

requirement applies to the designated, non-profit (under section 501(c)(3) of the tax code) arm of a religious organization.

Response: The statutory language clearly gives the beneficiary the right to object to the “religious character of the organization or institution from which the individual receives, or would receive, assistance. * * *.” We believe this gives the client the right to object, even when the services will be delivered without inherently religious activities by the non-profit arm of a faith-based group, so no clarification is necessary for the final rule.

X. Fiscal Accountability

Background

Section 260.34(h) of this rule sets forth the financial responsibility incurred through the receipt of Federal TANF or State MOE funds. Religious organizations that contract to provide TANF services or benefits are subject to the same requirements as other non-governmental organizations to account, in accordance with generally accepted auditing and accounting principles, for the use of such funds. Religious organizations may segregate their TANF accounts from non-governmental funds for other activities. If religious organizations choose to segregate their Federal TANF or State MOE funds in this manner, only the segregated funds are subject to audit by the government.

Comment: Some commenters would like ACF to require that faith-based organizations separate the TANF funds they receive from other funds, and incorporate oversight mechanisms. One of the commenters recommended that we revise the regulation to conform to the standards adopted by the Substance Abuse and Mental Health Services Administration (SAMHSA). Other commenters recommended making the language stronger to stress the importance of creating separate records. One of the commenters wrote that faith-based organizations and government officials need guidance regarding the procedures required to separately fund the activities. Another commenter asked us to maintain the provision that if a religious organization establishes a separate account, then only the TANF funds are subject to audit by the government.

Response: Section 104(h)(2) of PRWORA as amended (42 U.S.C. 604a(h)(2)) gives a religious organization the option of segregating the Federal funds received into a separate account. Therefore, we do not think it is appropriate to require separate accounts because this would be stricter than the

law stipulates. By contrast, the Charitable Choice provision applicable to SAMHSA, at 42 U.S.C. 290kk-1(g)(2), specifically requires that the religious organization program participant segregate the Federal funds provided under award from non-Federal funds.

The religious organizations are responsible for deciding whether to establish separate account(s) to receive and to disburse the funds and for developing their own means of doing so. Organizations that are able and willing to separate the funds received from the State into a separate account will have only those funds subject to audit.

Comment: One commenter asked us to clarify whether only the Federal TANF funds, as opposed to State MOE funds, are subject to audit when religious organizations segregate the funds into a separate account.

Response: The limited audit authority applies to Federal TANF and State MOE funds, whether received directly or indirectly, unless State law expressly prohibits this flexibility from extending to State MOE funds. Both Federal TANF and State MOE funds are subject to the TANF Charitable Choice provisions.

We recognize that the TANF Charitable Choice provision at section 104(h)(2) of PRWORA as amended (42 U.S.C. 604a(h)(2)) refers only to Federal TANF funds. But, the intent of this provision is to enable the organization to opt to limit the scope of fiscal audits. Therefore, we have concluded that extending the option to include State MOE funds is consistent with the statutory intent. We have clarified this point in § 260.34(h).

Comment: Some commenters think that the regulation does not adequately guard against using the funds for religious activities. One commenter asked us to address the accounting and/or separation principles which must be followed with respect to the separate funding of permitted and restricted activities in order to demonstrate that the organization has not expended any government funds on restricted activities. Several of the commenters requested that the final rule require that the religious organization establish a separate corporate structure (e.g., incorporate under 501(c)(3)) or other type of separate structure that would distinguish the religious entity from its government-funded social welfare organization. Another commenter is concerned that the option for religious organizations to commingle funds could make it more difficult and expensive for the State to ensure that public funds are not supporting “inherently religious activities.” This commenter noted that the Community Services Block Grant

program proposed rule does not allow for the commingling of funds by religious organizations.

Response: Under the TANF Charitable Choice statute, religious organizations may, but are not required to, establish a separate account structure, including incorporating or operating the separated part as a non-profit organization under section 501(c)(3) of the Internal Revenue Code. Because religious organizations do not have to incorporate or operate as a non-profit organization, we have deleted the definition of religious organization—i.e., “a non-profit religious organization” from the final regulation.

The final rule provides that religious organizations receiving Federal TANF or State MOE funds will be subject to audit, just like any other non-governmental organization receiving such funds. The State is responsible for the appropriate use of its Federal TANF and State MOE funds, so the organization needs to be able to show to the State and the auditor that it used the funds, whether provided directly or indirectly, for the purpose intended by the State. Specifically, as provided in 45 CFR 92.26, TANF grantees and sub-grantees are responsible for obtaining audits by an independent auditor following generally accepted government auditing standards, in accordance with both the Single Audit Act and OMB Circular A-133. These require that grantees spending more than \$300,000 in Federal funds per year must obtain an annual independent audit, normally conducted by a private firm. This authority is in 31 U.S.C. section 7502(a)(1)(A) and (c). The State or local government must determine whether the grantee and sub-grantees have complied with all laws applicable to expenditures, which includes a determination as to whether the proscription against using direct funding for inherently religious practices has been followed. State officials may want to establish reasonable and prudent procurement policies, building in real and meaningful safeguards to prevent the diversion of funds to any ineligible purpose.

Moreover, HHS is authorized to conduct any additional audits or reviews that are warranted, irrespective of the amount of Federal funds expended by the grantee annually, in order to ensure compliance with program requirements including the restriction against direct funding of inherently religious activities. This authority is in 45 CFR 92.40(e). HHS may determine that such audits or reviews are warranted based upon any