006.25
645	C035322	Dell Computers	2,823.89	1,953.57
665	CM719671	Ameridata	642.46	444.45
667	CM719592	Dell Marketing	2,201.37	1,522.91
665	C819916	Visiplex Comm	7,904.02	5,453.77
665	CM932002	Dell Computers	12,757.63	8,825.73
665	C933442	GE Capital	4,185.11	2,895.26
665	C933442	GE Capital	1,605.92	1,110.98
			<u>\$ 308,759.07</u>	<u>\$ 213,572.73</u>
<i>Part 2 - Retroactive charges:</i>				
616	CM810792	Softwaire Ce	\$ 5,899.27	\$ 4,081.11
616	CM810792	Softwaire Ce	0.05	0.03
616	CM810778	Softwaire Ce	882.75	610.69
645	CM810794	Government Stores	8,975.58	6,209.31
645	CM810775	Dell Marketing	3,329.48	2,303.33
645	CM810775	Dell Marketing	0.01	0.01
645	CM810773	Dell Marketing	19,976.85	13,819.98
833	M700648A	IBM Global Services	18,765.00	12,981.63
833	M700648A	IBM Global Services	31,522.50	21,807.27
833	M700642	IBM Global Services	16,942.50	11,720.82
833	M700642	IBM Global Services	28,755.50	19,893.05
616	CM719669	Softwaire Ce	450.96	311.97
665	CM719671	Ameridata	642.46	444.45
667	CM719592	Dell Marketing	2,201.37	1,522.91
910	ZV568722656	Government T	229.00	158.42
910	ZV567861283	Government T	240.00	166.03
910	ZV557413457	Government T	80.00	55.34
910	ZV556716088	Automated Co	610.00	422.00
910	ZV556716088	Government T	80.00	55.34
910	ZV552724061	Government T	379.00	262.19
910	ZV548645282	Government T	240.00	166.03
910	ZV547565876	Government T	299.00	206.85
910	ZV445729990	Automated Co	610.00	422.00
910	ZV445729990	Government T	80.00	55.34

\$ 141,191.28 \$ 97,676.10

EXHIBIT B

**DETAIL OF RESULTS OF
 AGREED-UPON PROCEDURES (Cont.)**

<u>Expense Code</u>	<u>Doc Number</u>	<u>Vendor</u>	<u>Before Allocation</u>	<u>After Allocation</u>
<i>Part 3 - Maintenance agreements:</i>				
616	CM815053	Anadac	\$ 15,000.00	\$ 10,377.00
616	CM815053	Anadac	3,055.00	2,113.45
616	CM815053	Anadac	3030.00	2,096.15
616	CM815053	Anadac	404	279.49
616	CM930973	Mercury	<u>40,421.00</u>	<u>27,963.25</u>
			<u>\$ 61,910.00</u>	<u>\$ 42,829.34</u>

<u>Month</u>	<u>Amount Charged</u>	<u>Acutal Amount</u>	<u>Unreconcilable Amounts</u>
<i>Part 4 - Unreconcilable expenditures:</i>			
June, 1998	\$ 2,067,708	\$ 2,058,711	\$ 8,997
September, 1998	823,282	820,652	2,630
June, 1999	1,637,883	1,630,965	<u>6,918</u>
			<u>\$ 18,545</u>

<u>Expense Code</u>	<u>Doc Number</u>	<u>Vendor</u>	<u>Before Allocation</u>	<u>After Allocation</u>
<i>Part 5 - Tuition and books:</i>				
840	ZT561726078	Nakamura	\$ 196.81	\$ 136.15
910	CM815053	Identix, Inc.	20,000.00	13,836.00
910	ZV380560286	Department of Labor	225.00	155.66
910	ZV226622597	Chet Harmer	250.00	250.00
910	ZV226622597	Chet Harmer	250.00	250.00
910	ZV561726078	University of	425.00	294.02
910	ZV468565699	Health and Welfare	<u>225.00</u>	<u>155.66</u>
			<u>\$ 21,571.81</u>	<u>\$ 15,077.49</u>

*Agreed-Upon Procedures on the State of California,
Employment Development Department's Year 2000 Grant Expenditures*

TEXT OF CAEDD'S RESPONSE TO THE DRAFT REPORT

The narrative of CAEDD's response to our draft report is presented after this title page. Names that were included in the narrative response and may not be disclosed because of the Privacy Act considerations have been removed. In addition, Attachments A and C to the response have been omitted, because they contain voluminous personal identifying information that was impractical to remove. However, the attachments are maintained with the working papers and available for resolution purposes, if needed.

*Agreed-Upon Procedures on the State of California,
Employment Development Department's Year 2000 Grant Expenditures*
