

LIMITED AUDIT REPORT

NEH GRANT AWARD


TO THE

FILMMAKERS COLLABORATIVE, INC.

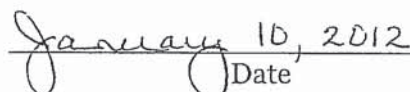
WALTHAM, MA

[TR-50093-09]

OIG-12-01 (EA)



Laura Davis, Acting Inspector General



Date

LIMITED AUDIT REPORT
NATIONAL ENDOWMENT FOR THE HUMANITIES (NEH)
GRANT AWARD
TO THE
FILMMAKERS COLLABORATIVE, INC.
WALTHAM, MA

I. INTRODUCTION

We have performed a limited audit of the Filmmakers Collaborative's (the "Collaborative") records as they relate to the following NEH grant award.

<u>Grant Number</u>	<u>Grant Period</u>	<u>Amount Awarded</u>
TR-50093-09	9/1/2009 – 7/31/2010	\$600,000

Grant Expenditures: As noted below, the intent of the grant award was to support the creation of a video documentary on the American Relief Administration's (ARA) work to combat starvation in Soviet Russia. The grantee has submitted the final financial report to the NEH and conveyed that the related expenditures conform to the intended grant purpose, as stipulated in the individual NEH grant award.

II. BACKGROUND

The Collaborative, founded in 1986, represents a non-profit association of Boston-based independent filmmakers formed to support the production of independent films and other educational materials that increase public understanding of social, cultural, political, and environmental issues. The Collaborative acts as a fiscal sponsor of film projects through sub-grants or contractual agreements with the filmmakers. The Collaborative, located in Waltham, Massachusetts, has been granted tax-exempt status under Section 501(c)(3) of the Internal Revenue Code.

NEH awarded the Collaborative a media production grant, totaling \$600,000, entitled "The Big Show in Bololand". This grant partially funded the production of a 60-minute documentary on the ARA's efforts to combat starvation in the new Soviet Russia from 1921 – 1923. Multiple distribution channels will be utilized to include PBS's *American Experience* television show, a website, and video sales. Acting as a fiscal sponsor, the Collaborative supervised the independent filmmaker, Austin Hoyt Productions, which actually produced the documentary.

III. LIMITED AUDIT OBJECTIVES, SCOPE, AND METHODOLOGY

The principal objectives of this limited audit were to determine that 1) grant expenditures were made in accordance with applicable provisions of NEH's *General Terms and Conditions for Awards to Organizations*, NEH's guide entitled *America's Media Makers: Production Grants*, and the terms of the approved grant award; 2) the Collaborative

properly implemented a comprehensive subrecipient monitoring program; and 3) proper controls over the use of Federal funds exist in accordance with minimum standards prescribed in OMB Circulars A-110 (2 CFR Part 215) and A-122 (2 CFR Part 230). Our review was conducted in accordance with *Generally Accepted Government Auditing Standards (GAGAS)* as promulgated by the Comptroller General of the United States.

We examined documentation provided by the Collaborative and Austin Hoyt Productions supporting the allowability of expenses charged to the NEH grant and reviewed the related accounting systems and internal controls applicable to both organizations.

IV. RESULTS OF LIMITED AUDIT

Overall, the NEH grant resulted in the successful production of a video documentary that was well received. However, our audit identified several deficiencies and questioned Federal costs as follows:

- The approved budget exceeded actual project costs by almost \$54,000; however, none of the cost savings were shared with NEH and the related accounting system did not properly identify project expenditures by funding source;
- NEH policy guidelines concerning fees associated with equipment and facilities owned by a grantee were not followed, resulting in questioned costs approximating \$7,300;
- Procurement and suspension/debarment rules mandated by OMB Circular A-110 and NEH *General Terms and Conditions for Awards to Organizations* were not followed;
- The Collaborative did not identify a material internal control weakness relating to the subrecipient (Austin Hoyt Productions).

A. Cumulative Project Costs – Cost Savings

The cumulative budget for the documentary project totaled \$900,000, of which \$600,000 was funded with Federal NEH funds and \$300,000 with private contributions. Ultimately, the project was completed under budget resulting in total expenditures of \$846,271. The full \$900,000 was collected from the Federal and non-Federal funders.

Although the NEH award represented “outright” funds (not contingent on additional fund-raising) and did not specifically institute a matching fund requirement, there is an expectation that recipients of NEH media production grants will cost-share and subsidize the overall costs of the project, as documented in the approved budget. Since the approved budget does not detail expense items by funding source, an equitable distribution of expenses is implied.

Furthermore, the accounting system maintained by Filmmakers Collaborative did not comply with the financial management standards set forth in OMB Circular A-110¹ and the

¹ OMB Circular A-110, Subpart C, Paragraph .21(b), stipulates that recipients’ financial management systems shall provide for the accurate, current, and complete disclosure of the financial results of each federally-sponsored project. Financial management systems shall include records that identify adequately the source and application of funds for federally-sponsored activities. These records shall contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, outlays, income and interest.

NEH *General Terms and Conditions for Awards to Organizations*. Specifically, the Collaborative’s accounting records do not provide for the detailed identification of allowable expenditures charged to the NEH award. In fact, the profit and loss statement produced by the grantee reports “NEH’s” share of total expenditures at \$567,002, which represents a simple two-thirds split of the project’s aggregate costs (\$846,271 x 2/3 = \$567,002). However, the final Federal Financial Report submitted by the grantee on December 9, 2010 reflects Federal expenditures in the amount of \$600,000.

Recommendation A

The cost principles for non-profit organizations (OMB Circular A-122) define the core factors to be considered when determining the allowability of costs charged to Federal awards. Several of these factors are relevant to this case and stipulate that costs must be 1) consistent with policies and procedures that apply uniformly to both federally-financed and other activities of the organization, 2) be accorded consistent treatment, and 3) be reasonable for the performance of the award. In consideration of these core tenants of OMB Circular A-122 and the noted deficiency with the grantee’s financial management system, the Collaborative should return a pro-rata share of the cost savings achieved as follows:

Total Expenditures Recorded for the Project	\$ 846,271
Less: Expenditures Paid Directly by WGBH	(79,304)
Balance of Project Expenses to be Supported ^[A]	766,967
NEH Funding Percentage	
[\$600,000 / (\$900,000-\$79,304)]	73%
Expenditures Allocable to the NEH	\$ 560,719
Total NEH Funds Drawn	\$ 600,000
Less: Expenditures Allocable to the NEH	(560,719)
Funds Drawn in Excess of Actual Expenditures	\$ 39,281

^[A] Portion of expenditures not tracked at a detailed level by funding source as required by OMB Circular A-110.

SUMMARY OF GRANTEE’S RESPONSE

The Collaborative formally responded with a letter dated November 16, 2011. The grantee disputes the questioned costs stating that the NEH funds came in first and were fully expended on production costs long before other funders contributed to the project (i.e. first-in, first-out methodology). Furthermore, since cost-sharing was not specifically required in the award document none of the cumulative unspent project funds need to be returned to NEH on a pro-rata basis as requested. See full copy of the Collaborative’s response at Appendix A.

OIG EVALUATION OF GRANTEE’S RESPONSE

Although the NEH award did not specifically institute a matching fund requirement, there is an expectation that recipients of NEH media production grants will cost-share and subsidize the overall project costs, as documented in the approved budget. Specifically,

NEH funding represented two-thirds of the estimated support for the project.² In this case, all expenses related to the project were commingled without specific assignment to the three funders (with the exception of certain disbursements paid directly by WGBH). Since the full \$900,000 received from the various funders was not expended during the defined grant term and the expense tracking was performed at the project level (vs. specific identification by funder)³, we could not ascertain whether all of the NEH money was spent. This led to the issuance of the audit finding in which the OIG recommended that the Collaborative return a pro-rata share of the unspent funds.

In the rebuttal, the Collaborative asserted that the profit and loss statement provided to the OIG incorrectly allocated expenses to NEH using a simple two-third split based upon the approved grant budget. In actuality, the NEH funds were received first and expended on production costs before contributions from the other funders were received. To test this assertion, the OIG reviewed the project's detailed cash account activity and determined that the last receipt from the NEH was posted by the subrecipient in late May 2010. As of this date, (1) the combination of total project cash disbursements and accrued expenses exceeded the NEH award amount⁴, and (2) funding from other sources was limited to one \$50,000 installment payment. These facts demonstrate that all NEH funds may have been spent under the first-in, first-out methodology. Even though the grantee did not specifically track project expenditures by funding source (as required by the OMB Circulars³), this cash flow analysis supports that the NEH funds were spent first in their entirety, assuming a first-in, first-out expenditure tracking methodology. Based on the results of this additional review and the fact that the unallowable costs identified during our detailed expense testing were limited to the issue discussed in Finding B, the OIG deems this finding cleared. However, we strongly recommend that the grantee begin tracking expenditures related to future Federal projects at the funder level versus the overall project level, as required by the OMB Circulars. This will necessitate the creation of project sub-codes to identify funding sources.

Furthermore, current Media Program guidelines advise that, although cost sharing is not required, NEH is rarely able to support the full costs of projects approved for funding. In most cases, America's Media Makers grants cover no more than fifty to sixty percent of project costs. Consequently, the grantee is typically required to secure additional sources of funding in order to cover project costs. Yet, the NEH does not formally require cost-sharing or specifically define which budget line items are to be funded by the NEH award. In the interest of resolving this inherent conflict, the OIG will make recommendations for NEH management's consideration that will assist all parties with cost-sharing expectations and enforcement.

B. Questioned Costs Related to Grantee-Owned Equipment/Facilities

Expenditures totaling \$56,450 were charged to the Occupancy and AVID Edit Suite budget/cost line items. The subrecipient (Austin Hoyt Productions), which owns the related facilities and equipment associated with these charges and did not identify this fact in the budget, imputed a cost based upon current fair market value rates.

² Total project budget came to \$900,000, funded as follows: NEH - \$600,000, two non-federal contributors - \$300,000.

³ OMB Circular A-110 Subpart C, Paragraph .21(b) and the related reference to the OMB Circular A-122, Cost Principles, define "allocability" standards that require financial management systems to adequately identify the application of funds by source.

⁴ Total cash disbursements approximated \$588,000 as of May 31, 2010 and accrued expenses exceeded \$12,000 based upon the volume of disbursements paid during the first week of June 2010.

Federal cost principles that govern grant expenditures require charges to a project to be based on actual costs. It would, therefore, be inappropriate for an organization to calculate costs charged to a grant, for the use of its own equipment and facilities, on the basis of commercial rates for renting or leasing such items, or on the basis of a rate schedule that includes profit.

NEH media production grants require the following treatment of these types of costs:

- For equipment and facilities that are not fully depreciated, the fee to be charged should be calculated by determining actual costs on the basis of the acquisition costs, divided by the useful life, times the period of use on the project; or
- For equipment and facilities that have been fully depreciated, the fee to be charged represents actual costs incurred to operate the asset, including the cost of maintenance, insurance, and other related expenses.

Furthermore, an applicant must identify all budget line items, in which the equipment/facilities are owned by the applicant, and document how the related charges were calculated.

Recommendation B

Using a thirty-year life span and current property tax rates, we determined that the fee charged for occupancy costs (\$26,450) materially agreed with the subrecipient's actual costs, as recomputed according to the policy above. However, our calculations related to an AVID edit suite⁵ concluded that the associated fee more closely represents commercial rates rather than actual costs. Accordingly, we are questioning \$7,300 of the related grant expense charged as follows:

AVID DS-10.5 Software and GenArts Sapphire plug in bundle*	\$12,795	
AVID Media Composer Mojo DX*	6,995	
AVID Xtore Studioraid 5Te*	5,868	
AVID Spare Drive Kit*	995	
PC Equipment	<u>2,500</u>	
Total	\$29,153	
	<u> </u>	
	<u> </u>	[Two Suites]
Total Cost (rounded up)	\$60,000	
Depreciable Life	<u>/ 3 years</u>	
Annual Cost (as calculated)	\$20,000	
Actual Expense Charged to Project	<u>\$30,000</u>	
Difference	\$10,000	
NEH Funding Percentage	<u>x 73%</u>	
Questioned Amount	\$7,300	

*Rates obtained online from a vendor website (B&H Photo) as of July 2011.

SUMMARY OF GRANTEE'S RESPONSE

The Collaborative formally responded with a letter dated November 16, 2011. The grantee acknowledges that specific NEH regulations governing charges for producer-owned equipment are in place; however, the Collaborative disputes the questioned costs stating that a rule preventing producers from receiving fair market value for self-owned

⁵ The components of the AVID edit suite listed above represent a high-end system recommended by the B&H Photo website and is not an actual representation of the suite used by Austin Hoyt Productions.

equipment seems arbitrary and unreasonable, since it is not the rate being charged to the grant that is a concern as much as who receives the benefit. They would like to see this regulation relaxed since it could invite chicanery in which two producers rent equipment to each other to receive the prevailing fair market rate.

OIG EVALUATION OF GRANTEE'S RESPONSE

After reviewing the grantee's rebuttal, the OIG believes this remains a valid finding since it is based upon specific NEH policy guidance and Federal cost principles. However, the amount of questioned cost is reduced from \$7,300 to \$6,667 based upon the first-in, first-out methodology accepted for Finding A above. Specifically, we determined that two-thirds of the AVID Edit Suite rental expenses were posted to the project general ledger as of May 31, 2010.⁶

*Note: The OIG utilized a three year depreciable life when performing the calculations related to this finding since the industry standard for computer equipment/software typically runs from three to seven years. To provide maximum credit to the grantee, we used the shorter life span which resulted in a higher depreciation charge.

C. Subrecipient Monitoring: Procurement Policies/Procedures

The subrecipient (Austin Hoyt Productions) has not implemented formal procurement policies and procedures as required by OMB Circular A-110 (2 CFR Part 215)⁷ and NEH *General Terms and Conditions for Awards to Organizations*. Specifically, procurement records and files for purchases in excess of the simplified acquisition threshold (currently \$100,000) shall include the basis for contractor selection, justification for lack of competition when competitive bids or offers are not obtained, and the basis for award cost or price. Furthermore, recipients must ensure that all parties with whom they contract for goods or services in excess of \$25,000, are not debarred or suspended from doing business with the Federal government.

Based upon our testing, we determined that the subrecipient executed one material contract in excess of \$100,000 to produce the Urals Mountain footage. There was no evidence that a search of the Excluded Parties List System (EPLS) was conducted and the procurement file lacked documentation supporting the sole source award made. Moreover, the Collaborative failed to identify this exception at the filmmaker since subrecipient oversight was limited to the inclusion of a clause referencing the Federal procurement rules in the sponsorship agreement signed with Austin Hoyt Productions.

Upon further testing, we determined that extensive negotiations between the contractor and subrecipient resulted in a large reduction in the initial fee proposed and professional fees charged fell within industry benchmarks. We also determined that the contractor is not currently suspended or debarred by the Federal government, based on a query of the Excluded Parties List System (EPLS).

Recommendation C

The acceptance of Federal funds requires the grantee to develop processes to ensure compliance with the various Federal procurement rules. We recommend that the

⁶ Total AVID Edit Suite Rental costs amounted to \$30,000. Of this amount, \$20,000 was booked from project inception through May 31, 2010. Accordingly, two-thirds of the AVID costs relate to the timeframe funded by NEH therefore the questioned amount has been revised to \$6,667 ($\$10,000 \times 2/3$).

⁷ OMB Circular A-110 does not directly apply to "for-profit" entities. However, the Collaborative's executed sponsorship agreement with Austin Hoyt Productions passed these requirements down to this subrecipient.

Collaborative expand the scope of its subrecipient monitoring activities and begin reviewing a sample of material contracts executed by subrecipients for compliance and gain an understanding of the related controls enacted over this process. The implementation of these new procedures will help ensure compliance with Federal procurement rules, as articulated in OMB Circular A-110.

SUMMARY OF GRANTEE'S RESPONSE

The Collaborative agrees with this finding and plans to expand the scope of its subrecipient monitoring activities. Specifically, the related procurement provisions will be pulled from the *NEH General Terms and Conditions for Awards* guidance and incorporated into all future contracts between the Collaborative and subrecipients of NEH grants. The Collaborative will not release funds until the subrecipient fully understands and accepts these Federal compliance rules.

D. Subrecipient Monitoring: Preliminary Review of Internal Control Structure

We gained an understanding of the key accounting cycles impacting the NEH grant at both the Collaborative and Austin Hoyt Productions. During this process, we determined that a material control weakness existed over the subrecipient's disbursement cycle. Specifically, no one individual should control an entire accounting process. In this case, the bookkeeper 1) processed invoices; 2) input disbursement entries into the accounting software; 3) prepared, signed, and mailed the checks; and 4) performed the monthly bank reconciliations.

OMB Circular A-110 (2 CFR 215) and NEH's *General Terms and Conditions for Awards to Organizations* require award recipients to implement sufficient internal controls in such a manner to protect company assets and ensure they are used solely for authorized purposes. As the primary recipient of the NEH award, the Collaborative must implement sufficient subrecipient monitoring procedures to ensure subrecipient organizations comply with this requirement.

Recommendation D

Although our testing did not reveal any evidence of fraudulent activity, we strongly encourage that the Collaborative begin performing a detailed review of each subrecipient's internal control structure prior to releasing any Federal funds. This new oversight function would identify material weaknesses up-front, guard against possible fraudulent activity, and ensure subrecipients tighten up their processes and internal controls before any Federal funds are put at risk. Under Federal standards, the Collaborative is ultimately responsible for compliance with all relevant laws and grant terms, and addressing any unallowable or questioned costs. Therefore, it's in the organization's best interest to strengthen current subrecipient monitoring procedures, especially in light of the fact that the Collaborative's reason for existence is to act as a sponsor for independent filmmakers.

SUMMARY OF GRANTEE'S RESPONSE

The Collaborative agrees that the employee performed the accounting functions as discussed in the finding. However, the grantee argued that this individual always worked under the authority and guidance of management and expenditures were reviewed by production staff.

The Collaborative acknowledges that a formal segregation of duties represents an important component of internal control but can be cost prohibitive to implement fully

therefore the organization plans to communicate practical steps available to subrecipients to mitigate the risks. Furthermore, the Collaborative will introduce a new, internal control checklist as a basis to query subrecipients and proactively identify potential internal control concerns at the outset of the NEH award.

OIG EVALUATION OF GRANTEE'S RESPONSE

One employee should not perform all of the accounting functions related to a specific accounting cycle. Industry studies have repeatedly demonstrated that this exposes an organization (smaller entities in particular) to heightened fraud risk. In this case, the employee performed all of the accounting steps involved with the accounts payable function to include inputting transactions into the accounting software; generating, signing, and mailing checks; and preparing the monthly bank reconciliations and financial reports. Even though other employees were involved with periphery duties such as approving invoices and periodically reviewing reports, the existing control structure provides the key person with an opportunity to conceal thefts through the use of accounting entries.

Subrecipient monitoring procedures that facilitate timely identification of significant internal control weaknesses, such as the one aforementioned, would enable the Collaborative to effectively address matters before any Federal funds are put at risk. We are pleased that the Collaborative plans to introduce the use of an internal control checklist as part of its subrecipient monitoring program moving forward.

VII. EXIT CONFERENCE

The results of our review were shared with Collaborative management ([REDACTED] ~ Acting Executive Director, [REDACTED] ~ Associate Director, and [REDACTED] ~ Past Executive Director) on August 24, 2011.

**APPENDIX A:
GRANTEE RESPONSE TO OIG
AUDIT REPORT**



National Endowment for the Humanities
Office of Inspector General
1100 Pennsylvania Avenue NW, Room 419
Washington, DC 20506
ATTN: Audit Resolution Section

November 16, 2011

RE: Audit Report OIG-12—01 (EA)

To: Laura Davis, Steve Elsberg

I. INTRODUCTION

Thank you for the audit report that was sent to Filmmakers Collaborative (“FC”) and that we received on October 15th. Thanks especially to Steve Elsberg, who has been available by phone and email and who has helped us understand the NEH’s concerns. This letter is the required written response to your findings.

This letter addresses the NEH’s “limited audit” related to the \$600,000 grant to Filmmakers Collaborative (FC) for a documentary by Austin Hoyt Productions (“AHP”) called “The Big Show in Bololand,” grant # TR-50093-09, with a grant period of 9/1/09 – 7/31/10. The NEH provided major funding for this documentary on the American Relief Administration’s efforts to combat starvation in Russia from 1921-1923. FC was the fiscal sponsor, working with Austin Hoyt who produced the documentary through his company, Austin Hoyt Productions. It premiered on the PBS *American Experience* series this past April as *The Great Famine* (<http://www.pbs.org/wgbh/americanexperience/films/famine/>).

The principal objective of your audit was to determine whether or not grant expenditures were made in accordance with applicable provisions of the NEH’s *General Terms and Conditions for Awards to Organizations*, and that FC monitored the subrecipient’s use of funds in accordance with the minimum standards prescribed in *OMB Circulars A-110 (2 CFR Part 215)* and *A-122 (2 CFR Part 230)*.

II. DISCUSSION OF NEH FINDINGS AND RECOMMENDATIONS

As a former subrecipient of many NEH grants and as a long-time FC Board member and newest Executive Director, I wholeheartedly agree that the subrecipient monitoring process be as clear and easy to follow as possible. In fact I would like to work with the NEH to develop a straightforward monitoring checklist that all fiscal sponsors can use.

We already work from the *General Terms and Conditions from Awards* but some of the OMB Circulars that this document references are not readily accessible.¹

Please note also that I am attaching a response from Austin Hoyt on points that concern him in the audit report. While AHP's perspective is woven into this report, Mr. Hoyt can provide narrative details that we think are important, and that we understand the NEH to have requested.²

Recommendation A

The audit reports that Austin Hoyt Productions raised \$900,000 for a documentary that Mr. Hoyt ultimately produced for \$846,271. The report concludes that the NEH should be entitled to share in a percentage of the difference, which is calculated to be \$39,281. We respectfully disagree with this finding. You note that \$600,000 of NEH funds were drawn (true) but that only \$570,719 were allocable to the NEH (not true). We understand how this conclusion was derived: the profit and loss statement of budgeted versus actual expenses does show a smaller amount of NEH funds expended.

However this is not accurate. [REDACTED], who was Austin Hoyt's business manager (and is now FC's Associate Director) prepared this profit and loss statement by allocating the entire budget equally across all funders. This was a fundamental error, because NEH funds had come in first and were fully expended on production costs long before other funders contributed to the project. The *American Experience* funding came in last and was not fully expended, as the profit and loss statement should have shown. As Mr. Hoyt points out, *American Experience* funds were precarious to the very end; if for any reason PBS had stopped its cash flow to WGBH, WGBH would not have released any funds to Mr. Hoyt's project. He was prepared to cover the shortfall himself if that happened, as he had no unspent federal funds to rely on at that late date.

Furthermore, while it is true that Mr. Hoyt managed to come in under budget for production, he also spent considerable unpaid time marketing and promoting the film after it was finished – as is usual for independent producers. In his attached addendum please note that he estimates roughly \$35,000 in unpaid costs for this last, unbudgeted phase of work. We at FC understand the life cycle of production and do not question the appropriateness of producers recouping a portion of their losses if they can, by savings incurred during production – as long as it does not violate any funder regulations.

In the case you cite of *OMB Circular A-122*, which defines the core factors to be considered in determining allowability of costs charged to federal awards, we do not see where cost sharing with the NEH is required unless cost-sharing is specifically required by the award. Indeed, the last line of paragraph 1 of *OMB Circular A-122* states that

¹ For instance, they reference *OMB Circulars A-110 (2 CFR Part 215.36)*, *A-122 (2 CFR Part 230)* and *OMB A-133* together include several thousand pages of regulations.

² Email from Steve Elsberg to [REDACTED] (former FC executive director) dated August 24, 2011.

“provision for profit or other increment above cost is outside the scope of this Circular.”³ Furthermore, we have reviewed *OMB Circular A-122* and see that the guiding principal of the circular is that costs charged to federal awards be reasonable. As Mr. Hoyt can substantiate all costs, and FC has reviewed them and deemed them reasonable, and the NEH has not disputed this, is there an issue we are not seeing?

Therefore, since the \$600,000 from the NEH were fully expended on allowable costs, we respectfully disagree with your conclusion that Austin Hoyt Productions or FC should return \$39,281 to the NEH.

Recommendation B

Here you question \$7,300 in charges for the AVID Editing Suite, because the subrecipient (AHP) owned the equipment and should have charged the grant according to an NEH formula instead of using fair market values. While we do understand the NEH regulations governing charges for producer-owned equipment, and while we will henceforth make these regulations clear to all producers a) before they submit budgets to the NEH, and b) before we release funds for projects, we do find them to be unfair in general, and especially as they pertain to this project. Independent producers that we work with are never able to write off equipment in three successive years of production since that is almost never how funding and production cycles work. And the NEH’s position that producers cannot receive fair market value for equipment rented seems arbitrary and unreasonable, since it is not the rate being charged to the grant that is a concern as much as who receives the benefit. As an organization that supports independent production, we would like to see the NEH relax this regulation – especially since it can, as Mr. Hoyt points out, “invite chicanery” such as two producers renting equipment to each other. It would be simpler and cleaner to allow fair market rentals across the board, in FC’s opinion.

Recommendation C

We understand the Endowment’s concern here to be that AHP executed one contract in excess of \$100,000 to produce recreations in the Ural Mountains, and that FC failed to require documentation regarding this payment in the audit. However, we did have conversations with Mr. Hoyt, and he represented that the company paid was in fact the only feature film producer in Ufa, Bashkortostan available to assist with this project (not surprisingly), and that far from being a potential “enemy,” the company they worked with was “a gift from the gods.”⁴

³ <http://www.nonprofitaccountingbasics.org/audits-external-reporting-disclosure/compliance-audits-federal-awards/omb-circular-122>

⁴ References are to the Excluded Parties List System” mentioned in the *General Terms... Appendix A (a)* and to email correspondence with Austin Hoyt.

Nevertheless we do agree with your finding that FC should expand the scope of its subrecipient monitoring activities, and we are already taking steps to do this.⁵

Recommendation D

As mentioned earlier, [REDACTED] was the “bookkeeper” (more accurately, “business manager”) that the NEH deemed to have exercised excessive control over AHP’s accounting processes. She is now Associate Director of FC, and has explained that however it might have appeared to the NEH, she never had any “control” over the money. She did the work that you described (processing invoices, writing and signing checks, keeping the books and performing monthly bank reconciliations) but it was always under the authority and guidance of Mr. Hoyt, the project director and her boss. It should be noted that a co-producer was responsible for overseeing all charges to the project. Expenditures were reviewed by the person on the production team who initiated the charge.

While we agree that a formal segregation of duties is an important component of internal control, it is simply cost-prohibitive to implement. However, we plan to work diligently to communicate to all subrecipients of federal awards practical steps that can be taken to mitigate the lack of segregation of duties. In addition, the checklist we previously discussed will contain queries to identify potential internal control deficiencies with subrecipients, to proactively address these concerns.

III. SUMMARY

In summary, on behalf of FC I would like to assure the NEH that FC is as eager as you are to have a very clear set of policies that govern how we monitor projects and how we expect subrecipients to monitor projects. As I have mentioned in phone conversations with Steve Elsberg, FC has undergone some changes in the last three years. In particular, there has been significant turnover in the Executive Director position: [REDACTED] left after ten years as Executive Director, and [REDACTED] left after one year. I have been a filmmaker-member of FC for thirteen years, on the Board of Directors for eight, and this past summer became Acting Executive Director. As much as anyone I see the necessity of having very clear policies that govern how we monitor projects, and I welcome any assistance the NEH can provide with this process. FC has now been in business for 25 years, and this milestone is an excellent time to review and improve how we conduct our fiscal sponsorship duties. In particular, your assistance in extracting the most important requirements of *OMB Circular A-110 (2 CFR Part 215)*, *OMB Circular A-122 (2 CFR Part 230)* as well as *OMB Circular A-133* will be most appreciated.

⁵ We now will make the provisions of the *General Terms and Conditions for Awards* part of every contract between FC and the subrecipient of an NEH grant, and require that they are read and accepted before grant funds are allocated.

Within the next month I plan to compile this information in an easy-to-read format, marry it to the subrecipient requirements outlined in the *General Terms and Conditions for Awards to Organizations*, and make this document part of all FC-Project Director contracts for NEH grants. As we are currently reviewing our bylaws, contracts and policies, this is an ideal time to implement these changes

Thank you again for your help. We look forward to hearing your response to this audit response. In the meantime my very best wishes to you.

Sincerely,

[Redacted signature]

[Redacted name]

Acting Executive Director, FC

Attachment: AHP Response to NEH Audit

cc: [Redacted], FC Chairman of the Board
[Redacted], FC Treasurer and CFO
Austin Hoyt, Project Director, TR-50093-09