



UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF ADMINISTRATIVE LAW JUDGES

APPLICATION OF SCHOOL DISTRICT

OF PHILADELPHIA,

Applicant.

Docket No. 11-33-R

Recovery of Funds Proceeding

ACN: ED-OIG-A03H0010

ORDER RE MOTION TO DISMISS BY THE PHILADELPHIA SCHOOL DISTRICT AND ACCEPTANCE OF JURISDICTION

This matter involves an appeal by the School District of Philadelphia (PSD) of a preliminary departmental decision (also known as a program determination letter (PDL)) issued by the Assistant Secretary for Elementary and Secondary Education and the Assistant Deputy Secretary for Safe and Drug Free Schools (ED) in which ED demanded the return of \$9,968,423 in Title I and II funds for the period July 1, 2005 through June 30, 2006. On June 3, 2011, PSD filed a motion to dismiss this action on the theory that the PDL does not establish a prima facie case as required by 34 C.F.R. § 81.34(b) (2010) and that it must be returned to ED as required by 34 C.F.R. § 81.38(b). ED opposed the motion and asserted that the 13 instances of errors identified by PSD in ED's PDL did not constitute errors or, if so, were so insignificant as not to warrant the return of the PDL. For the reasons stated below, PSD's motion to dismiss is denied.

Under 20 U.S.C. § 1234a(a)(1), the Secretary is required to provide written notice of a PDL to a grantee "whenever the Secretary determines that a recipient of a grant . . . under an applicable program must return funds because the recipient has made an expenditure of funds that is not allowable under that grant . . . or has otherwise failed to discharge its obligation to account properly for funds under the grant." This written document serves a dual function.¹ It is a notice to a grantee for return of grant funds. It also constitutes the Department's presentation

¹ A PDL is the formal request for repayment of various grant monies that purportedly have been misspent. Generally, a PDL includes a summary of the findings and recommendations by the auditors, responses by the auditee, and the determination by the appropriate Assistant Secretary or other designated official.

of its case in chief regarding the disallowed expenditures. As such, the PDL represents the first step in the process of receiving evidence in a contested matter during the administrative review. As an evidentiary matter, the Department's case in chief must establish a prima facie case and, if it fails to do so, the PDL is returned to the issuing officer. Thus, Section 1234a provides—

(a)(2) In a . . . [PDL], the Secretary shall have the burden of establishing a prima facie case for the recovery of funds . . . The facts to serve as the basis of the . . . [PDL] may come from an audit report, an investigative report, a monitoring report, or other evidence.^[2]

(b)(1) . . . As expeditiously as possible, the [tribunal] . . . shall return to the Secretary for such action as the Secretary considers appropriate any [PDL] . . . which the [tribunal] . . . determines does not meet the requirements of subsection (a)(2) of this section.

A prima facie case is established if “the law and the facts . . . unless rebutted, is sufficient to sustain the conclusion drawn” in the PDL. 34 C.F.R. § 81.34(b)(2).

Under the Department's administrative review process, the tribunal examines a PDL and ascertains whether it establishes a prima facie case. That is, from an evidentiary point of view, has the Department met its burden of going forward based on the facts and law in the PDL? *See generally In Re South Dakota*, Dkt. No. 91-24-R (ALJ Op. Aug 16, 1991) at 3. The tribunal, in accordance with the Secretary's decision in *In re South Dakota*, Dkt. No. 91-24-R (Oct. 21, 1991), returns only that portion of the PDL that fails to establish a prima facie case--

[f]inally, although I find that the PD[L] does state a prima facie case on the interest issue, even if it did not, the return of the entire PD[L] to OVAE would not be the appropriate remedy. South Dakota challenged only one basis for the disallowance of the \$150,000, the other two rationale for the disallowance [of the \$150,000] were not challenged and clearly meet the prima facie case requirement. Accordingly, the appropriate remedy for failure to state a prima facie case on the interest finding would have been to return only that portion of the PD[L]. The remainder of the PD[L] would have remained in effect.

In re South Dakota, at 5.

It is incumbent upon the moving party in a motion to dismiss to articulate the aspect or aspects of a PDL in which ED failed to establish a prima facie case. As to each aspect, the moving party shall identify the fact or facts that have not been established and explain how the absence of that fact or facts, in turn, results in ED's failure to establish a prima facie case.

² In addition to facts as a means to establish a prima facie case, a prima facie case may also be established if the recipient fails “to maintain records required by law, or to allow the Secretary access to such records.” 20 U.S.C. § 1234a(a)(3).

In the instant case, the PDL contains three findings and several subparts within each finding as well as ten exhibits. It seeks the recovery of the following amounts--

| Finding | Amount |
|----------------------|-------------|
| Finding 2 | \$6,796,172 |
| Finding 4, Section A | \$1,815,754 |
| Finding 4, Section B | \$ 2,198 |
| Finding 5, Section A | \$1,343,986 |
| Finding 5, Section B | \$ 10,313 |

PSD asserts 13 instances of errors each of which causes the PDL to fail to establish a prima facie case. This, in turn, warrants the return of the PDL to ED. These errors are addressed below.

In Finding 2, ED determined that PSD used Federal grant funds to supplant state and local funding with respect to various contracts in the total amount of \$5,248,988. The essence of this finding is that various items of expenditures were charged against the general fund. Subsequently, these charges were reversed and then charged to an account of Federal funds. In the preceding year, similar costs with the same transaction codes were paid from the general fund.

The first error noted by PSD is in the first paragraph on page 9 of the PDL. This paragraph sets forth the facts regarding the \$5,248,988 of expenditures by PSD that were backed out of the general fund and then charged against the Federal grant under Title I, Part A. Error 1 is the PDL's mistake in articulating the size of the auditor's sample. In the first sentence, the size was stated as 60 transactions even though it was only 50 transactions as noted correctly in the second to the last sentence in the same paragraph. The error in the stated size of the sample is harmless because the correct sample size is readily apparent.

The second error concerns the date on which PSD changed the payment source of the expenditures from the general fund to the Federal grant. The summary paragraph on page 9 of the PDL identifies the date of the transactions as 9/3/3006. This date is an obvious error. The correct date is 9/30/2006 and is readily apparent from its inclusion in the in-depth discussion of these transactions located in the third preceding paragraph of the PDL. As such, the error is harmless and has no effect on whether the PDL establishes a prima facie case in Finding 2.

In Finding 2, the PDL levies a charge of supplanting concerning the teacher training program in the total amount of \$1,395,685. The PDL identifies two samples compiled by the auditors -- sample 18 has 20 individual transactions and sample 19 has 15 individual transactions. These transactions represent charges in the total amount of \$1,395,685 to its Title II, Part A program. These charges were traced using their accounting codes to their original entries. As a result, it was discovered that PSD originally charged these expenditures to a State-funded Empowerment Grant and later reversed the transactions and charged these expenditures against the Federal, Title II, Part A grant funds. In addition, the PDL notes that PSD charged the same costs to its State-funded Empowerment Grant in the preceding year.

In footnote 8 (PDL at 10), the PDL contains two virtually identical paragraphs that address matters concerning sample 18 and sample 19. Each paragraph contains a citation to various pages in the attached exhibit wherein individual transactions are identified that reflected the transfer of funds from the State-funded Empowerment Grant to the Federal Title II, Part A grant.

Error 3 concerns an incorrect exhibit number in a citation in the first paragraph of footnote 8. While the citation is to various pages in “Ex. 3”, the correct exhibit number is “Ex. 2.” This error is obvious given that Exhibit 3 contains only 2 pages while the citation refers to pages ranging from 3 to 29. It is also apparent from the text of Finding 2 concerning the teacher training program, including the date of transfer of the charges and the ABC codes, and the remaining citations within footnote 8 that the correct exhibit citation is Exhibit 2. This mistake is harmless error with regard to ED’s requirement that the PDL establish a prima facie case.

In error 4, PSD asserts that Exhibit 2 has two sets of page numbers and that it cannot with certainty identify the correct set used by the issuing officials. One set has the form “x / xxx” and the other set has numbers. The tribunal finds no confusion in the pagination of the PDL.³

In Finding 4, the PDL addresses various travel reimbursements by PSD that the auditors found unallowable or unsupported. The PDL notes that the auditors reviewed 75 travel reimbursements, totaling \$51,651, and determined that \$9,532 of the travel expenditures were unallowable. The auditors also found unallowable the indirect costs associated with these expenditures. PDL at 18.

In the PDL, ED sustained the auditors’ findings and concurred with their recommendations—

[t]he various columns in PDL Ex. 7 identify each travel reimbursement that the auditors found unallowable or unsupported, and provide an explanation of the auditors’ reasons for doing so. For reasons summarized by the auditors on pp. 40-42 of the audit report, we agree that in each instance PSD’s expenditure of funds is either unallowable on its face, or unallowable for lack of adequate documentation . . .

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The applicable statute of limitations . . . provides that a grantee shall not be liable to refund funds expended in a manner not authorized by law more than five years before the recipient received the Department’s program determination. While we conclude that all

³ With regard to various disallowed charges, ED seeks to recover an additional amount reflecting the indirect costs associated with each of these charges. On page 5a of Exhibit 6, there is a calculation that illustrates the mathematical determination of the additional recovery reflecting the indirect cost component. In photocopying this exhibit, a portion of the text identifying the cost and indirect cost was omitted from PSD’s copy of the PDL. This omission is error 5. In its response, ED provided PSD with a complete copy of this page. This exhibit is only marginally related to the matter at hand and was added to the PDL as a mere illustration. Hence, it has no bearing on whether the PDL establishes a prima facie case.

of the \$9,532 the auditors identified as misspent is, in fact, unallowable, for purposes of this PDL we have concluded from our calculation of misspent funds those that PSD charged on or prior to 3/17/2006 (Sample 62 on PDL Ex. 7). [fn omitted] The remainder of unallowable costs that the auditors identified on PDL Ex. 7 (*itemized in the second to last column "Total Questioned Costs" on p. 2b of Ex.7*) is \$2,149.^{fn16}

We determine that \$2,149 that PSD spent for travel costs were misspent and are subject to recovery.

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The \$2,198 identified above (\$2,149 in direct costs and \$49 in indirect costs) neither paid for services authorized by the Federal programs, nor for a charge that was reasonable, necessary, or allocable to program funds Therefore, we have determined that PSD misspent \$2,198 of Federal funds that is subject to recovery.

Fn. 16 Those costs not subject to the statute of limitations are reflected on pp. 3a and 3b of PDL Ex. 7.

(Emphasis added); PDL at 20-21.

Under error 6, PSD notes that the column "Total Questioned Costs" (italicized in the second paragraph of the quoted material from the PDL) was missing from page 2b of Exhibit 7. Moreover, this exhibit had only one column on page 2b, not at least two columns on that page as indicated in the italicized material. In error 7, PSD notes that pages 3a and 3b to Exhibit 7 are missing.

As explained by ED, the size of the font inexplicably changed during the copying of the final set of exhibit pages for Exhibit 7. As a result, the column "Total Questioned Costs" was produced on page 2a, leaving only one column, not two, on page 2b. In addition, the change in font moved the information on pages 3a and 3b to pages 2a and 2b. Hence, the format of the pages was altered; however, no information was omitted. Thus, this aspect of error 6 and error 7 are of no consequence.

As noted above in the PDL, ED determined that \$9,532 of the travel expenditures was unallowable. The PDL also noted that certain expenditures were barred from recovery due to the effect of the statute of limitations. As such, only the expenditures made after March 17, 2006, are recoverable and not barred by the statute of limitations. According to the PDL, ED is limited to a recovery of \$2,149 of the \$9,532 of misspent expenditures.

In its motion to dismiss, PSD questions the \$2,149 figure and its source. In its response, ED acknowledges that this figure is incorrect and that the correct amount of recovery should be \$2,520 based on the nine transactions that occurred after March 17, 2006. ED Response Br. at 14-15; Ex. 7 at 1a and 1b. ED argues that the error was made in determining the effect of the statute of limitations on the amount of the recovery, an affirmative defense that is typically raised by a grantee. As such, this error had no effect on whether the PDL established a prima facie case as that matter deals with the expenditures that comprise the \$9,532 of travel expenses.

In its reply, PSD asserts that this error results in a lack of clarity regarding the amount being sought for recovery and therefore argues that ED failed to meet its burden of establishing the facts and law to support the recovery of funds.

The tribunal agrees with ED. At his stage of the proceeding, the sole focus is on ED's presentation of its case in chief as it has the burden of going forward and must establish a prima facie case. The statute of limitations is an affirmative defense and, as such, is a matter considered as part of PSD's case. In this context, the mistake in the amount of recovery attributable to the effect of the statute of limitations is harmless error.

In Finding 5, the PDL levied a charge of supplanting concerning various transportation costs incurred in the amount of \$1,322,875. Once again, the expenditures had been charged to the general fund, then reversed, and charged to a Federal grant.

Errors 8 and 9 concern the misidentification of references regarding Finding 5A. In error 8, the PDL misidentified a secondary citation in a paragraph in which the PDL summarizes the auditors' conclusion in Finding 5A dealing with bus and school choice transportation costs in the approximate amount of \$43,000. Here, the citation was to pages 5-6 of Exhibit 8 while the correct cite was to pages 5-6 of Exhibit 9. Because the auditors' conclusion was rejected by ED, the misidentification of the appropriate exhibit number is a harmless error. This reference was also misidentified in a subsequent paragraph on page 29 of the PDL. Here, the purpose of the citation was merely to confirm a statement made in the body of the PDL. Hence, this error is also harmless.

Error 9 asserts three instances of misidentification in two paragraphs in Exhibit 9. In each instance, Exhibit 9 was erroneously identified as Exhibit 8. The statements in the text of the PDL set forth the relevant facts. These references were made to the exhibit as a means to identify the underlying documentation. The errors are harmless and have no effect on whether the PDL establishes a prima facie case.

As part of Finding 5B, the PDL concluded that PSD charged \$41,920 of transportation costs to Title I, Part A in six transactions as a result of the after-school program at the Pepper Middle School. Of the \$41,920, \$11,040 was considered a proper charge and \$30,880 was unsupported. Since two of the six charges against the grant funds in the total amount of \$10,240 were barred from recovery by virtue of the statute of limitations, the amount of the recovery sought by the PDL was reduced from \$30,880 to \$20,640.

In its reply brief, PSD asserts two concerns. There is an unexplained inconsistency between the total of the unsupported transportation charges of \$53,695 as detailed and reported on page 2 of Exhibit 8 and the total charges associated with transportation to and from the program of \$41,920 as detailed on page 27 of the PDL. In its view, the numbers cannot be reconciled.

The tribunal finds that the numbers are consistent and reconcilable. The total charges associated with transportation, i.e. \$41,920, is the difference between the total of the unsupported transportation charges of \$53,695 and several adjustment made to its components as follows—

| | Original Total | Reduction | Net | Cite |
|-----------|------------------|-----------|------------------|------------------------|
| ACC 6740 | \$ 1,600 | \$1,600 | 0 | PDL at 30 |
| OMBG 1813 | 3,520 | 0 | 3,520 | |
| OMBG 1910 | 7,275 | 555 | 6,720 | Ex. 9, sample 10, p. 2 |
| OMBG 1937 | 4,260 | 740 | 3,520 | Ex. 9, sample 13, p. 2 |
| OMBG 1993 | 7,045 | 2,405 | 4,640 | Ex. 9, sample 16, p. 3 |
| OMBG 2091 | 12,160 | 0 | 12,160 | |
| OMBG 2091 | 370 | 370 | 0 | Ex. 9, sample 26, p. 4 |
| OMBG 2113 | 12,100 | 740 | 11,360 | Ex. 9, sample 28, p. 5 |
| OMBG 2150 | 4,255 | 4,255 | 0 | |
| OMBG 2155 | 1,110 | 1,100 | 0 | |
| | <u>\$ 53,695</u> | | <u>\$ 41,920</u> | |

The second concern is the purported failure by the PDL to identify those transactions among the ten transactions pertaining to transportation on page 2 of Exhibit 8 that were supported and unsupported. The method of determining the allocation of the \$41,920 between supported and unsupported charges is addressed on pages 26 and 27 of the PDL and warrants no further discussion here.

The last series of errors deals with Finding 5B that addresses the proper approach to calculate PSD's indirect costs. Indirect costs were recorded at the discretion of the PSD's analysts. In some instances, multiple charges to indirect costs were made during the fiscal year. In determining the indirect costs after the initial charge for indirect costs, PSD did not, however, reduce the total expenditure by the amount of the previously recorded indirect costs. As a consequence, the base for the indirect cost assessment was overstated and thereby inflated the subsequent determination of the amount of its indirect costs. The PDL and Exhibit 10 identify six transactions in which this occurred and provide the details. The PDL notes that the first of the six transactions, and the earliest in time, is dated March 26, 2006. The PDL concludes that the total unallowable costs for the double charges is \$11,063. Lastly, the PDL indicates that the

statute of limitations bars the recovery of the March 26, 2006 transaction in the amount of \$750 and, therefore, the amount of recovery was reduced from \$11,063 to \$10,313.

In its error 10, PSD notes that the date of the “first” transaction as identified in the PDL is not March 26, 2006, rather it is March 16, 2006. Moreover, the PDL incorrectly identifies this charge as the earliest in time because there was another transaction, identified as sample 2 on pages 2a and 2b of Exhibit 10, that occurred on September 28, 2005.⁴ Lastly, error 12 maintains that the amount of the March 26th transaction as identified in the PDL was not \$750, rather it was \$775.

ED acknowledges that the PDL misidentified the date and the amount of the “first” transaction as well as its chronological order in the sequence of the six transactions. The correct date of the transaction is March 16, 2006 and the correct amount is \$775. As such, it was the second of the six transactions by the date of its occurrence. In its view, however, these errors are not relevant to the validity of the PDL and whether it establishes a prima facie case.

The tribunal agrees that the PDL contains these errors. These errors are relevant with regard to the effect of the statute of limitations. As noted earlier, this affirmative defense is a matter for consideration as part of PSD’s case. As such, it is not a factor to be considered in determining whether the PDL establishes a prima facie case. These errors are harmless.

ORDER

In conclusion, the various mistakes and misidentifications in the program determination letter as noted by PSD constitute harmless errors and have no effect on whether the program determination letter issued by the Assistant Secretary for Elementary and Secondary Education and the Assistant Deputy Secretary for Safe and Drug Free Schools establishes a prima facie case as required by 20 U.S.C. § 1234a(a)(2). Accordingly, PSD’s motion to dismiss the program determination letter is hereby denied.⁵

In addition, the tribunal reviewed the program determination letter and concludes that it establishes “a prima facie case for the recovery of funds, including an analysis reflecting the value of the program services actually obtained in a determination of harm to the Federal interest.” 20 U.S.C. § 1234a(a)(2).

Lastly, PSD’s application for review has also been examined. It complies with the requirements of 34 C.F.R. § 81.37 and was filed within the period allowed by 20 U.S.C. § 1234a(b)(1).

⁴ In error 11, PSD argues that two of the six transactions were booked in fiscal year 2005. This is incorrect. The transactions occurred in fiscal year 2006.

⁵ Due to a thorough discussion of the issues on brief by the parties, an oral argument is not necessary. The argument scheduled for August 26, 2011, is cancelled.

/s/

Allan C. Lewis
Chief Administrative Law Judge

Issued: August 10, 2011
Washington, D.C.