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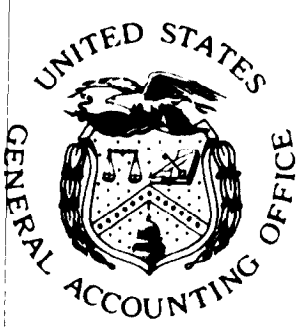
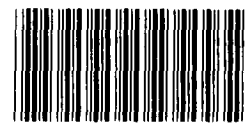
BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Secretary Of The Interior

The Department Of The Interior Should Improve Its Policies And Practices On Grant-Related Income

Many Department of the Interior grantees generate income under programs financed in whole or in part with Federal assistance. This income is a potential source of revenue for either increasing the size of Interior programs or reducing the Federal Government's and grantees' share of costs. However, these objectives were not always being attained because regulations directing the grantees' use of the income did not exist or Interior's agencies and grantees were not always complying with existing regulations. GAO recommends a number of corrective actions.





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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

GENERAL GOVERNMENT
DIVISION

B-202774

The Honorable James G. Watt
The Secretary of the Interior

Dear Mr. Secretary:

We recently performed a Government-wide review of Federal agencies' and grantees' policies and practices on handling income generated under federally assisted programs. We found that a number of Federal agencies, including the Department of the Interior, had not established regulations addressing some grant related income issues, were not conforming to the Office of Management and Budget's grant related income standards, and/or were not adequately implementing their grant related income regulations. As a result, the objectives which the income standards sought to attain--using the income to increase the size of the federally assisted programs or to reduce the Federal Government's and grantees' shares of program costs--were not always being attained. We are reporting the findings as they relate to your agency and recommending that you direct the Interior agencies included in our review to develop regulations on some grant related income issues and to comply with existing grant related income regulations so that the income standards' objectives can be attained.

As you know, 31 U.S.C. §720 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs within 60 days of the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report. Our recommendations to you appear on pages 12 and 13.

We are sending copies of this report to the Director, Office of Management and Budget; appropriate Senate and House Committees; and other interested parties.

Sincerely yours,

W. J. Anderson

William J. Anderson
Director

RESULTS OF GAO'S REVIEW OF INCOME GENERATED UNDER DEPARTMENT OF THE INTERIOR ASSISTANCE PROGRAMS

BACKGROUND

Grant-related income is any money received by grantees during the course of operating federally assisted programs. Grantees in a number of Interior programs generate income from (1) rents for land, housing, and industrial facilities collected on properties acquired with Federal assistance; (2) investment income (interest) earned on grant project funds; and (3) proceeds realized from the sale of property, oil, and natural gas. OMB issued standards during the 1970's requiring grantees to account for income generated under programs financed in whole or in part with Federal funds.[1]

OMB categorized different types of income by source and provided principles for each type's disposition, as follows:

--Interest earned by States or their instrumentalities on advances of Federal funds pending disbursement need not be remitted to Federal agencies per the provisions of the Intergovernmental Cooperation Act of 1968.

--Interest earned by others on advances of Federal funds must be remitted to Federal agencies.

--Proceeds from the sale of real and personal property are to be remitted to the Federal Government in proportion to the percentage of Federal participation in the cost of the original project.

--All other program income (fees, rents, lease income, etc.) earned during the grant period is to be retained by grantees but used in one of three ways.

The circulars specify the three available options for handling the last type of income--other program income. The grant agreement is to specify which of the following options the grantee is to use:

--**Additive:** Add the income to the funds committed to the project by the grantor and grantee and use it to further eligible program objectives. This is intended to

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[1]Attachment E of Circular A-102: Uniform Administrative Requirements for Grants-in-Aid to State and Local Governments, issued in 1971 (revised January 1981) and Attachment D of Circular A-110: Uniform Administrative Requirements for Grants and Agreements With Institutions of Higher Education, Hospitals, and Other Nonprofit Organizations, issued in 1976.

result in a larger program than what would otherwise be the case.

--**Cost-sharing:** Use the income to finance the non-Federal share of the project. This is to result in the same size program. The grantee is allowed to use program income as part or all of its contribution towards project costs rather than having to contribute its share from its own resources. The Federal contribution remains the same.

--**Deductive:** Deduct the income from total project costs to arrive at net costs on which the grantor and grantee shares will be based. This is to result in the same size program, and unanticipated program income is used to reduce the grantor and grantee contributions rather than to increase the funds committed to the project.

These three options for handling other program income are graphically displayed in appendix II.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our review was undertaken to assess agencies' policies and practices for reporting and disposing of grant-related income. Two of your agencies were included in our review--the Fish and Wildlife Service (FWS) and the National Park Service (NPS).

Federal financial assistance for Interior programs is provided to State and local agencies through many programs. Because existing information and reporting systems were inadequate for determining which programs were generating income, we selected and examined four programs--the FWS' Wildlife Restoration and Fish Restoration programs and the NPS' Historic Preservation and Outdoor Recreation programs--that generated income, based on reports issued by Interior's Inspector General.

The number of States we visited and grantees/subgrantees we contacted is shown below by program.

Programs	Number of States visited	Number of grantees/ subgrantees contacted
Wildlife Restoration	10	10
Fish Restoration	7	7
Historic Preservation	5	12
Outdoor Recreation	6	9

Our selection was generally designed to yield grantees with varying dollar size grants and a combination of grants for which

income was and was not reported. We interviewed grantee officials having program, administrative, and financial responsibilities and examined grantee records to verify the information obtained.

In Washington, D.C., (headquarters) and in four Federal Regions--New York, Atlanta, Denver, and Seattle--we interviewed Interior officials having program, grants administration, accounting, budgeting, auditing, and legal responsibilities. We examined agency records and reviewed several hundred internal audit and Inspector General reports for the period 1974 to mid-1981. We used these reports, along with information we obtained from our audit work, to develop our findings. Because of the large number of audit reports reviewed, we did not verify the supporting data and did not pursue what corrective action was taken. We conducted these interviews and record reviews to ascertain Interior's policies on grant-related income and to determine whether agency and grantee practices were in accord with the policies.

This audit was performed in accordance with generally accepted government auditing standards.

GRANTEES SHOULD USE PROGRAM INCOME FOR PROGRAM PURPOSES

OMB's program income standards provide that grantees are to retain program income and, in accordance with the grant agreement, use the income under one of the three program income options. Applying these options results in expanded programs or reduced Federal and grantee costs. Interior programs we reviewed all have regulations requiring grantees to retain the income and use it for program purposes. We found, however, that grantees were not always retaining and using the income under the options available, and thus, Interior programs did not always benefit when income was generated.

Outdoor Recreation Program regulations require grantees to retain program income and to apply it to the program according to the additive or deductive option. We found that in 1980, New Jersey generated $72,500 of income from the lease of a State park funded, in part, under the Outdoor Recreation Program. An additional $105,000 was generated at other State parks, some of which received Federal outdoor recreation funds. However, none of this income was used on the projects; instead, in accordance with State law, the income was deposited to the State's general fund. State officials told us that the State's accounting system does not distinguish between income generated from federally and nonfederally assisted projects and that they did not determine whether some of the lease income may be applicable to the federally assisted projects. We asked them to make this determination, but they have not responded to date.

Under Interior's Wildlife Restoration Program, federally assisted wildlife areas have been leased by the States to private concerns for extracting oil, gas, and mineral deposits. While Interior's Wildlife Restoration Program policies require grantees to apply all income to wildlife projects, we found some cases where lease and royalty income was deposited in States' general funds rather than being applied to the grantees' wildlife projects.

In Utah, for example, which as of January 1982 had 111 leases covering over 58,000 acres, nearly $59,000 in lease income was generated. Over 40,000 of the acres are in federally assisted wildlife management areas. The State was depositing all proceeds from mineral leases in the general fund in accordance with a State statute. Regional Interior officials in 1981 questioned the disposition of the income, citing FWS regulations prohibiting the diversion of income from wildlife purposes. Interior and State officials recognize that a conflict exists between the State statute and Interior's regulations, and they are working to resolve the conflict.

In Indiana, State law requires the deposit of oil royalties to the State's general fund. In February 1981, FWS officials questioned State officials on the practice of crediting the State's general fund with oil income generated on federally assisted wildlife management areas. Discussions between State and FWS officials occurred intermittently until March 1982 when the Governor of Indiana wrote to the Secretary of the Interior stating that the oil royalties were not program income. In July 1982, Interior responded that the oil income was program income and should have been credited to wildlife programs. In a letter dated November 15, 1982, the State advised Interior regional officials that nearly $115,000 in oil revenues generated during the period July 1973 to June 1982 will be credited to wildlife purposes and that income generated after June 1982 would also be credited to wildlife purposes.

Other situations such as these have arisen over the past few years. Yet, to our knowledge, Interior agencies have not systematically reviewed State practices to ensure compliance with agency regulations. In our opinion, Interior agencies need to review grantees' practices and to emphasize the program income requirements contained in program regulations so that when grantees receive income from operating federally assisted programs, the income will be applied toward accomplishing the program income objectives.

FOR WHAT PURPOSES CAN PROGRAM INCOME BE USED?

Interior agencies have varying policies on the use of program income. For instance, Wildlife Restoration Program policies consider program income as Federal funds subject to the same standards of cost allowability. FWS program policies state

that program income becomes Federal funds if the Federal Government participated in the activities which produced the income. According to the policy statement, the use of the income is subject to the same constraints, limitations, and requirements that apply to the use of Federal funds.

Interior's Outdoor Recreation Program funds are available for planning, acquisition, and development activities but not for the operation and maintenance of outdoor recreation facilities. The Outdoor Recreation Program regulations, however, are silent on the expenditure of program income funds for operation and maintenance. In Louisiana, substantial income is expected to be derived from mineral leases on outdoor recreation land acquired with Federal assistance. Louisiana proposed to establish a trust fund for financing outdoor recreation acquisition and for outdoor and indoor recreation development projects. Based on an opinion of Interior's Solicitor, Louisiana was advised that the income could be used for outdoor recreation acquisition, development, operation, and maintenance but not on indoor recreation projects. Thus, it appears that program income, but not Federal funds, may be used to fund operation and maintenance of outdoor recreation activities.

OMB, in its Circular A-87 which establishes cost principles applicable to grants with State and local governments, states that grant program funds can be used only for allowable costs. OMB defines grant program as an activity funded by Federal and grantee funds. In our report[2] on grants awarded to nonprofit organizations, we stated that a grant program is comprised of not only the Federal and grantee funds but also any program income generated under the program. Thus, in our opinion, program income funds could be used only for allowable costs.

Although this determination applied only to the case we considered, we believe it would be desirable for Interior, in view of the uniformity sought by OMB Circulars A-102 and A-87, to reexamine the different program policies on the allowable uses of program income funds.

WHEN SHOULD PROGRAM INCOME BE SPENT?

The Interior Wildlife Restoration Program had no regulations on when program income should be spent. Lacking Federal agency direction, we found that some grantees retained and planned to spend the income later during or after the project period and thus, they did not reflect program income in their drawdowns of Federal funds. In addition to the cash management implications of this practice, it may be difficult for Federal

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[2]"Restrictions on Abortion and Lobbying Activities in Family Planning Programs Need Clarification" (GAO/HRD-82-106, Sept. 24, 1982).

agencies to ensure that program income retained for expenditure after the project period will be used for originally agreed upon purposes.

Under the Wildlife Restoration Program, Florida and Georgia earned, and planned to spend in future years, substantial income from the sale of special hunting permits, wildlife management area stamps, and in one case, a long-term lease. In Florida, annual permit sale revenues totaled over $1 million in 1981 and, after deducting for certain expenses, were deposited to a land acquisition trust fund. This fund totaled $1.7 million as of June 30, 1981. Florida also received $1 million in 1981 as a lump-sum payment under a 45-year lease agreement wherein 884 acres of a federally assisted wildlife management area were leased to a city for waste treatment purposes. The money was placed in a special trust account for future development of wildlife management areas.

In Georgia, income from hunting stamp sales is remitted to the State Treasury. Income in fiscal year 1980 was about $320,000. These funds are appropriated by the State for wildlife purposes in the following year.

During our review, we examined the Federal control of and share in Florida's $1.7 million land acquisition trust fund. Federal officials told us that they have reached agreement with State officials that any future land acquisition paid for out of the trust fund will have a Federal share. In response to our question as to the amount of the Federal share, Florida officials provided us with their computations showing that of the almost $1.2 million added to the fund for the 3-year period ending 1981, about $150,000 or 12.6 percent represented the Federal share. We suggested that because the Federal agency participated in financing 75 percent of project costs, 75 percent of the income would appear to more equitably represent the Federal share. After we discussed this with Interior regional and State officials, they agreed that a 75-percent Federal share exists in the $1.7 million trust fund as well as in lands purchased with trust fund assets. Interior regional officials also agreed to clarify the Federal share of the $1 million special trust fund.

The matter of when to spend program income funds is important when viewed in the context of Federal cash management objectives. Reduced Federal borrowing costs due to reduced Federal fund advances or reimbursements could result if grantees were required to use program income funds to defray project costs before requesting Federal funds. Although not explicit, this appears to be the objective sought by attachment H of OMB Circular A-102 which requires grantees to subtract program income from their requests for Federal funds. However, in the Florida and Georgia examples discussed previously, program income was not subtracted from requests for Federal funds.

Establishing a regulation calling for the spending of program income before spending Federal funds would ensure that the income is spent during the time the project is active and on project purposes and would result in a reduction of grantees' immediate needs for Federal funds.

INTEREST EARNED ON PROGRAM INCOME

Program income accruing to grantees is being invested and is earning interest. Although Interior agencies' regulations guide the disposition of program income, they do not address the disposition of interest earned on program income. We did note that some agreements with States under the Outdoor Recreation Program provided for the disposition of interest earned on certain types of income. In the absence of regulations in this area, however, the other grantees we reviewed were guided by State and local laws.

Some States require that all interest received from invested program income funds be credited to State accounts rather than to the program whose funds earned the interest. In other States, interest earned on invested funds is credited to the individual program account; thus making available additional funds for accomplishing program purposes. The different ways grantees treated interest earned on program income where no Federal policies or regulations exist are identified below:

--In Colorado, all wildlife program income is deposited to the State's wildlife account. The wildlife account, however, is not credited for any interest earned on the funds because the State's statute requires that all interest be credited to the State's general fund.

--In Wyoming, wildlife program income is deposited in the State's wildlife accounts. Interest earned on these accounts is used for furthering wildlife purposes.

--In Georgia, proceeds derived from special hunting permit fees under the wildlife program are deposited to the State general fund and invested. In the following year, the State appropriates an amount equal to the permit revenues to the State wildlife agency, which, in effect, denies the agency any interest earned on the funds.

--In New Jersey, all lease income generated from State parks developed or acquired with Federal outdoor recreation funds and the interest thereon is deposited to the State's general fund.

--In Florida, a certain percentage of proceeds from the sale of special hunting permits under the wildlife program is deposited to a land acquisition trust fund. Interest earned is retained in the account and totaled

$143,000 in fiscal year 1981 on a principal amount of $1.7 million.

--Also in Florida, lease income of over $1 million under the wildlife program was deposited in a special trust fund and earned $108,000 in interest over nearly a 2-year period. The interest was retained in the special account.

Under Interior's Outdoor Recreation Program, some States are involved in the extraction of oil, gas, and mineral deposits from lands acquired with outdoor recreation funds. In the cases we reviewed in which States proposed to extract deposits, the agreements between the States and the Interior contained provisions requiring that the income be dedicated to outdoor recreation purposes. For the most part, the agreements also specified that any interest earned on invested income must also be dedicated to outdoor recreation purposes.

We believe that Interior should establish regulations dealing with the disposition of interest earned on invested program income funds. Consideration could be given to designing the regulations along the lines of having grantees treat the interest as they treat the program income. Thus, programs could get larger or costs to the Federal Government could be further reduced depending on which program income option is being applied.

We also believe that Interior should determine whether any Federal share exists in the interest earned on the $1.7 million Florida wildlife trust fund and the $1 million special trust fund.

AGENCIES' REGULATIONS CONFLICT INTERNALLY

FWS and NPS have each issued program income regulations or adopted practices which conflict internally and possibly with statutory provisions thus confusing grantees on the proper use of program income. FWS has program income regulations allowing two of the three OMB options--the additive and deductive. The statutes authorizing Fish and Wildlife programs, however, appear to allow only the additive option for certain types of program income. At the regional level, one official told us he uses the OMB circular as his criteria. In another region, an FWS official told us he allows two of the three options in the OMB Circular--the additive and deductive--but he also allows grantees to use the income to fund an entirely separate project.

NPS' Historic Preservation Program Manual states that program income is to be retained by the grantees and used to further the objectives of the legislation. This language is similar to that used by OMB to describe the additive option under which program income is added to the program. However, the NPS

manual does not offer the additive option but instead offers only the cost sharing and deductive options.

We believe the two Interior agencies need to review their regulations concerning the options available for using program income to make them clear and consistent and reflective of statutory requirements.

BETTER REPORTING OF GRANT-RELATED INCOME IS NEEDED

Although certain types of program income are required to be reported, grantees are failing to report millions of dollars of such income generated under Interior programs. Also, other types of income, such as interest and sales proceeds, are not reported because reporting is not required. As a result, Federal oversight and control of the income's disposition are impeded. Accurate and complete reporting of grant-related income would produce the information needed to effectively oversee and control the significant amounts of income generated under federally assisted programs.

To determine the magnitude of the nonreporting, we judgmentally selected and reviewed about one-third of Interior's audit reports from 1974 to mid-1981. This review showed that unreported program income, as identified in 40 of the audit reports, totaled over $3.8 million during that period.

An Outdoor Recreation Program grantee in Idaho did not report $38,000 in program income during 1980 as required. However, during our review, the grantee said that he planned to report it on a future billing. Two grantees in the Historic Preservation Program earned income but, contrary to agency regulations, failed to report it. One grantee in Utah earned about $71,000 and the other grantee, in Colorado, earned about $14,700.

We also noted that three grantees in the Fish and Wildlife Restoration programs were earning, but not reporting, grant-related income. In New York, a grantee generated, but did not report, $2,970 of program income. A Utah grantee earned $6,653 of income which a State official agreed to report on a future request for reimbursement. A Florida State grantee earned $108,000 in interest on funds received from leasing a wildlife management area. The grantee reported the lease transaction to FWS officials but did not report the interest consistent with FWS regulations which do not require the reporting of interest.

In one case, a State grantee was not required by FWS to report permit sales even though two other States which had permit sales income were required to report their income. Under Interior's Wildlife Restoration Program, 2 of the 10 States in our review derived income from special hunting permit sales on federally assisted wildlife management areas. FWS regional

officials consider these permit sales to be program income in Georgia and Florida and require the States to report the income. But the permit sales are not considered program income in another State, North Carolina, and therefore the income is not required to be reported.

FWS policy on program income cites the sale of management area permits as an example of income producing activities whose proceeds must be reported. Thus, as a result of a February 1977 audit report, in which Interior auditors noted that Georgia permit sales of $415,000 had not been reported, the Assistant Regional Director for Federal Assistance advised Georgia that "Since these Wildlife Management Areas were financed in part with Federal Aid funds, the revenue received must be treated in accordance with the program income provisions of [OMB Circular A-102]."

In contrast, a May 1977 audit report noted that North Carolina did not report permit sales income of over $800,000 for the 29-month period ending September 1976, but FWS' Deputy Associate Director concluded that the North Carolina permit sales were not program income, "* * *based on the criteria established that the management of game lands is not the income-producing activity." The Interior official, however, did acknowledge that Federal aid funds were used in managing all State-controlled lands.

In our opinion, the FWS' determination that North Carolina permit revenues did not represent program income, although similar income in Georgia and Florida was considered program income, is inconsistent and may be contrary to FWS policy on program income.

INTERIOR GRANTEES SHOULD USE THE FINANCIAL STATUS REPORT

The basic financial reporting form prescribed by OMB's standards is the Standard Form 269: Financial Status Report (FSR). However, the OMB standards provide Federal agencies with the option of not requiring grantees to use the FSR when other OMB forms used by the agency provide adequate information.

FWS officials in the Atlanta region told us that they do not require grantees to use the FSR because the information on other OMB forms meets their needs. The OMB forms are the SF 270: Request for Advance or Reimbursement and SF 272: Federal Cash Transactions Report. Both provide space for grantees to report on program income but for different purposes and in different ways. The stated purpose of the SF 272 is to assist Federal agencies in monitoring advances to grantees and to obtain disbursement information. The stated purpose of SF 270 is for grantees to request advances and reimbursements.

Unlike the FSR, SF's 270 and 272 do not require grantees to report on the source and disposition of program income. Furthermore, the language on the forms, as it relates to reporting income, is confusing because it does not clearly relate to the language used in the Fish and Wildlife Restoration programs' regulations regarding the options for using program income. For example, the instructions on the SF 270 require grantees to "* * *enter only the amount applicable to program income that was required to be used for the project or program by the terms of the grant or other agreement." The only language in the programs' regulations that is close to this language is that used to describe the additive option, and, thus, it may be confusing to grantees using other options.

The SF 272 requires grantees to "Enter the Federal share of program income that was required to be used on the project or program by the terms of the grant or agreement." No explanation is provided on the form or in the FWS program income regulations as to what the "Federal share" is or how it is calculated.

Although the FSR, in its present form, is not entirely adequate for reporting on the source, amount, and disposition of program income, we believe it is nevertheless preferable to the SF's 270 and 272. We therefore believe it would be desirable for Interior to require grantees to use the FSR for reporting program income and to further require that grantees report all types of grant-related income. We have therefore recommended to OMB, in a separate report,[3] that the FSR be revised to provide space for reporting the source, amount, and disposition of all types of grant-related income.

GRANTEES SHOULD REMIT PROPERTY SALES PROCEEDS

Historic Preservation Program regulations reference OMB Circular A-102, Attachment N, property management standards which require, in part, payment of the Federal share when property acquired in whole or in part with Federal assistance is sold. We found, however, that the following subgrantees sold real property that was either acquired or developed in part with Federal funds but did not remit the Federal share of the sales proceeds:

--Georgia subgranted to the City of Marietta $15,000 of Federal funds to assist in the $75,000 cost of acquiring the Kennesaw House property. Later, the City sold the property to a private developer for $75,000, but did not remit to the Interior the Federal share ($15,000) of the sales proceeds.

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[3]"Improved Standards Needed for Managing and Reporting Income Generated Under Federal Assistance Programs" (GAO/GGD-83-55, July 22, 1983).

APPENDIX I

--Georgia subgranted Federal funds of $30,000 to the Athens-Clarke Heritage Foundation to assist in stabilizing the Franklin House project. The subgrantee's match was provided by the value of the property, which was purchased for $75,000. Three years later, the property was sold for $75,000 to a private individual for further development. The subgrantee retained the entire amount and did not remit the Federal share of sales proceeds amounting to about $21,000.

--Oregon subgranted Federal funds of nearly $30,000 to a private individual in Portland to assist in acquiring the Bishop's House property at a total cost of $120,000. Three years later, the property was sold for $200,000 to another individual who subsequently applied for and received Federal funds for restoring the property (painting). The seller retained all proceeds and did not remit the Federal share amounting to $50,000.

We discussed the two Georgia cases with State and Federal regional officials. They stated that because the sales occurred after the project period, no computation and remittance of a Federal share of the proceeds was required.

The OMB property management standards provide that grantees should use the real property for authorized purposes of the original grant and when the real property is no longer needed and is sold, the Federal Government is to be paid its fair share of the sales proceeds. Further, the standards do not distinguish between property sold before or after the project period. We believe the standards require payment of the Federal share when property is sold, regardless of the time of disposition.

RECOMMENDATIONS TO THE SECRETARY OF THE INTERIOR

We recommend that the Secretary of the Interior

--Direct the NPS and FWS to review grantees' practices on the use of income and to emphasize that program income must be used for program purposes.

--Direct the NPS and FWS to establish regulations governing the (1) timing and allowability of program income expenditures and (2) disposition of interest earned on invested program income funds.

--Direct FWS officials to determine whether any Federal share exists in the interest earned on the two Florida wildlife accounts.

--Direct the NPS and FWS to review and, where appropriate, revise their regulations on the options available to

grantees for using program income to ensure that they reflect statutory requirements and clarify them as appropriate to remove internal conflicts.

--Direct FWS officials to be consistent in requiring grantees to account for and report on income from the sale of wildlife management area permits, taking into consideration FWS' policy statement on this issue.

--Direct the FWS to require grantees to use the Financial Status Report for reporting program income and all other types of grant-related income.

--Direct the NPS to enforce the Historic Preservation Program regulations requiring grantees to remit the Federal share of proceeds realized from the sale of real property without regard to whether the property is sold during or after the project period.

AGENCY COMMENTS AND OUR EVALUATION

Interior generally agreed with our recommendations, stating that it recognizes a need to provide more explicit guidance to grantees. Interior will consider our report and recommendations in preparing such guidance. (See app. III.)

Interior also commented that it supported the need for improvements in dealing with the issue of grant-related income. To obtain Government-wide consistency, Interior would like OMB to establish standards on the timing and allowability of program income expenditures and the disposition of interest earned on invested income. In a report to OMB, we made recommendations along these lines.[4]

Regarding our recommendation that NPS and FWS review grantee program income practices and emphasize that the income be used for program purposes, NPS commented that it relies on periodic fiscal compliance audits and inspections to monitor grantees' program income practices and will continue to do so. NPS added, however, that it will also explore the possibility of increasing the emphasis on grantee reporting of income to address our concerns about grantees neglecting to report income.

FWS stated that its policies are clear, that the use of program income is limited to eligible program activities, and because of limited FWS staff resources, it must rely on grantees to comply with the policy. FWS added that it did not believe that large-scale violations of the policy existed. The intent of our recommendation to FWS was not to suggest that it conduct

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[4]"Improved Standards Needed for Managing and Reporting Income Generated Under Federal Assistance Programs" (GAO/GGD-83-55, July 22, 1983).

separate reviews of grantees' program income practices, but merely for FWS during its normal grantee audits and reviews to pay special attention to the recently emerging problem as identified in Utah, Indiana, and several other States.

FWS agreed to clarify its guidance on the timing and allowability of program income expenditures and to incorporate in its guidance a discussion on the disposition of interest earned on invested program income funds pending OMB concurrence with the principle we proposed. OMB, in its comments to us on a related report, agreed to establish standards on the disposition of interest.

NPS believes that the interest on program income should generally be treated the same as the income itself and, with regard to the timing and allowability of income expenditures, that grantees should be clearly informed on the requirements. NPS pointed out, however, that we did not clearly distinguish among the different types of income and the consequent variations in need for program controls. Using the OMB standards as criteria, our concern and report discussion center only on that program income earned from nonrecreational activities (as defined by NPS) during the project period and on sales proceeds. Thus, this is the type of income for which we recommend that NPS establish program requirements.

FWS agreed to review the two Florida wildlife accounts in regard to the Federal share of the interest being earned on them. FWS, subject to the issuance of a policy on interest, stated that it will request that future, but probably not past, interest earnings be returned to the program. We understand FWS' reluctance to require a retroactive adjustment and are satisfied with its agreement to address the issue on a prospective basis.

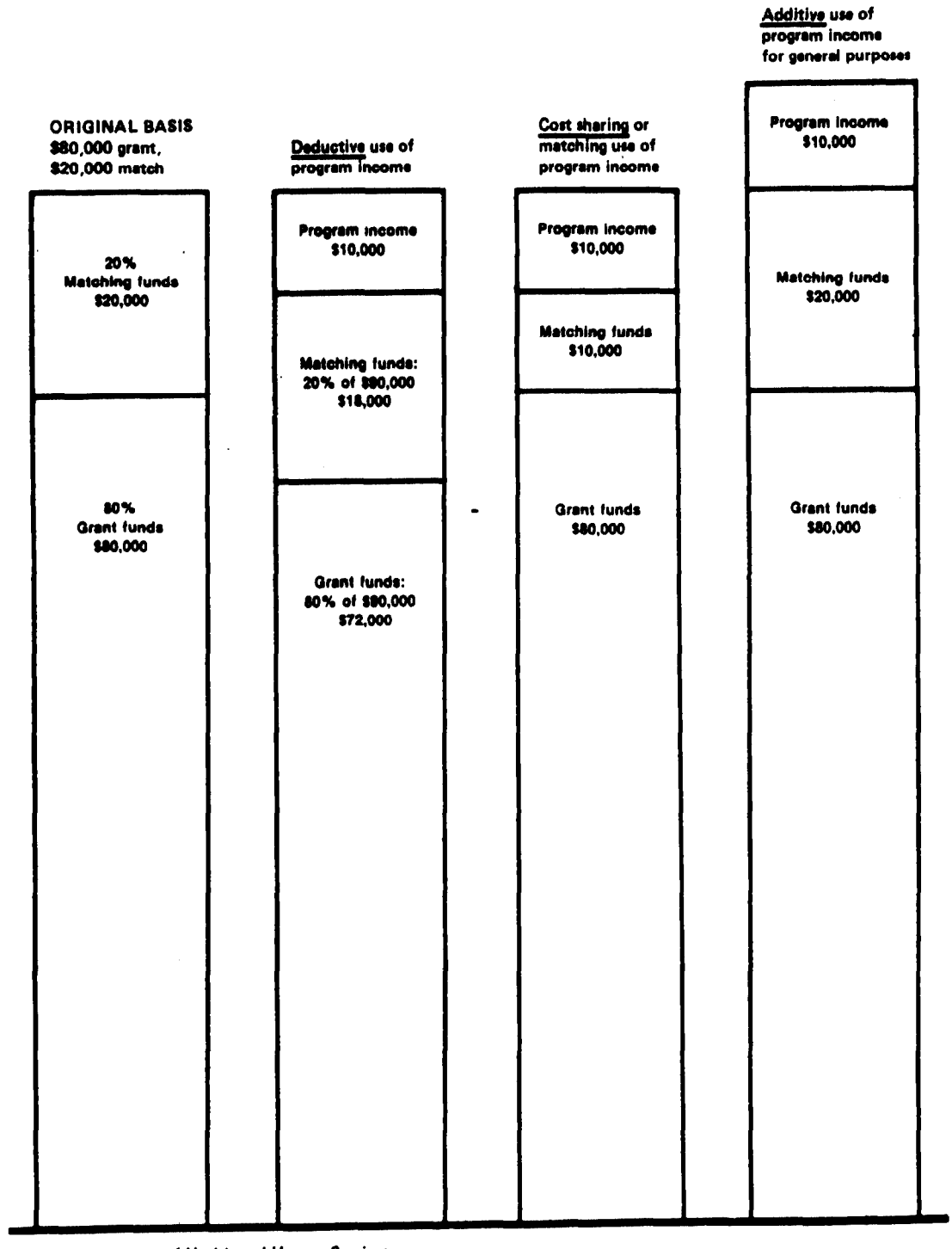
FWS also agreed to (1) clarify the requirements for accounting and reporting of income from the sale of wildlife management area permits and (2) review its current financial reporting requirements related to the reporting of income. Further, both FWS and NPS agreed to clarify their guidance on the options for using program income.

NPS disagreed with our recommendation that it require grantees to remit the Federal share of proceeds realized from the sale of real property. NPS maintains that its grantees are not buying or developing property for use by the Federal Government or the States, but are preserving the property from destruction or disrepair. Thus, NPS states, OMB Circular A-102 (Attachment N) is not fully applicable to these situations and does not require repayment of the Federal share when property is sold. According to OMB, there is no question that Attachment N requires the repayment of the Federal share when property is sold. Thus, as long as NPS has regulations incorporating Attachment N requirements, it is required to enforce them. We

therefore continue to believe that NPS should require remittance of the Federal share of real property sales proceeds.

APPENDIX II

USE OF PROGRAM INCOME



Source: Department of Health and Human Services

APPENDIX III

United States Department of the Interior

OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20240

JUL -6 1983

Mr. J. Dexter Peach, Director
Resources, Community, and Economic
Development Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Peach:

This responds to your request for comments on the draft report, "Interior Should Improve Its Policies and Practices on Grant-Related Income".

Enclosed are our comments in response to the specific recommendations made in this report.

The Department supports the need for improvement in the area of grant-related income and urges that several recommendations be made to OMB for clarifying the Attachment on Program Income in Circulars A-102 and A-110. Specifically, we believe that governmentwide consistency could be achieved if timing and allowability of program income expenditures and disposition of interest earned on invested program income funds were covered in the Attachment and if a requirement were added that agreements should also cover these issues when applicable.

Since the draft report indicates that plans are being made to recommend to OMB revision of the Financial Status Report - Standard Form 269 and since we understand that a project is underway at OMB to revise the Circulars A-102 and A-110, we believe that this would be an appropriate time to recommend additional changes as discussed above.

Thank you for an opportunity to comment.

Sincerely,

Deputy Assistant Secretary -
Policy, Budget, and Administration

Enclosure

APPENDIX III

THE DEPARTMENT OF THE INTERIOR
RESPONSE TO GAO DRAFT REPORT

"INTERIOR SHOULD IMPROVE ITS POLICIES AND PRACTICES
ON GRANT-RELATED INCOME"

General Comment:

The Fish and Wildlife Service

The Fish and Wildlife Service's grant programs cover a broad range of activities, many of which have the potential for producing program income. Recognizing the complexity of the program income issue, we developed, in consultation with the Office of Audit and Investigation, guidance on program income. This guidance was issued in 1977 and incorporated previous formal and informal guidance on specific questions. Our guidance represented an attempt to clarify a complex subject based on our interpretation of A-102 provisions applied to our grant programs.

We have recognized a need for providing more explicit guidance to grantees as part of our Federal Aid Manual. Preliminary work has begun on this guidance and will consider your report and recommendations in preparation of the guidance. We anticipate completion of this project by September 30.

RECOMMENDATION:

Direct the NPS and FWS to review grantees' practices on the use of income and to emphasize that program income must be used for program purposes.

RESPONSE:

The Fish and Wildlife Service

We believe our current policies are clear that the use of program income is limited to eligible program activities. Given our limited manpower resources, we cannot review all active and completed projects which may produce income. Therefore, we must to a large extent rely upon grantees to comply with this policy. The examples given, i.e., Utah and Colorado, were disclosed through existing relationships with the grantees. We do not believe there are large-scale violations of this policy which would indicate a need for the allocation of additional resources to monitoring or for the imposition of additional administrative burden on all the grantees.

The National Park Service

The NPS questions the need for a separate review of grantee practices on use of program income. Controls over such practices are already included in existing audit and project inspection programs. These controls appear sufficient to provide for correction of significant abuses.

Both Historic Preservation Fund and the Land and Water Conservation Fund (L&WCF) programs have been covered for years by standard and periodic fiscal compliance audits. The L&WCF program also provides for periodic

inspections of active and completed grant sites. While audit procedures have changed over the years, from the multiple agency to the single agency concept for example, this area of concern will continue to be covered under Attachment P audits (Circular A-102) currently required, as well as by the agency's on-site inspections. However, the Service will explore the possibility of increased emphasis on grantee reporting of income on active projects to complement existing compliance efforts and address the report's concerns about grantee failures to report income.

RECOMMENDATION:

Direct the NPS and FWS to establish regulations governing the (1) timing and allowability of program income expenditures, and (2) disposition of interest earned on invested program income funds.

RESPONSE:

The Fish and Wildlife Service

We agree that program income should be promptly used and will clarify this in our guidance. However, not all income can be used during the period of the project. For example, income from closed projects such as proceeds from sales cannot be deducted from or added to the project. Therefore, we would allow a reasonable period to use these funds to carry out other eligible program work. The treatment of interest earnings on program income is not clear in Attachment E of A-102 and was not addressed in our previous guidance. However, we agree to incorporate a discussion of interest in our revised guidance if OMB concurs with this principle.

The National Park Service

We agree that grantees should be clearly informed on the disposition of program income, but feel that the report fails to distinguish clearly among different types of program income and the consequent variations in need for program controls.

1) Income on active versus completed projects: There are substantial differences between program income which accrues during a project's active matching period and income that becomes available once a project is completed and all Federal matching funds are expended. In the former case, the "deductive" and "cost sharing" options defined in OMB Circulars A-102 and A-110 are feasible, although generally difficult to apply. In the latter case, the "additive" approach is the only reasonable choice for most completed grants.

2) Income from property sales or leases versus income from entrance or user fees: The Land and Water Conservation Fund (Outdoor Recreation) grants program has strong, legislatively-mandated controls over "conversion" income from sale or lease of grant-assisted properties (cf. section 6(f)3 of L&WCF Act). Reimbursements for or replacements of any sold property are required by the Secretary. Lease income in these cases would normally be earmarked for use, in an additive fashion, to support further development or operation of grant assisted facilities.

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The historically-accepted use of entrance or user fees at park and historic sites to defray a portion of operational and maintenance costs is an entirely different matter. It is our opinion that State or local development or operational expenditures which equal or exceed such user-generated income adequately and automatically meet legislative and executive mandates for additive use of program income, regardless of the timing or disposition of actual revenues (i.e., the fiscal year of expenditure and the particular account into which user revenues are deposited are irrelevant so long as user revenues do not exceed actual State or local expeditures for program purposes during a given period).

It would also be unreasonable to impose "allowable cost" standards on such expenditures from program fees, since they are imposed and intended specifically to meet operation and maintenance purposes that are required by the L&WCF and HPF legislation, but are not eligible for Federal matching funds under the two programs.

3) The relatively small Historic Preservation Fund grant program is unique among Interior programs. These grants are awarded to States annually on a total program basis, rather than for individual acquisitions or developments. States subgrant allocated funds to third parties in addition to funding their own projects and programs. In this highly complex situation, suggested revisions could cause unnecessarily burdensome paperwork and administrative efforts greatly out of proportion to the small amounts of program income ordinarily generated.

4) Direct program income versus interest on program income: The NPS is essentially in agreement with the report's conclusion that interest on program income should fall under the same requirements as direct income, taking into account the distinctions made in comments (1) through (3) above.

RECOMMENDATION:

Direct FWS officials to determine whether any Federal share exists in the interest earned on the two Florida wildlife accounts.

RESPONSE:

The Fish and Wildlife Service

We will review the two Florida wildlife accounts. Subject to the issuance of a policy on interest, we will request that future interest earnings on program income should be returned to the program. Given our lack of a previous policy on this matter, we are reluctant to require a retroactive adjustment.

RECOMMENDATION:

Direct the NPS and FWS to review and, where appropriate, revise their regulations on the options available to grantees for using program income

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to ensure that they reflect statutory requirements and clarify them as appropriate to remove internal conflicts.

RESPONSE:

The Fish and Wildlife Service

We will attempt to clarify the options for using program income in our revised guidance.

RESPONSE:

The National Park Service

The Land and Water Conservation Fund (Outdoor Recreation) grants program has strong legislatively-mandated controls over "conversion" income from sale or lease of grant-assisted properties. It is our opinion that State or local development or operational expenditures which equal or exceed income generated from entrance or user fees adequately and automatically meet legislative and executive mandates for additive use of program income, regardless of the timing or disposition of actual revenues.

For Historic Preservation Grants, the wording in the program's Grants Management Manual does not provide a separate definition of the additive option. The manual states the additive option as the objective, with the cost-sharing and deductive options specified as alternatives. The additive approach is the intended preference. Because of a possible lack of clarity in this area, the Grants Management Manual will be revised in the future to specify explicitly the three options listed in Attachment E of Circular A-102.

RECOMMENDATION:

Direct FWS officials to be consistent in requiring grantees to account for and report on income from the sale of wildlife management area permits, taking into consideration FWS' policy statement on this issue.

RESPONSE:

The Fish and Wildlife Service

We will attempt to clarify the requirements for accounting and reporting of income from user fees.

RECOMMENDATION:

Direct the FWS to require grantees to use the Financial Status Report for reporting program income and all other types of grant-related income.

RESPONSE:

The Fish and Wildlife Service

We will review our current financial reporting requirements related to

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the reporting of program income. Our basic policy has been to minimize the reporting burden on the grantees, and we elected to waive the Financial Status Report. We believed that sufficient financial information was available on the SF-270 and SF-183.

RECOMMENDATION:

Direct the NPS to enforce the Historic Preservation Program regulations requiring grantees to remit the Federal share of proceeds realized from the sale of real property without regard to whether the property is sold during or after the project period.

RESPONSE:

The National Park Service

There are several issues involved. First, this recommendation appears inconsistent with the definition of program income provided in the introductory Background section of the report. Program income is "...any money received by grantees during the course of operating federally assisted programs." (Underline supplied.) Second, the examples are Historic Preservation Fund subgrants from the States of Georgia and Oregon to third parties, one city, one foundation and one private individual. In each instance the primary purpose of the subgrant was not to transfer use of the property; instead, the purpose of the grant was to insure the preservation of each property for at least 20 years for public benefit. This view is based on Section 101(a)(2) of the National Historic Preservation Act of 1966, which authorizes grants to the States to preserve properties for public benefit and prohibits the Secretary of the Interior from granting funds unless the grantee (the State) has agreed to assume, after completion of the project, the total cost of the continued maintenance, repair, and administration of the property (Section 102(a)(5)). Covenants (or deed easements) for privately-owned property and contract provisions with respect to public property are required to assure compliance with these two provisions of law. The continued maintenance requirements of Section 102(a)(5) apply to and are finally enforceable upon the State unless the State passes the burden to the property owners.

Therefore, what is being obtained with the Federal grant is a preservation easement for the benefit of the general public. The easement remains even though the property is subsequently sold. Attachment N is not fully applicable because the property was not purchased or developed for the use of the Federal Government or the State, but rather to preserve the property from destruction or disrepair. The Federal Government does not obtain an interest in the property except to oversee the State's monitoring of the preservation easement. In this relationship, the grant is viewed as a gift and proceeds of the grant are not taxable as ordinary income (Section 162(a)(6). We disagree that Attachment N requires repayment of the Federal share when the property is sold.

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