July 2009

RECOVERY ACT

States' and Localities' Current and Planned Uses of Funds While Facing Fiscal Stresses

GAO Highlights

Accountability•Integrity•Reliability

Highlights of GAO-09-829, a report to the Senate and House Committees on Appropriations, Senate Committee on Homeland Security and Governmental Affairs, and House Committee on Oversight and Government Reform

Why GAO Did This Study

This report, the second in response to a mandate under the American Recovery and Reinvestment Act of 2009 (Recovery Act), addresses the following objectives: (1) selected states' and localities' uses of Recovery Act funds, (2) the approaches taken by the selected states and localities to ensure accountability for Recovery Act funds, and (3) states' plans to evaluate the impact of the Recovery Act funds they received. GAO's work for this report is focused on 16 states and certain localities in those jurisdictions as well as the District of Columbia—representing about 65 percent of the U.S. population and two-thirds of the intergovernmental federal assistance available. GAO collected documents and interviewed state and local officials. GAO analyzed federal agency guidance and spoke with Office of Management and Budget (OMB) officials and with relevant program officials at the Centers for Medicare and Medicaid Services (CMS), and the U.S. Departments of Education, Energy, Housing and Urban Development (HUD), Justice, Labor, and Transportation (DOT).

What GAO Recommends

GAO makes recommendations and a matter for congressional consideration discussed on the next page. The report draft was discussed with federal and state officials who generally agreed with its contents. OMB officials generally agreed with GAO's recommendations to OMB; DOT agreed to consider GAO's recommendation.

View GAO-09-829 or key components.
For state summaries, see GAO-09-830SP.
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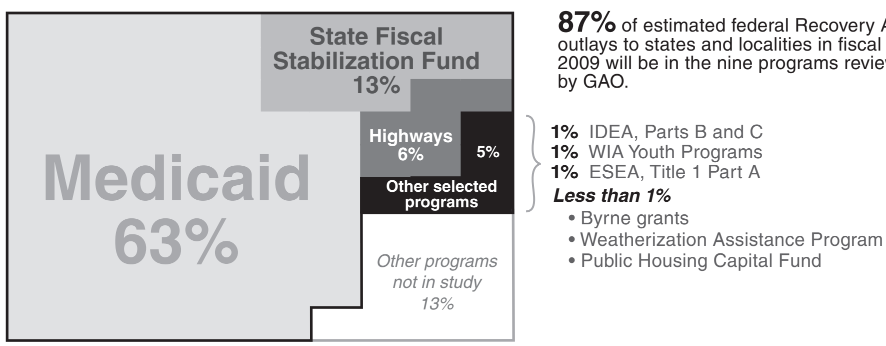
What GAO Found

Across the United States, as of June 19, 2009, Treasury had outlayed about $29 billion of the estimated $49 billion in Recovery Act funds projected for use in states and localities in fiscal year 2009. More than 90 percent of the $29 billion in federal outlays has been provided through the increased Medicaid Federal Medical Assistance Percentage (FMAP) and the State Fiscal Stabilization Fund (SFSF) administered by the Department of Education.

GAO's work focused on nine federal programs that are estimated to account for approximately 87 percent of federal Recovery Act outlays in fiscal year 2009 for programs administered by states and localities. The following figure shows the distribution by program of anticipated federal Recovery Act spending in fiscal year 2009 for the nine programs discussed in this report.



Source: GAO analysis of Congressional Budget Office and Federal Funds Information for States data.

<u>Increased Medicaid FMAP Funding</u>

All 16 states and the District have drawn down increased Medicaid FMAP grant awards of just over $15 billion for October 1, 2008, through June 29, 2009, which amounted to almost 86 percent of funds available. Medicaid enrollment increased for most of the selected states and the District, and several states noted that the increased FMAP funds were critical in their efforts to maintain coverage at current levels. States and the District reported they are planning to use the increased federal funds to cover their increased Medicaid caseload and to maintain current benefits and eligibility levels. Due to the increased federal share of Medicaid funding, most state officials also said they would use freed-up state funds to help cope with fiscal stresses.

<u>Highway Infrastructure Investment</u>

As of June 25, DOT had obligated about $9.2 billion for almost 2,600 highway infrastructure and other eligible projects in the 16 states and the District and had reimbursed about $96.4 million. Across the nation, almost half of the obligations have been for pavement improvement projects because they did not require extensive environmental clearances, were quick to design, obligate and bid on, could employ people quickly, and could be completed within 3 years. Officials from most states considered project readiness, including the 3-year completion requirement, when making project selections and only later identified to what extent these projects fulfilled the economically distressed area (EDA) requirement. We found substantial variation in how states identified areas in economically distressed areas and how they prioritized project selection for these areas.

State Fiscal Stabilization Fund
As of June 30, 2009, of the 16 states and the District, only Texas had not submitted an SFSF application. Pennsylvania recently submitted an application but had not yet received funding. The remaining 14 states and the District had been awarded a total of about $17 billion in initial funding from Education—of which about $4.3 billion has been drawn down. School districts said that they would use SFSF funds to maintain current levels of education funding, particularly for retaining staff and current education programs. They also said that SFSF funds would help offset state budget cuts.

Overall, states reported using Recovery Act funds to stabilize state budgets and to cope with fiscal stresses. The funds helped them maintain staffing for existing programs and minimize or avoid tax increases as well as reductions in services.

Accountability
States have implemented various internal control programs; however, federal Single Audit guidance and reporting does not fully address Recovery Act risk. The Single Audit reporting deadline is too late to provide audit results in time for the audited entity to take action on deficiencies noted in Recovery Act programs. Moreover, current guidance does not achieve the level of accountability needed to effectively respond to Recovery Act risks. Finally, state auditors need additional flexibility and funding to undertake the added Single Audit responsibilities under the Recovery Act.

Impact
Direct recipients of Recovery Act funds, including states and localities, are expected to report quarterly on a number of measures, including the use of funds and estimates of the number of jobs created and the number of jobs retained. The first of these reports is due in October 2009. OMB—in consultation with a broad range of stakeholders—issued additional implementing guidance for recipient reporting on June 22, 2009, that clarifies some requirements and establishes a central reporting framework.

In addition to employment-related reporting, OMB requires reporting on the use of funds by recipients and nonfederal subrecipients receiving Recovery Act funds. The tracking of funds is consistent with the Federal Funding Accountability and Transparency Act (FFATA). Like the Recovery Act, FFATA requires a publicly available Web site—www.USAspending.gov—to report financial information about entities awarded federal funds. Yet, significant questions have been raised about the reliability of the data on www.USAspending.gov, primarily because what is reported by the prime recipients is dependent on the unknown data quality and reporting capabilities of subrecipients.

GAO's Recommendations

Accountability and Transparency
To leverage Single Audits as an effective oversight tool for Recovery Act programs, the Director of OMB should

- develop requirements for reporting on internal controls during 2009 before significant Recovery Act expenditures occur, as well as for ongoing reporting after the initial report;
- provide more direct focus on Recovery Act programs through the Single Audit to help ensure that smaller programs with high risk have audit coverage in the area of internal controls and compliance;
- evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act; and
- develop mechanisms to help fund the additional Single Audit costs and efforts for auditing Recovery Act programs.

Matter for Congressional Consideration: Congress should consider a mechanism to help fund the additional Single Audit costs and efforts for auditing Recovery Act programs.

Reporting on Impact
The Director of OMB should work with federal agencies to provide recipients with examples of the application of OMB's guidance on recipient reporting of jobs created and retained. In addition, the Director of OMB should work with agencies to clarify what new or existing program performance measures are needed to assess the impact of Recovery Act funding.

Communications and Guidance
To strengthen the effort to track funds and their uses, the Director of OMB should (1) ensure more direct communication with key state officials, (2) provide a long range time line on issuing federal guidance, (3) clarify what constitutes appropriate quality control and reconciliation by prime recipients, and (4) specify who should best provide formal certification and approval of the data reported.

The Secretary of Transportation should develop clear guidance on identifying and giving priority to economically distressed areas that are in accordance with the requirements of the Recovery Act and the Public Works and Economic Development Act of 1965, as amended, and more consistent procedures for the Federal Highway Administration to use in reviewing and approving states' criteria.