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RECOVERY ACT

Clean Water Projects Are Underway, but Procedures May Not Be in Place to Ensure Adequate Oversight

Statement of David C. Trimble, Acting Director
Natural Resources and Environment



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Highlights of [GAO-10-761T](#), testimony before the Committee on Transportation and Infrastructure, House of Representatives

Why GAO Did This Study

The American Recovery and Reinvestment Act of 2009 (Recovery Act) included \$4 billion for the Environmental Protection Agency's (EPA) Clean Water State Revolving Fund (SRF). This testimony—based on GAO's report GAO-10-604, issued on May 26, 2010, in response to a mandate under the Recovery Act—addresses (1) state efforts to meet requirements associated with the Recovery Act and SRF program, (2) the uses of Recovery Act funds, and (3) EPA's and states' efforts to oversee the use of these funds.

GAO's review of the Clean Water SRF program focused on 14 states and selected localities—known as subrecipients—in each of these states. These 14 states received approximately 50 percent of the total appropriated under the Recovery Act for the Clean Water SRF. GAO obtained data from EPA and the 14 states, including the amounts and types of financial assistance each SRF program provided, which subrecipients were first-time recipients of Clean Water SRF funding, and which projects serve disadvantaged communities.

What GAO Recommends

GAO-10-604 recommended that the EPA Administrator work with the states to implement specific oversight procedures to monitor and ensure subrecipients' compliance with the provisions of the Recovery Act-funded Clean Water SRF program. EPA neither agreed nor disagreed with our recommendation.

View [GAO-10-761T](#) or [key components](#). For more information, contact David C. Trimble at (202) 512-3841 or trimbled@gao.gov.

RECOVERY ACT

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What GAO Found

The 14 states we reviewed for the Clean Water SRF program had all projects under contract by the 1-year, February 17, 2010, deadline and also took steps to give priority to projects that were ready to proceed to construction by that same date. Eighty-seven percent of Clean Water SRF projects were under construction within 12 months of enactment of the Recovery Act. In addition, the 14 Clean Water SRFs exceeded the 20 percent green reserve requirement, using 29 percent of SRF funds to provide assistance for projects that met EPA criteria for being “green,” such as water or energy efficiency projects; these states also met or exceeded the requirement to use at least 50 percent of Recovery Act funds to provide additional subsidization in the form of, for example, principal forgiveness or grants. SRF officials in most of the states we reviewed said that they faced challenges in meeting Recovery Act requirements, including the increased number of applications needing review and the number of new subrecipients requiring additional support in complying with the SRF program and Recovery Act requirements. States used a variety of techniques to address these concerns to meet the 1-year deadline, such as hiring additional staff to help administer the SRF program.

The 14 states we reviewed distributed nearly \$2 billion in Recovery Act funds among 890 water projects through their Clean Water SRF program. Overall, these 14 states distributed about 79 percent of their funds as additional subsidization, with most of the remaining funds provided as low- or zero-interest loans that will recycle back into the programs as subrecipients repay their loans. In addition, states we reviewed used at least 40 percent of Clean Water SRF Recovery Act project funds (\$787 million) to provide assistance for projects that serve disadvantaged communities, and almost all of this funding was provided in the form of additional subsidization. Almost half of the Clean Water SRF subrecipients had never previously received assistance through that program. Of the 890 projects awarded Recovery Act Clean Water SRF program funds in these states, more than one-third are for green projects, and almost all of these (93 percent) were awarded additional subsidization.

EPA has modified its existing oversight of state SRF programs by planning additional performance reviews beyond the annual reviews it already conducts, but these reviews do not include an examination of state subrecipient monitoring procedures. According to EPA officials, EPA has not established new subrecipient monitoring requirements for Recovery Act-funded projects and has given states a high degree of flexibility to operate their SRF programs based on each state's unique needs. Although many states have expanded their existing monitoring procedures, the oversight procedures in some states may not be sufficient given that (1) federal funds awarded to each state under the Recovery Act have increased as compared with average annual awards; (2) all Recovery Act projects had to be under contract within 1 year; and (3) EPA and states had little experience with some new Recovery Act requirements, such as the Buy American requirements. For example, some projects have been completed before any site inspection has occurred.

Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss our work examining selected states' use of funds made available for clean water projects under the American Recovery and Reinvestment Act of 2009 (Recovery Act).¹ Congress and the administration have fashioned a significant response to what is generally considered to be the nation's most serious economic crisis since the Great Depression. The Recovery Act's combined spending and tax provisions are estimated to cost \$787 billion, including \$4 billion for the Environmental Protection Agency's (EPA) Clean Water State Revolving Fund (SRF). The Recovery Act specified several roles for us, including conducting ongoing reviews of selected states' and localities' use of funds made available under the act. We recently completed our sixth review, being issued today, which examined a core group of 16 states, the District of Columbia, and selected localities.² One component of this review focused on the Clean Water SRF program in 14 of those states and selected localities—known as subrecipients—in each of these states.³ These 14 states received approximately 50 percent of the total amount appropriated for the Clean Water SRF.

My statement today is based on this work as it relates to the Clean Water SRF program's use of Recovery Act funds and addresses (1) state efforts to meet requirements associated with the Recovery Act, (2) the uses of Recovery Act funds, and (3) EPA's and states' efforts to oversee the use of these funds. We obtained data from EPA's Clean Water SRF Benefits Reporting system as well as each of the 14 states in our review, including the amounts and types of financial assistance that each SRF program provided using Recovery Act funds, the type of Clean Water SRF projects funded, the contract completion and construction start dates for these projects, which subrecipients were first-time recipients of the Clean Water SRF program, and which projects serve disadvantaged communities. We also reviewed relevant regulations and federal guidance and interviewed EPA officials that administer the programs in headquarters and 4 of the 10

¹Pub. L. No. 111-5, 123 Stat. 115 (Feb. 17, 2009).

²GAO, Recovery Act: States' and Localities' Uses of Funds and Actions Needed to Address Implementation Challenges and Bolster Accountability, [GAO-10-604](#) (Washington, D.C.: May 26, 2010). For related state appendixes, see [GAO-10-605SP](#).

³The 14 states we reviewed are Arizona, California, Colorado, Florida, Georgia, Iowa, Massachusetts, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, and Texas.

EPA regions.⁴ In addition, we conducted semistructured interviews with state officials who administer the SRF programs and with subrecipients who received Recovery Act funds. We conducted performance audits for this review from November 2009 to May 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

The Recovery Act appropriated \$4 billion for the Clean Water SRF program.⁵ This funding represents a significant increase compared with federal funds awarded as annual appropriations to the SRF program in recent years. From fiscal years 2000 through 2009, annual appropriations averaged about \$1.1 billion for the Clean Water SRF program. Established in 1987, EPA's Clean Water SRF program provides states and local communities independent and permanent sources of subsidized financial assistance, such as low- or no-interest loans for projects that protect or improve water quality and that are needed to comply with federal water quality regulations.

In addition to providing increased funds, the Recovery Act included some new requirements for the SRF programs. For example, states were required to have all Recovery Act funds awarded to projects under contract within 1-year of enactment—which was February 17, 2010⁶—and

⁴We interviewed officials in EPA Region 3 (Philadelphia), Region 6 (Dallas), Region 8 (Denver), and Region 9 (San Francisco).

⁵EPA allocates clean water funds to the states based on a statutory formula. The \$4 billion in Recovery Act funds includes about \$39 million in Clean Water Act (CWA) Section 604(b) Water Quality Management Planning Grants. Section 604(b) of the CWA requires the reservation each fiscal year of a small portion of each state's Clean Water SRF allotment - usually 1 percent - to carry out planning under Sections 205(j) and 303(e) of the CWA. States generally use 604(b) grants to fund regional comprehensive water quality management planning activities to improve local water quality. In this testimony, any reference to Recovery Act funds excludes these planning grants.

⁶In this report we use the word "project" to mean an assistance agreement, i.e., a loan or grant agreement made by the state SRF program to a subrecipient for the purpose of a Recovery Act project.

EPA was directed to reallocate any funds not under contract by that date.⁷ In addition, under the Recovery Act, states should give priority to projects that were ready to proceed to construction within 12 months of enactment. States were also required to use at least 20 percent of funds as a “green reserve” to provide assistance for green infrastructure projects, water or energy efficiency improvements, or other environmentally innovative activities. Further, states were required to use at least 50 percent of Recovery Act funds to provide assistance in the form of, for example, principal forgiveness or grants. These types of assistance are referred to as additional subsidization and are more generous than the low- or no-interest loans that the Clean Water SRF programs generally provide.

Despite Challenges, States Met Recovery Act Requirements for the SRFs

The 14 states we reviewed for the Clean Water SRF program met all Recovery Act requirements specific to the Clean Water SRF. Specifically, the states we reviewed had all projects under contract by the 1-year deadline and also took steps to give priority to projects that were ready to proceed to construction within 12 months of enactment of the Recovery Act. Eighty-seven percent of Clean Water SRF projects were under construction within 12 months of enactment. In addition, the 14 Clean Water SRFs we reviewed exceeded the 20 percent green reserve requirement, using 29 percent of Recovery Act SRF funds in these states to provide assistance for projects that met EPA criteria for the green reserve. These states also met or exceeded the 50 percent additional subsidization requirement; overall, the 14 states distributed a total of 79 percent of Recovery Act Clean Water SRF funds as additional subsidization.

SRF officials in most of the states we reviewed said that they faced challenges in meeting Recovery Act requirements, especially the 1-year contracting deadline. Under the base program, it could take up to several years from when funds are awarded before the loan agreement is signed, according to EPA officials. Some SRF officials told us that the compressed time frame imposed by the Recovery Act posed challenges and that their

⁷The Recovery Act requires states to have all funds awarded to projects “under contract or construction” by the 1-year deadline. EPA interprets this as requiring states to have all projects under contract in an amount equal to the full value of the Recovery Act assistance agreement by the deadline, regardless of whether construction has begun, according to a September 2009 memorandum. Thus, in this report, we use “under contract” when referring to this requirement. Further, according to EPA’s March 2, 2009, memorandum, the agency will deobligate any Recovery Act SRF funds that a state does not have awarded to projects under contract by the 1-year deadline and reallocate them to other states.

workloads increased significantly as a result of the 1-year deadline. Among the factors affecting workload are the following:

- *Reviewing applications for Recovery Act funds was burdensome.* Officials in some states said that the number of applications increased significantly, in some cases more than doubling compared with prior years, and that reviewing these applications was a challenge. For example, New Jersey received twice as many applications than in past years, according to SRF officials in that state.
- *Explaining new Recovery Act requirements was time-consuming.* Because projects that receive any Recovery Act funds must comply with Buy American requirements and Davis-Bacon wage requirements,⁸ state SRF officials had to take additional steps to ensure that both applicants for Recovery Act funds and those awarded Recovery Act funds understood these requirements.
- *Applicants and subrecipients required additional support.* Many states took steps to target Recovery Act funds to new recipients, including nontraditional recipients of Clean Water SRF funds, such as disadvantaged communities.⁹ According to SRF officials in some states, new applicants and subrecipients required additional support in complying with SRF program and Recovery Act requirements. In the states we reviewed, nearly half of Clean Water SRF subrecipients had not previously received assistance through that program.
- *Project costs were difficult to predict.* Officials in some states told us that actual costs were lower than estimated for many projects awarded Recovery Act funds and, as a result, some states had to scramble to ensure that all Recovery Act funds were under contract by the 1-year deadline. For example, in January 2010, officials from Florida's SRF programs told us that a few contracts for Recovery Act-funded projects in the state had

⁸The Buy American provisions of the Recovery Act generally require that iron, steel, and manufactured goods acquired for use on a public building or public work be produced in the United States, subject to limited exceptions. The Davis-Bacon provisions of the Recovery Act require that contractors and subcontractors pay all laborers and mechanics working on Recovery Act projects at least the prevailing wage rates in the local area where they are employed, as determined by the Secretary of Labor.

⁹States differ in how they define disadvantaged communities. In general, disadvantaged community status takes into account factors such as median household income and community size. At least one state included in this report determines disadvantaged community status at the county level. Some states have introduced efforts to provide base SRF funds to disadvantaged communities, while others have not.

come in below their original project cost estimates, and that this was likely to be the program staff’s largest concern as the deadline approached. However, lower estimates also allowed some states to undertake additional projects that they would otherwise have been unable to fund with the Recovery Act funding.

States used a variety of techniques to address these workload concerns and meet the 1-year contracting deadline, according to state SRF officials with whom we spoke. Some states hired additional staff to help administer the SRF programs, although SRF officials in other states told us that they were unable to do so because of resource constraints. For example, New Jersey hired contractors to help administer the state’s base Clean Water SRF funds, allowing experienced staff to focus on meeting Recovery Act requirements, according to SRF officials in that state. Moreover, some states hired contractors to provide assistance to both applicants and subrecipients. For example, California hired contractors—including the Rural Community Assistance Corporation—to help communities apply for Recovery Act funds. Furthermore, states took steps to ensure that they would have all Recovery Act funds under contract even if projects dropped out because of Recovery Act requirements or time frames. For example, most of the states we reviewed awarded a combination of Recovery Act and base funds to projects to allow for more flexibility in shifting Recovery Act funds among projects.

States also used a variety of techniques to ensure that they would meet the green reserve requirement. For example, some of the states we reviewed conducted outreach to communities and nonprofit organizations to solicit applications for green projects. Moreover, to make green projects more attractive to communities, some states offered additional subsidization to all green projects or relied on a small number of high-cost green projects to meet the requirement. For example, Mississippi officials told us that the state funded three large energy efficiency projects that helped the state’s Clean Water SRF program meet the green reserve requirement.

Recovery Act Funds Went to Many Disadvantaged Communities and New Recipients

The 14 states we reviewed distributed nearly \$2 billion in Recovery Act funds among 890 water projects through their Clean Water SRF program. These states took a variety of approaches to distributing funds. For example, four states distributed at least 95 percent of Recovery Act funds as additional subsidization, while three other states distributed only 50 percent as additional subsidization, the smallest amount permitted under the Recovery Act. Overall, these 14 states distributed approximately 79 percent of Clean Water SRF Recovery Act funds as additional

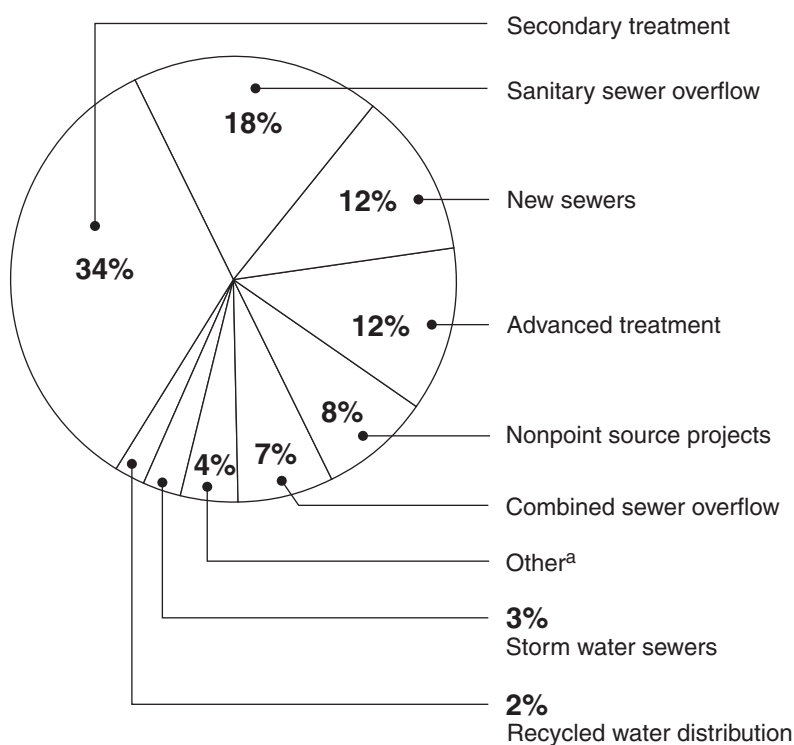
subsidization, with most of the remaining funds provided as low- or no-interest loans that will recycle back into the programs as subrecipients repay their loans. As the funds are repaid, they can then be used to provide assistance to SRF recipients in the future. Furthermore, states varied in the number of projects they chose to fund. For example, Ohio distributed approximately \$221 million among 274 Clean Water SRF projects, while Texas distributed more than \$172 million among 21 projects. Some states funded more projects than originally anticipated because other projects were less costly than expected, according to officials. For example, Texas was able to provide funds for two additional clean water projects because costs—especially material costs—were lower than anticipated for other projects.

States we reviewed used at least 40 percent of Recovery Act Clean Water SRF project funds (\$787 million) to provide assistance for projects that serve disadvantaged communities.¹⁰ Most of the states we reviewed took steps to target some or all Recovery Act funds to these low-income communities, generally by considering a community's median household income when selecting projects and determining which projects would receive additional subsidization in the form of principal forgiveness, negative interest loans, or grants. According to state officials from nine Clean Water SRF programs, 50 percent of all projects funded by those states' SRF programs serve disadvantaged communities, and all of these disadvantaged communities were provided with additional subsidization. SRF officials in some states told us that Recovery Act funds—especially in the form of additional subsidization—have provided significant benefits to disadvantaged communities in their states. For example, according to officials from California's Clean Water SRF program, that state used funds to provide assistance for 25 wastewater projects that serve disadvantaged communities, and approximately half of these projects would not have gone forward as quickly or at all without additional subsidization. Officials from the City of Fresno confirmed that one of these projects—which will replace septic systems with connections to the city's sewer systems in two disadvantaged communities—would not have gone forward without additional subsidization. Local officials told us that this project will decrease the amount of nitrates in the region's groundwater, which is the source of the city's drinking water.

¹⁰Because three states do not maintain information on which projects serve disadvantaged communities and two additional states maintain only limited information on which projects serve disadvantaged communities, we cannot provide complete information on the number of projects serving these communities.

The Clean Water SRF programs from the 14 states we reviewed used Recovery Act funds to provide assistance for 890 projects that will meet a variety of local needs. Figure 1 shows how the 14 states distributed Recovery Act funds across various clean water categories.

Figure 1: Share of Recovery Act Funds Provided to Clean Water SRF Projects in 14 States, by Category



Source: GAO analysis of EPA data and information provided by states.

^aThree states—California, Massachusetts, and Texas—reported awarding Recovery Act funds to other types of Clean Water SRF projects or project components. These projects include, for example, expanding a disposal system, constructing a reclaimed water delivery system, and constructing a wind turbine.

In the states we reviewed, the Clean Water SRF programs used more than 70 percent of Recovery Act project funds to provide assistance for projects in the following categories:

- *Secondary treatment and advanced treatment.* States we reviewed used nearly half of all Recovery Act project funds to support wastewater infrastructure intended to meet or exceed EPA’s secondary treatment standards for wastewater treatment facilities. Projects intended to achieve compliance with these standards are referred to as secondary treatment

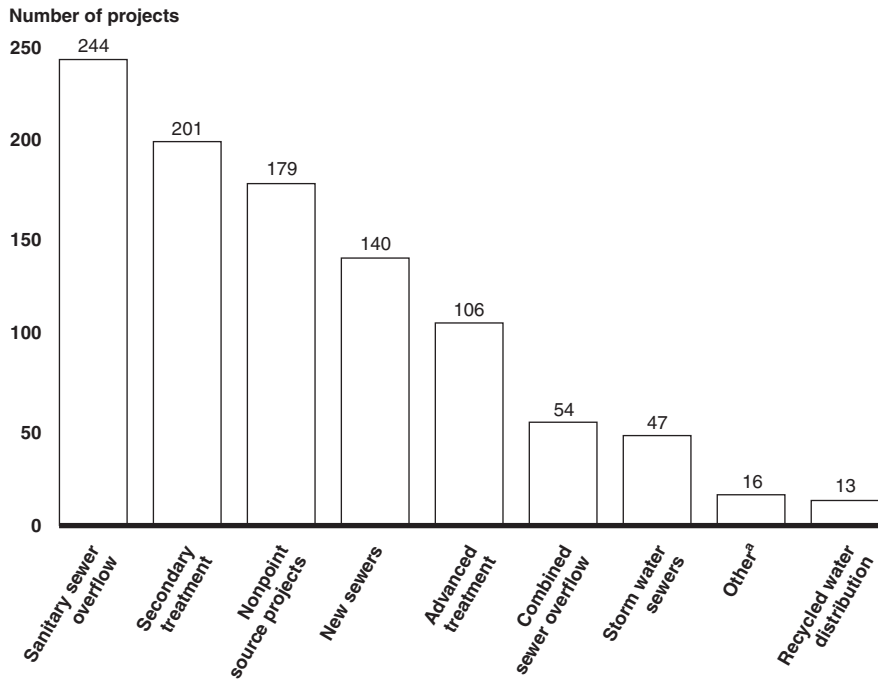
projects, while projects intended to exceed compliance with these standards are referred to as advanced treatment projects. For example, Massachusetts' Clean Water SRF program awarded over \$2 million in Recovery Act funds to provide upgrades intended to help the City of Leominster's secondary wastewater treatment facility achieve compliance with EPA's discharge limits for phosphorous.

- *Sanitary sewer overflow and combined sewer overflow.* States we reviewed used about 25 percent of Recovery Act project funds to support efforts to prevent or mitigate discharges of untreated wastewater into nearby water bodies. Such sewer overflows, which can occur as a result of inclement weather, can pose significant public health and pollution problems, according to EPA. For example, Pennsylvania used 56 percent of project funds to address sewer overflows from municipal sanitary sewer systems and combined sewer systems.¹¹ In another example, Iowa's Clean Water SRF program used Recovery Act funds to help the City of Garwin implement sanitary sewer improvements. Officials from that city told us that during heavy rains, untreated water has bypassed the city's pump station and backed up into basements of homes and businesses, and that the city expects all backups to be eliminated as a result of planned improvements.

In addition to funding conventional wastewater treatment projects, 9 of the 14 Clean Water SRF programs we reviewed used Recovery Act funds to provide assistance for projects intended to address nonpoint source pollution—projects intended to protect or improve water quality by, for example, controlling runoff from city streets and agricultural areas. The Clean Water SRF programs we reviewed used 8 percent of project funds to support these nonpoint source projects, but nonpoint source projects account for 20 percent (179 out of 890) of all projects. A large number of these projects—131 out of 179—were initiated by California or Ohio. For example, California used Recovery Act funds to provide assistance for the Tomales Bay Wetland Restoration and Monitoring Program, which restores wetlands that had been converted into a dairy farm. Figure 2 shows the number of projects that fall into various clean water categories.

¹¹Combined sewer systems are designed to collect rainwater runoff, domestic sewage, and industrial wastewater in the same pipe.

Figure 2: Clean Water SRF Projects Awarded Recovery Act Funds in 14 States, by Category



Source: GAO analysis of EPA data and information provided by states.

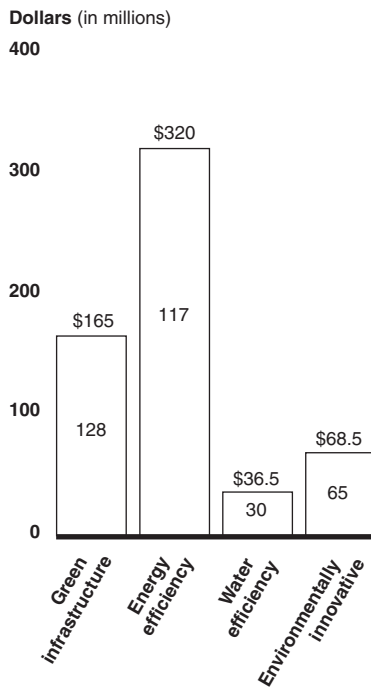
Note: Some projects fall into more than one category.

^aThree states—California, Massachusetts, and Texas—reported awarding Recovery Act funds to other types of Clean Water SRF projects or project components. These projects include, for example, expanding a disposal system, constructing a reclaimed water delivery system, and constructing a wind turbine.

Of the 890 projects awarded Recovery Act funds by the Clean Water SRF programs in the states we reviewed, more than one-third (312) address the green reserve requirement. Of these green projects, 289 (93 percent) were awarded additional subsidization. Figure 3 shows the number of projects that fall into each of the four green reserve categories included in the Recovery Act. Many of these projects are intended to improve energy efficiency and are expected to result in long-term cost savings for some communities as a result of these improvements. For example, the Massachusetts Water Resources Authority is using Recovery Act funds provided through that state’s Clean Water SRF program to help construct a wind turbine at the DeLauri Pump Station, and the Authority estimates that, as a result of this wind turbine, more than \$350,000 each year in electricity purchases will be avoided. Furthermore, some projects provide green alternatives for infrastructure improvements. For example, New

York's Clean Water SRF program provided Recovery Act funds to help construct a park designed to naturally filter stormwater runoff and reduce the amount of stormwater that enters New York City's sewers. More than half of the city's sewers are combined sewers, and during heavy rains, sewage sometimes discharges into Paerdatag Basin, which feeds into Jamaica Bay.

Figure 3: Green Reserve Projects Awarded Recovery Act Clean Water SRF Program Funds in 14 States, by Category



Source: GAO analysis of EPA data and information provided by states.

Note: Some projects fall into more than one category.

Although EPA and States Have Expanded Existing Oversight Procedures to Address Recovery Act Requirements, the Procedures May Not Ensure Adequate Oversight

EPA has modified its existing oversight of state SRF programs by planning additional performance reviews beyond the annual reviews it is already conducting, but these reviews do not include an examination of state subrecipient monitoring procedures. Specifically, EPA is conducting midyear and end-of-year Recovery Act reviews in fiscal year 2010 to assess how each state is meeting Recovery Act requirements. As part of these reviews, EPA has modified its annual review checklist to incorporate elements that address the Recovery Act requirements. Further, EPA officials will review four project files in each state for compliance with Recovery Act requirements and four federal disbursements to the state to help ensure erroneous payments are not occurring. According to EPA officials, through these added reviews, EPA is providing additional scrutiny over how states are using the Recovery Act funds and meeting Recovery Act requirements as compared with base program funds. As of May 14, 2010, EPA completed field work for its mid-year Recovery Act reviews in 13 of the states we reviewed and completed final reports for 3 of these states (Iowa, Ohio, and Pennsylvania). EPA has plans to begin field work in the final state at the end of May 2010.

Although the frequency of reviews has increased, these reviews do not examine state subrecipient monitoring procedures. In 2008, the EPA Office of Inspector General (OIG) examined state SRF programs' compliance with subrecipient monitoring requirements of the Single Audit Act and found that states complied with the subrecipient monitoring requirements but that EPA's annual review process did not address state subrecipient monitoring procedures. The OIG suggested that EPA include a review of how states monitor borrowers as part of its annual review procedures. EPA officials told us that they agreed with the idea to include a review of subrecipient monitoring procedures as part of the annual review but have not had time to implement this suggestion because EPA's SRF program officials have focused most of their attention on the Recovery Act since the OIG published its report. EPA officials also told us that they believe the reviews of project files and federal disbursements could possibly identify internal control weaknesses that may exist for financial controls, such as weaknesses in subrecipient monitoring procedures. These reviews occur as part of the Recovery Act review and aim to assess a project's compliance with Recovery Act requirements and help ensure that no erroneous payments are occurring.

In terms of state oversight of subrecipients, EPA has not established new subrecipient monitoring requirements for Recovery Act-funded projects, according to EPA officials. Under the base Clean Water SRF program, EPA gives states a high degree of flexibility to operate their SRF programs

based on each state's unique needs and circumstances in accordance with federal and state laws and requirements. According to EPA officials, although EPA has established minimum requirements for subrecipient monitoring, such as requiring states to review reimbursement requests, states are allowed to determine their own subrecipient monitoring procedures, including the frequency of project site inspections.

While EPA has not deviated from this approach with regard to monitoring Recovery Act-funded projects, it has provided states with voluntary tools and guidance to help with monitoring efforts. For example, EPA provided states with an optional inspection checklist to help states evaluate a subrecipient's compliance with Recovery Act requirements, such as the Buy American and job reporting requirements. EPA has also provided training for states on the Recovery Act requirements. For example, as of May 14, 2010, EPA has made available 11 on-line training sessions (i.e. webcasts) for state officials in all states to help them understand the Recovery Act requirements. EPA has also provided four workshops with on-site training on its inspection checklist for state officials in California, Louisiana, New Mexico, and Puerto Rico.

Although EPA has not required that states change their subrecipient oversight approach, many states have expanded their existing monitoring procedures in a variety of ways. However, the oversight procedures may not be sufficient given that (1) federal funds awarded to each state under the Recovery Act have increased as compared with average annually awarded amounts; (2) all Recovery Act projects had to be ready to proceed to construction more quickly than projects funded with base SRF funds; and (3) EPA and states had little previous experience with some of the Recovery Act's new requirements, such as Buy American provisions, according to EPA officials. The following are ways in which oversight procedures may not be sufficient:

- *Review procedures for job data.* According to OMB guidance on Recovery Act reporting, states should establish internal controls to ensure data quality, completeness, accuracy, and timely reporting of all amounts funded by the Recovery Act. We found that most states we reviewed had not developed review procedures to verify the accuracy of job figures reported by subrecipients using supporting documentation, such as certified payroll records. As a result, states may be unable to verify the accuracy of these figures. For example, Mississippi SRF officials told us that they do not have the resources to validate the job counts reported by comparing them against certified payroll records. In addition, during interviews with some subrecipients, we found inconsistencies among

subrecipients on the types of hours that should be included and the extent that they verified job data submitted to them by contractors. For example, in New Jersey one subrecipient told us they included hours worked by the project engineer in the job counts, while another subrecipient did not.

- *Review procedures for loan disbursements.* According to EPA officials, the agency requires states to verify that all loan payments and construction reimbursements are for eligible program costs. In addition, according to EPA guidance, states often involve technical staff who are directly involved in construction inspections to help verify disbursement requests because they have additional information, such as the status of construction, that can help accurately approve these requests. However, we found that in two states we reviewed, technical or engineering staff did not review documentation supporting reimbursement requests from the subrecipient to ensure they were for legitimate project costs. For example, officials in Pennsylvania told us that technical staff from the state's Department of Environmental Protection—which provides technical assistance to SRF subrecipients—do not verify monthly payments to subrecipients that are made by the Pennsylvania Infrastructure Investment Authority, the state agency with funds management responsibility for the state's SRF programs. Instead, Department of Environmental Protection staff approve project cost estimates prior to loan settlement, when they review bid proposals submitted by contractors, and Pennsylvania Infrastructure Investment Authority officials verify monthly payments against the approved cost estimates.
- *Inspection procedures.* According to EPA officials, the agency requires that SRF programs have procedures to help ensure subrecipients are using Recovery Act SRF funding for eligible purposes. While EPA has not established required procedures for state project inspections, it has provided states its optional Recovery Act inspection checklist to help them evaluate a subrecipient's compliance with Recovery Act requirements, such as the Buy American and job reporting requirements. Some states we reviewed have adopted EPA's Recovery Act inspection checklist procedures and modified their procedures accordingly. For example, California and Arizona plan to implement all elements of EPA's checklist for conducting inspections of Recovery Act projects, according to officials in these states. Other states have modified their existing inspection procedures to account for the new Recovery Act requirements. For example, officials from Georgia said they added visual examination of purchased materials and file review steps to their monthly inspections to verify that subrecipients are complying with the Buy American provision. In contrast, the Pennsylvania Department of Environmental Protection's inspection procedures do not include a review of Recovery Act

requirements. For example, we found that inspection reports for three Recovery Act projects we visited in Pennsylvania do not include inspection elements that covered Davis-Bacon or Buy American provisions. Instead, the Pennsylvania Infrastructure Investment Authority requires subrecipients to self-certify their compliance with these Recovery Act requirements when requesting payment from the state's funds disbursement system. Registered professional engineers who work for the subrecipients must sign off on these self-certifications and subrecipients could face loss of funds if a certification is subsequently found to be false, according to the Executive Director of the Authority.

- *Frequency and timing of inspections.* According to EPA officials, the agency does not have requirements on how often a state SRF program must complete project inspections, and the frequency and complexity of inspections vary by state for the base SRF program. Officials from several states told us they have increased the frequency of project site inspections. For example, Colorado SRF officials said the state is conducting quarterly project site inspections of each of the state's Recovery Act funded SRF projects, whereas under the state's base SRF programs, Colorado inspects project sites during construction only when the state has concerns. However, we found that two states either did not conduct site inspections of some projects that are complete or had not yet inspected projects that were near completion. For example, as of April 19, 2010, Ohio EPA had inspected about 41 percent of its Clean Water SRF projects, but our review of Ohio's inspection records showed that at least 6 projects are complete and have not been inspected, and a number of others are nearing completion and have not been inspected.
- *Monitoring compliance with Recovery Act requirements.* We found issues in several states during interviews with SRF subrecipients that suggest uncertainty about subrecipients' compliance with Recovery Act requirements. For example, we interviewed one subrecipient in Ohio whose documentation of Buy American compliance raised questions as to whether all of the manufactured goods used in its project were produced domestically. In particular, the specificity and detail of the documentation provided about one of the products used left questions as to whether it was produced at one of the manufacturer's nondomestic locations. Further, another subrecipient in Ohio was almost 2 months late in conducting interviews of contractor employees to ensure payment of Davis-Bacon wages.

In summary, EPA and the states successfully met the Recovery Act deadlines for having all projects under contract by the 1-year deadline, and almost all Clean Water SRF projects were under construction by that date

as well. Furthermore, Recovery Act funds were distributed to many new recipients and supported projects that serve disadvantaged communities. In addition, Recovery Act Clean Water SRF program funds have supported a variety of projects that are expected to provide tangible benefits to improving local water quality. However, as demonstrated in the above examples, the oversight mechanisms used by EPA and the states may not be sufficient to ensure compliance with all Recovery Act requirements. The combination of a large increase in program funding, compressed time frames, and new Recovery Act requirements present a significant challenge to EPA's current oversight approach. As a result, we recommended that the EPA Administrator work with the states to implement specific oversight procedures to monitor and ensure subrecipients' compliance with the provisions of the Recovery Act-funded Clean Water and Drinking Water SRF programs. EPA neither agreed nor disagreed with this recommendation.

Mr. Chairman, this concludes my prepared statement. I would be pleased to respond to any questions that you or other Members of the Committee might have.

GAO Contact and Staff Acknowledgments

For further information regarding this statement, please contact David C. Trimble at (202) 512-3841 or trimbled@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals who made key contributions to this statement include Nancy Crothers, Elizabeth Erdmann, Brian M. Friedman, Gary C. Guggolz, Emily Hanawalt, Carol Kolarik, and Jonathan Kucskar.

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