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December 21, 2005

The Honorable James M. Inhofe
Chairman
The Honorable Jim Jeffords
Ranking Minority Member
Committee on Environment and Public Works
United States Senate

The Honorable Don Young
Chairman
The Honorable James L. Oberstar
Ranking Democratic Member
Committee on Transportation and Infrastructure
House of Representatives

Subject: *Status of Two Authorities Granted to the Department of Commerce's Economic Development Administration*

The Department of Commerce's (Commerce) Economic Development Administration (EDA) Reauthorization Act of 2004¹ directed us to regularly review the implementation of two authorities granted to the Secretary of Commerce: (1) allowing excess funds from projects constructed under projected cost to be reinvested in new or existing projects and (2) establishing a performance award process for grant recipients that meet or exceed performance measures established in connection with the grant. This report transmits briefing slides we provided to committee staff on October 27, 2005.

As agreed with the committees of jurisdiction, because the authorities came into effect on October 1, 2005—too recently to allow for a full assessment—we limited our initial analysis to interviews with agency officials and a review of the legislative history, appropriate budget documents, and proposed regulations. We conducted our review from June 2005 through November 2005 in Washington, D.C., in accordance with generally accepted government auditing standards.

This report (1) discusses EDA's authority to reinvest excess funds and provides information on the portion of these funds EDA has had to return to the U.S. Treasury and (2) describes the status of the performance award system and identifies some steps EDA could take to develop a useful performance award system.

¹Pub. L. No. 1808-373 (2004). The act directed us to report no later than 1 year after the date that this subsection was enacted, or no later than October 27, 2005. As agreed, we fulfilled this requirement by providing the enclosed briefing slides to you by that date.

Background

EDA provides two types of funding for construction projects: public works and economic adjustment grants. Public works grants are designed to help distressed communities attract new industry; encourage business expansion; diversify their economies; and generate long-term, private sector jobs. Economic adjustment grants help areas develop and implement strategies to address structural economic problems resulting from sudden and severe economic dislocation, natural disasters, and spending reductions related to the closure of defense installations and military bases. In addition to providing direct assistance, both types of grants are intended to leverage local and private sector matching funds, sometimes as much as 50 percent of the total project costs. Of EDA's \$292 million in budget obligations for 2005, just under three-fourths (\$212 million) were for construction grants funded under the public works and economic adjustment assistance programs.

EDA published an interim final rule in the Federal Register on August 11, 2005, that included the two authorities. The rule, which went into effect on October 1, 2005, gives Commerce's Assistant Secretary for Economic Development the discretion to use excess funds and performance awards to increase EDA's investment rate for projects to up to 100 percent of cost, in some cases eliminating the need for matching funds. EDA has not yet published a final rule and is in the process of incorporating revisions from Congress on certain provisions of the interim final rule. According to EDA officials, these revisions to the provisions are not applicable to the two authorities. All changes to the provisions will be reflected in the final rule.

EDA Has Been Able to Reinvest Excess Funds since Fiscal Year 2000

Before the EDA Reform Act of 1998, EDA, which was funded with annual funds, was required to return to the U.S. Treasury all funds from construction projects that were constructed for less than the projected cost (cost underruns). The EDA Reform Act of 1998 modified EDA's authorizing legislation (the Public Works and Economic Development Act of 1965, as amended) to permit EDA to retain funds recovered from projects constructed under cost to improve the project, and not return those particular funds, even though they were annual funds, to the U.S. Treasury. Cost underrun funds that could not be used to improve the project had to be returned.

Beginning in fiscal year 2000, appropriations language permitted EDA to retain all program funds until the money was expended—that is, no-year funding. However, according to EDA officials, after the agency started receiving no-year funding, the agency's 1998 authorization legislation had the unintended consequence of requiring EDA to return to the U.S. Treasury cost underrun funds that could not be used to improve the specific construction project, even though the funds were no-year funds. The 2004 authorizing legislation corrected this unintended consequence, and EDA may now retain all cost underrun funding and use the funds for other projects.

EDA officials stated that between fiscal years 2000 and 2004 about \$127.2 million of excess funds was reinvested. Of this amount, about \$79.3 million (62 percent) was used to improve existing projects and about \$47.9 million (38 percent) was reinvested in new projects. EDA officials also said that between fiscal years 2000 and 2005, the agency returned about \$5.7 million of excess funds to the U.S. Treasury—\$3.8 million in fiscal year 2004 and \$1.9 million in fiscal year 2005. In addition, EDA returned about \$6.7 million to the U.S. Treasury that was rescinded in fiscal year 2004 as part of an across-the-board cut in nondefense spending.

EDA Does Not Plan to Implement the Performance Award System in the Near Future

EDA officials told us that the agency has not yet issued any performance awards but was developing policy and procedures that would allow the agency to offer such incentives. But the officials added that they did not foresee the agency issuing any awards in the near future. They said that the agency needed more time to refine the general criteria set out in the interim final rule and noted that any changes would be reflected in the final rule.

Under the new interim final rule, as amended, to qualify for a performance award a grant recipient must be rated as meeting or exceeding certain standards.² That is, recipients' projects must generate at least the number of jobs and the amount of private investment that was initially estimated and must meet the initial target dates that were set for starting and completing the projects. The new rule gives Commerce's Assistant Secretary for Economic Development discretion in determining other performance characteristics. Performance awards would be issued after the projects were closed out, which is a process that takes, on average, about 3 years, and the amounts awarded could not exceed 10 percent of the original project costs. As part of previous analyses, we found difficulties in estimating jobs and private investments both before and after the projects were closed out. Some of these difficulties had to do with limited data being available to measure the impact of construction projects and inconsistencies on the part of some EDA officials in verifying and reconciling initial estimates of projected jobs and private investments with reported results.³ Clearly defined and supportable criteria could improve the basis for granting performance awards, as well as utilizing independent sources to verify estimates.

Agency Comments

We provided a draft of our briefing slides to EDA for review and comment. They generally agreed with the briefing slides and provided technical comments. We have incorporated their comments in this report where appropriate.

Copies of this report are being sent to the Assistant Secretary of Commerce for Economic Development; the Director, Office of Management and Budget; and other interested parties. We will also make copies available upon request. In addition, the report will be available at no charge in GAO's Web site at <http://www.gao.gov>.

²On December 15, 2005, EDA published certain amendments to the interim final rule in the *Federal Register*.

³GAO, *Economic Development Administration: Remediation Activities Account for a Small Percentage of Total Brownfield Grant Funding*, [GAO-06-7](#) (Washington, D.C.: Oct. 27, 2005); *Economic Development: Limited Information Exists on the Impact of Assistance Provided by Three Agencies*, [GAO/RCED-96-103](#) (Washington D.C.: Apr. 3, 1996); and *Economic Development: Observations Regarding the Economic Development Administration's May 1998 Final Report on Its Public Works Program*, [GAO/RCED-99-11R](#): Mar. 23, 1999).

If you or your staffs have any questions about this report, please contact me at (202) 512-4325 or at shearw@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Andy Finkel, Assistance Director; Roberto Piñero; Emily Chalmers; and Tania Calhoun made key contributions to this report.



William B. Shear
Director, Financial Markets and
Community Investment

Enclosure



Excess Funds and Performance Awards

Briefing to Senate Committee on Environment
and Public Works and House Committee on
Transportation and Infrastructure

October 27, 2005



- EDA Mandates
- Objectives
- Background
- Use of Excess Funds
- Performance Awards



The EDA Reauthorization Act of 2004 requires us to evaluate two authorities granted to the Secretary of Commerce:

- The use of funds that remain after projects receiving EDA grants are completed at less than the projected cost (excess funds).
- Performance awards to EDA grant recipients that meet or exceed certain standards.



Our review has two objectives:

- To describe how excess funds are currently used and determine the amount of excess funds that EDA returns to the U.S. Treasury.
- To determine the status of the performance award system that is being developed and identify some of the steps that should be taken next.



- About three-fourths of EDA's budget is used to fund construction-related projects.
- In 2005, \$212 million in budget obligations was designated for construction-related grants.
- EDA's primary construction-related initiatives are the Public Works Program and the Economic Adjustment Program.
- Construction-related projects could be eligible for excess funds, performance awards, or both.



- Before FY 2000, funds for projects were made available annually.
- Authorizing legislation required EDA to return all excess funds to the U.S. Treasury at the end of the fiscal year in which they were awarded.
- Beginning in FY 2000, appropriation language permitted EDA to keep all program funds until the money was expended (no-year money).



- On August 11, 2005, EDA published an Interim Final Rule that included the two authorities.
- On October 1, 2005, the Interim Final Rule became effective (with limited exceptions that were not applicable to the two authorities).
- EDA can now use these two authorities for other purposes, including to increase the investment rate of affected projects and reduce the matching funds requirement.



- EDA has not yet published a Final Rule.
- Discussions with Congress indicate a desire to revise certain provisions of the Interim Final Rule.
- All changes will be reflected in the Final Rule.

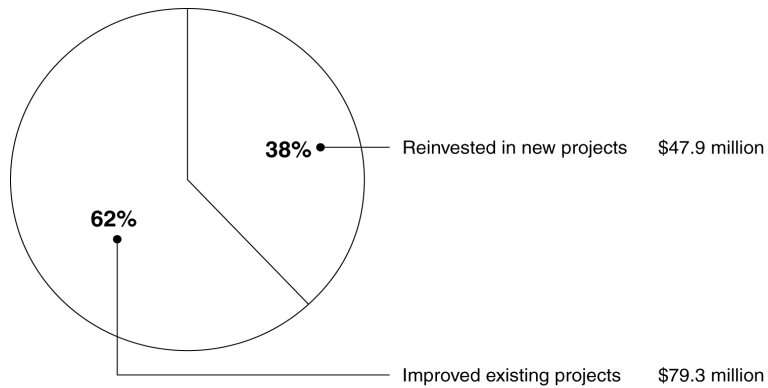


EDA officials told us that the agency:

- needed the new authority, which makes clear that the no-year funds do not need to be returned to the U.S. Treasury, and
- has been able to reinvest some of the excess funds since 2000, but may need this authority to reinvest excess funds in new projects.



Between 2000 and 2004, about \$127.2 million in excess funds was reinvested in new or existing projects:

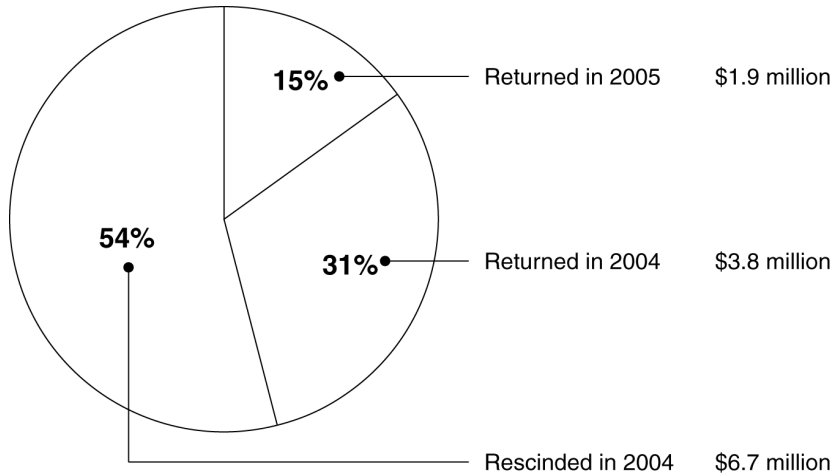


Source: GAO analysis of EDA data.

EDA was unable to tell us how much in excess funds was used to improve original projects on a case-by-case basis.



Between 2000 and 2005, EDA returned about \$12.4 million to the U.S. Treasury:



Source: GAO analysis of EDA data.



EDA officials told us that:

- the agency had not yet issued any awards but was developing the policy and procedures to do so;
- they did not foresee issuing any awards soon;
- awards would be issued after projects were closed out (on average, about 3 years after the time of the award); and
- EDA needed more time to refine general criteria set out in the Interim Final Rule and that any changes would be reflected in the Final Rule.



Under the Interim Final Rule, to qualify for a performance award a grant recipient must be rated as meeting or exceeding the following standards:

- projected number of jobs created;
- projected private investment;
- target dates for starting and completing the project; and
- other characteristics, as determined by the Assistant Secretary of Commerce.

The award may not exceed 10 percent of the EDA grant.



In previous GAO reports, we noted that:

- limited data made quantifying gains from EDA programs difficult,
- discrepancies existed between the initial estimates of jobs and private investment and the actual results reported after 6 years, and
- some EDA regional offices had not followed procedures in verifying estimates.

Clearly defined and supportable criteria are needed as a basis for granting performance awards, as well as independent sources to verify estimates.



Questions?

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