

September 30, 2005

MEMORANDUM FOR: EMILY STOVER DeROCCO  
Assistant Secretary for  
Employment and Training



FROM: ELLIOT P. LEWIS  
Assistant Inspector General  
for Audit

SUBJECT: Insufficient Federal Guidance  
Could Result in Misuse of Incumbent  
Worker Training Program Funds  
Management Letter No. 06-05-003-03-390

## **SUMMARY**

The Department of Labor should strengthen its guidance to states on how to properly spend Workforce Investment Act (WIA) incumbent worker funds. Lack of such guidance could lead to misuse of funds as evidenced by the State of Arkansas' use of WIA funds as incentive monies offered to the Nestle Corporation to locate in Jonesboro, Arkansas. Under the existing WIA, only the State can fund incumbent worker training under the Governor's 15 percent statewide set-aside funds.

Our concern over lack of Federal guidance is timely since proposed legislation for WIA reauthorization provides that local boards could spend up to 10 percent of their funds for incumbent worker training. Consequently, more funds may be spent on this program in the future.

The purpose of this management letter is to communicate our conclusions and make recommendations for corrective action.

## **BACKGROUND**

The Arkansas Division of Legislative Audit (ADLA) received a complaint alleging mismanagement of State and/or Federal funds by the Arkansas Workforce Investment Board (AWIB), the Arkansas Employment Security Department (AESD), and the Northeast Arkansas Workforce Investment Board (NEAWIB). The ADLA requested the

Office of Inspector General's (OIG) assistance in reviewing the allegations involving U.S. Department of Labor (DOL) funds.

## **OBJECTIVE, SCOPE, AND METHODOLOGY**

One of the objectives of our performance audit<sup>1</sup> was to determine whether the NEAWIB promised Nestle Corporation \$1 million in WIA funds as incentive money to attract the industry to Jonesboro, Arkansas.

For the allegation regarding the incumbent worker training, we reviewed the AWIB's minutes dated May 8, 2001, through August 20, 2004. We interviewed AWIB, AESD, NEAWIB, and Nestle Corporation staff; reviewed participant files, previously issued audit reports and state auditors' working papers and other documents as related to the allegations; and researched Federal and State laws, regulations, policies and procedures. We performed fieldwork at the AESD and AWIB offices in Little Rock, Arkansas, and Nestle's food processing plant in Jonesboro, Arkansas.

We conducted and reported our work in accordance with Government Auditing Standards.

This management letter should be read in conjunction with the audit report identified in footnote 1.

### **ISSUE: Federal incumbent worker training funds are intended to pay for upgrading current workers skills, not business start-up cost or production costs.**

The preamble to the final WIA Regulations states that incumbent worker training is targeted to workers of a specific employer or employer association to upgrade skills of a particular workforce. We do not believe that WIA Regulations allow employers to use incumbent worker funds to pay for start-up production costs. According to the preamble to the WIA Rules and Regulations published in Federal Register, Volume 65, No. 156, August 11, 2000, page 49333:

Generally, incumbent worker training is developed with an employer or employer association to upgrade skills of a particular workforce. It usually takes place in the workplace or after work hours for employees of a specific employer or employer association. . . . Frequently, such training is part of an economic development or business retention strategy developed by a State. In such cases, the employer is involved in the arrangement of the training curricula and usually has a role in the selection of the training provider. . . .

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<sup>1</sup> On March 31, 2005, the OIG issued Report Number 06-05-002-03-390, Review of Allegations Regarding ETA Funds Granted to Arkansas.

The AWIB contract with Nestle was used to pay part of the cost of supervisors' salaries at the plant in Jonesboro rather than for outside training instructors or courses. The newly constructed plant had both new production equipment and all new employees. Thus, all employees received on-the-job training including some training provided by original equipment manufacturing representatives, prior to production start up. Additionally, employees received some classroom training in plant operating policies and procedures. We concluded the training represented start-up costs for a new plant, not training for incumbent workers. The \$859,904 the AWIB reimbursed Nestle under the guise of an incumbent worker training program was incentive money for locating its plant in Jonesboro, Arkansas and these Federal funds supplanted the employer's costs.

**ISSUE 2: No Federal criteria define how long an employer must be in business or employee must be employed to qualify as an incumbent worker. Consequently, a state could decide that any employer or employee can qualify for a WIA funded incumbent worker program.**

WIA rules in 667.262 prohibit spending WIA Title I funds on "employment generating activities, economic development, and other similar activities, unless they are directly related to training for eligible individuals. . . ." However, no Federal definition of "eligible individual" exists for incumbent worker training. Instead each state defines eligibility for "incumbent worker" services since incumbent worker training is an allowable statewide activity under WIA section 134(a)(3)(A)(iv)(I). According to final WIA regulations (Section 665.220):

States may establish policies and definitions to determine which workers or groups of workers are eligible for incumbent worker services under this subpart. An incumbent worker is an individual who is employed, but an incumbent worker does not necessarily have to meet the eligibility requirements of intensive and training services for employed adults and dislocated workers at 20 CFR 663.220(b) and 663.310.

Arkansas did not have a policy specifically defining WIA "incumbent worker" eligibility other than its "Arkansas Incumbent Workforce Training Program Application and Instructions." Page 5 of this document provides:

The goal of Arkansas' [WIA] Incumbent Workforce funds is to train the current and newly hired workers as industry demands. . . .

This statement makes any employee in the State eligible for incumbent worker training funds even though under WIA these funds are intended to "upgrade skills of a particular workforce." All Nestle's newly hired employees were considered incumbent workers.

The State of Arkansas had established a State "incumbent worker" training program prior to WIA that the Arkansas Department of Economic Development operated. This State program defined eligible workers and employers.

The Arkansas Existing Workforce Training Act (Act 791 of 1995), as amended by Senate Bill 280 during the 82<sup>nd</sup> General Assembly, Regular Session, 1999, provides that “eligible recipients” for such training program means “a full-time permanent employee of an Arkansas company. . . .” The Rules and Regulations for this training program defines a “full-time permanent employee” as a person “working at an Arkansas company, who has been working at the company for at least twenty-six (26) weeks and who works at least thirty (30) hours a week.” In addition, an eligible company was defined as one that had filed an Arkansas income tax return for the year before filing an application for incumbent worker training funds.

However, the State chose not to apply these eligibility criteria to the WIA incumbent worker funds it awarded to Nestle. The Nestle WIA contract was negotiated prior to Nestle locating in Jonesboro, and before the company had any Jonesboro employees.

## **RECOMMENDATIONS**

We recommend the Assistant Secretary for Employment and Training:

1. Issue guidance to the states that clarifies that incumbent worker training programs are intended to pay for skills upgrading, not start-up training costs for a new business. Such guidance might state that skills upgrading includes training that:
  - a. helps an employer’s existing workforce to keep up with technology or other job changes to allow employees to keep their jobs, or
  - b. help workers acquire skills to allow them to be promoted to higher paying jobs.
2. Issue guidance to the states encouraging the states to:
  - a. Establish policies and definitions that set some minimum time period for a company to be in business in a state in order to qualify for incumbent worker training funds available under either WIA statewide activities or local board activities (if current WIA reauthorization proposal becomes law); and
  - b. Set some minimum time for a worker to be employed by his or her current employer in order to qualify as an incumbent worker.
3. Seek to incorporate the recommendations, cited above, into the WIA reauthorization legislation.

## **Agency Response**

ETA disagreed with the OIG's findings in the draft Management Letter that Arkansas' use of Workforce Investment Act (WIA) funding for incumbent worker training was contrary to WIA statute and regulations. However, ETA agreed that additional policy guidance is needed as it relates to both incumbent worker training generally and economic development and employer generating activities that are prohibited by WIA.

The response referenced ETA's policy position that, for the workforce investment system to be relevant and successful in promoting a competitive workforce, it must always be framed in the context of economic development. Also, the response stated that it is a premise of WIA to provide states and local areas with maximum flexibility to design a workforce investment system and utilize funding in ways that meet the unique needs of states and local areas.

While ETA does not agree with limiting the states definition of "incumbent workers," ETA stated its position is that incumbent workers may include any employed worker. ETA also stated that clarity is needed regarding incumbent worker training policy and ETA had already begun developing policy guidance prior to this management letter.

A complete copy of ETA's response to the draft report is included as an attachment to this report.

## **OIG's Conclusion**

Additional policy guidance from ETA regarding incumbent worker training will be helpful. However, we disagree with the specific comments regarding the State's use of incumbent worker training funds.

OIG's report, Report No. 06-05-002-03-390, Review of Allegations Regarding ETA Funds Granted to Arkansas, provides factual evidence that WIA funds were committed for an economic development incentive (for Nestle Corporation to establish a new plant) prior to Nestle's establishing the plant or hiring employees. In other words, at the time of the commitment, there were no employees. WIA regulations at 20 CFR 667.262 (a) prohibit the spending of WIA Title I funds on "employment generating activities, economic development, and other similar activities, unless they are directly related to training for eligible individuals." There was no representation or documentation that the employees who received training met the WIA eligibility requirements.

Also, ETA's assertion that the term incumbent workers may include any employed worker is tantamount to saying that the term has no specific meaning in the context of the program. We question why the drafters of WIA would choose to authorize a

special program for incumbent workers if, in fact, the term could apply broadly to any employed worker.

The report recommendations are unresolved pending receipt and review of the policy guidance ETA is preparing on incumbent worker training and economic development activities.

Attachment

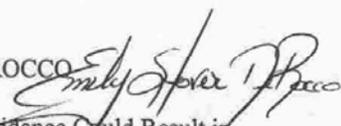
U.S. Department of Labor

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SEP 28 2005

MEMORANDUM FOR: ELLIOT P. LEWIS  
Assistant Inspector General  
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FROM: EMILY STOVER DeROCCO 

SUBJECT: Insufficient Federal Guidance Could Result in  
Misuse of Incumbent Worker Training Program Funds  
Draft Management Letter No. 06-05-003-03-390

The Office of Inspector General (OIG) suggests in the referenced Draft Management Letter that Arkansas' use of Workforce Investment Act (WIA) funding for incumbent worker training was contrary to the WIA statute and regulations. ETA strongly disagrees with the OIG's findings. However, ETA does agree that additional policy guidance is needed as it relates to both incumbent worker training generally and as it relates to the economic development and employer generating activities that are prohibited by WIA. Below are general comments on the flexibility offered under WIA for investment in incumbent worker training and specific comments that speak to the issues identified in the Draft Management Letter.

**General Comments**

It is the position of this Administration that for the workforce investment system to be relevant and successful in promoting a competitive workforce, it must be a strong component of economic development. State and local workforce investment boards must continuously assess where the jobs will be, assess the skills and competencies needed for those jobs, and develop investment strategies that ensure workers have the right skills needed by businesses. This clearly necessitates an ongoing and close connection to economic development efforts within a state or community. This approach is fully aligned with the provisions of the WIA. WIA references are very specific indicators that the authors of the Act fully understood the connection of workforce development to economic development.

One of the stated purposes for the workforce investment system in Subtitle B of WIA – Statewide and Local Workforce Investment Systems is to “enhance the productivity and competitiveness of the Nation.”

Membership on the State Workforce Investment Board, as prescribed in Section 111 of WIA, is business driven and business led, and governors are encouraged to designate state agency officials responsible for economic development as members.

Section 112 (b)(4)(C) provides that states should consider the economic development needs of the state in the development of the state's strategic plan for workforce investment.

At the same time, WIA also provides specific safeguards for use of funding for some economic development activities by restricting their use for business relocation (Section 181(d)) or capitalization of businesses and other activities not directly related to training (Section 181(e)).

Another premise of the WIA is providing states and local areas with maximum flexibility to design a workforce investment system and utilize funding in ways that meet the specific needs of states and local areas. A unique feature of this flexibility is that statewide funds are reserved for governors to use for a wide array of workforce activities, including the implementation of innovative incumbent worker training programs.

In the 21<sup>st</sup> century economy, where innovation and technology are continuously changing the skills needed by almost every business and industry at an ever increasing pace, it is critical to have innovative workforce strategies, including incumbent worker training, that build and secure the economic competitiveness of our businesses and our nation. Through WIA reauthorization, the Administration is proposing enhanced availability of incumbent worker training for this purpose.

#### Specific Comments

- 1. The OIG finds the funds used by Arkansas for incumbent worker training were used for "business start up costs" and as incentive money for the business to locate its plant in Jonesboro, AR, and not training of incumbent workers.**

The OIG raises the issue in this section as to whether the reported incumbent worker training costs were actually spent on training or on economic development activities not directly related to training. Apart from this factual issue, ETA does not agree with the underlying premise of this finding. The OIG's statements would indicate that the costs associated with training in conjunction with a new business as it is ramping up should be considered "business start up costs" and not appropriate for use of WIA funds. There is nothing in the WIA statute that indicates this distinction, and it was not part of the legislative debate when WIA was initially passed. It is ETA's position that in the context of economic development, where a new business is being created or expanded in a community, it is entirely appropriate for WIA funds to be expended for training workers with the skills needed for the new jobs. The section quoted by the OIG from the preamble to the WIA rules very specifically says that incumbent worker training is frequently part of an economic development or business retention strategy.

The OIG indicates that some of the money was used to reimburse salaries of supervisors who conducted the training. There is no statutory or regulatory direction on the components of training costs and no limitation that prevents instructors from being employees of a private sector company. Other provisions under WIA are consistent with an interpretation that it is feasible to reimburse employers for training costs such as utilizing staff as instructors. For example, under the WIA formula programs for adults and dislocated workers, it is possible for private sector companies to be eligible training providers and the costs of training workers that ultimately become their employees may be covered. In addition, the formula funds may also be used for on-the-job training, and employers are reimbursed the extraordinary costs associated with the training.

**2. The OIG finds that Arkansas did not have a policy that defines “incumbent worker” eligibility other than a policy for a separate state training program which would have excluded the use of state funds for training the Nestle workers.**

The determinative issue for use of WIA funds for economic development activities is whether the activities are directly related to training for eligible individuals (20 CFR §667.262). Incumbent worker training is expressly authorized as a statewide activity and neither the WIA statute nor regulations make any distinction regarding the length of employment of participating workers that would suggest that new hires are ineligible for such training.

ETA agrees that the establishment of better state policies on incumbent worker training is desirable and has the potential to lead to better services and more effective administration. However, the failure to establish a specific policy for this program does not render the costs of the training unallowable.

The WIA statute and regulations do not mandate that states have a policy that defines incumbent workers. The regulations at 20 CFR §665.220 indicate that “States **MAY** establish definitions to determine which workers, or groups of workers, are eligible for incumbent workers services . . . [emphasis added].” The fact that Arkansas defined incumbent workers for a separate state-funded training program has no relevance. It is ETA’s position that incumbent workers may be broadly defined to include any employed worker, including recently hired workers.

**3. The OIG recommends ETA issue guidance clarifying the parameters of incumbent worker training under WIA. The OIG suggests the policy include establishing a minimum time frame for employment in order to be considered an “incumbent worker.”**

ETA agrees that clarity is needed regarding incumbent worker training policy and policy guidance was under development prior to the OIG's letter. ETA does not agree with limiting the definition of "incumbent workers." It is the Administration's position that states and local areas should have maximum flexibility in developing their workforce investment strategies to align with the economic needs of their states and communities, including investments in incumbent worker training.

**Summary**

ETA is currently requesting additional information from the state to validate that no WIA funds were spent improperly. ETA will be issuing policies on both incumbent worker training and economic development activities in the near future.