



United States Department of Agriculture
Office of Inspector General





United States Department of Agriculture
Office of Inspector General
Washington, D.C. 20250



DATE: July 24, 2012

AUDIT
NUMBER: 09703-0001-AT

TO: Jonathan Adelstein
Administrator
Rural Utilities Service

ATTN: John Purcell
Director
Financial Management Division

FROM: Gil H. Harden
Assistant Inspector General
For Audit

SUBJECT: Rural Utilities Service's Controls over Water and Waste Disposal Loan and Grant
Program for the Recovery Act

This report presents the results of the subject audit. Your written response to the official draft dated June 1, 2012, is included in its entirety at the end of the report. Excerpts from your response to our Fast Reports and the Office of Inspector General's position are incorporated in the relevant Findings and Recommendations sections of the report. Based on your responses, we were able to accept management decision on all recommendations in the report, and no further response to us is necessary.

In accordance with Departmental Regulation 1720-1, final action is required to be taken within 1 year of each management decision to prevent being listed in the Department's annual Performance and Accountability Report. Please follow your internal agency procedures in forwarding final action correspondence to the Office of the Chief Financial Officer, Director, Planning and Accountability Division.

We appreciate the courtesies and cooperation extended to us by members of your staff during our audit fieldwork and subsequent discussions.

Table of Contents

Executive Summary	1
Background and Objectives	5
Section 1: Recovery Act Issues.....	7
Finding 1: Rural Utilities Service Needs to Improve Project Transparency for the Water and Waste Disposal System Recovery Act Projects.....	7
Recommendation 1	9
Finding 2: Inappropriate Use of Unexpended Grant Funds.....	11
Recommendation 2	12
Recommendation 3	13
Scope and Methodology.....	15
Exhibit A: Summary of Monetary Results	17
Exhibit B: Recovery Act Funds Obligation Dates, Amounts, Construction Dates, Expenditures, and Elapsed Time	18
Exhibit C: Number of Jobs	21
Exhibit D: State and Area Offices Reviewed.....	22
Exhibit E: Sampling Methodology and Results	23
Abbreviations	24
Agency’s Response	25

Rural Utilities Service's Controls Over Water and Waste Disposal Loan and Grant Program for the Recovery Act

Executive Summary

In order to improve the quality of life for rural residents, while creating and saving jobs in rural communities, Congress, as a part of the American Recovery and Reinvestment Act of 2009 (Recovery Act), designated \$3.8 billion in funds for the Water and Waste Disposal System Loan and Grants Program (WWD) in rural areas. Three of the Recovery Act's stated goals were (1) to preserve and create jobs to promote economic recovery; (2) to assist those most impacted by the recession; and (3) to invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits. In enacting the Recovery Act, Congress emphasized the need for accountability over the expenditure of funds. In response, the Office of Management and Budget (OMB) required Federal agencies to establish rigorous internal controls to ensure that Recovery Act funds were distributed in accordance with that objective.¹ In addition, the Office of Inspector General (OIG) was required to provide monitoring and oversight to ensure accountability and transparency of Recovery Act funds.

Therefore, OIG initiated this audit (1) to evaluate the effectiveness of the Rural Utilities Service's (RUS) control systems for achieving the WWD goals of providing loans and grants for sewer, storm water, and solid waste disposal systems in cities and towns having populations up to 10,000 people; (2) to ensure program participants fully met eligibility requirements and complied with program requirements; and (3) to evaluate whether projects met the provisions and intent of the Recovery Act. As of September 30, 2011, RUS had obligated \$3.3 billion² in grants and loans to fund 854 WWD projects throughout the United States. Using RUS' universe of \$1.5 billion in Recovery Act obligations as of September 30, 2009, we selected and reviewed a sample of 22 of 429 WWD projects, totaling \$189 million in obligations.³

Generally, we found RUS had effective controls in place to ensure that WWD loans and grants were provided to eligible program participants and that the participants complied with program requirements. In addition, we concluded the WWD infrastructure improvements that were funded will most likely contribute to economic growth in the future, as emphasized under the Recovery Act. However, our review disclosed improvements are needed to ensure that transparency and accountability requirements emphasized under the Recovery Act are followed. In our review of a sample of 22 projects, we found the Recovery Act's stated goal to promote economic recovery through the preservation and creation of jobs has not yet been fully met, over 30 months after the passing of the Recovery Act. This was evident in the 22 WWD projects reviewed that reported less than 20 percent of the actual jobs identified in planning estimates. Specifically, RUS estimated that 3,384 jobs would be created or saved from our sample projects.

¹ "Initial Implementing Guidance for the Recovery Act," dated February 18, 2009, and, "Updated Implementing Guidance for the Recovery Act," dated April 3, 2009. More updates have since been issued, including those on December 18, 2009 (M-10-08), March 22, 2010 (M-10-14), and, most recently, on September 24, 2010 (M-10-34).

² As of November 23, 2011, RUS had de-obligated \$71 million of this amount.

³ See exhibit E.

However, as of September 30, 2011, RUS reported a total of only 415 actual jobs on Recovery.gov as created or saved (see exhibit C).⁴

RUS deems projects "started" at the time loan and/or grant funds are obligated. We found that projects experienced long periods between the obligation of the funds and the start of the actual construction phase, where most project spending and job creation occurs, due to preconstruction requirements. The Recovery Act states that preference should be given to activities that could be started and completed expeditiously, including a goal of using at least 50 percent of the funds for projects that could be started within 4 months. However, we found only 3 of our 22 WWD (totaling \$33 million) projects actually met this timeframe. In fact, we found that construction for 16 of 22 WWD projects (totaling \$103.1 million) was not started until 5 to 30 months after the obligation of funds, while 3 other projects (totaling \$52.9 million) had yet to reach the actual construction phase as of November 2011. For these three projects, the timeframes between funding obligation and estimated start of construction ranges from 30-36 months.⁵

Overall, RUS estimated 56,000 jobs would be created or retained as a result of the WWD Recovery Act funding; however RUS does not report on the Recovery Act's website the total number of actual jobs created or saved.⁶ In addition, we found that RUS does not clearly identify on its website the amount of time needed to initiate construction of water and waste disposal projects once funds are obligated and the impact such timing has on project spending and job creation. Without RUS' disclosure of project timing, the public may not fully understand the progress of water and waste disposal projects in meeting the goals of the Recovery Act.

RUS officials agreed that job creation is an important element of the Recovery Act, but believe that the WWD projects funded were more intended to address the 4th component of the Recovery Act's stated purpose, "to invest in transportation, environmental protection and other infrastructure that will provide long-term economic benefits." We agree with RUS officials that the WWD infrastructure improvements funded will most likely contribute to economic growth in the future. However, a primary goal of the Recovery Act is to promote economic recovery through the preservation and creation of jobs. As a result, we conclude that greater transparency through disclosure of project timing is needed, so that the public may fully understand the progress of water and waste disposal projects in meeting all the goals of the Recovery Act.

⁴ Our August 31, 2011, Fast Report 09703-0001-AT (2), "Rural Utilities Service Needs to Improve Project Transparency for the Water and Waste Disposal System Recovery Act Projects," stated that 13 of the 22 projects reported on Recovery.gov expenditures totaling \$28.6 million and 178 actual jobs created or saved as of March 31, 2011.

⁵ Our August 31, 2011, Fast Report 09703-0001-AT (2), "Rural Utilities Service Needs to Improve Project Transparency for the Water and Waste Disposal System Recovery Act Projects," found that actual construction for 3 of the 22 projects (totaling \$33 million) started within 4 months of the obligation date, the preferred time stated in the Recovery Act. However, construction for 14 other projects (totaling \$65.8 million) started 5 to 21 months after obligation of funds; while the remaining 5 projects (totaling \$90.1 million) had yet to reach the actual construction phase as of July 22, 2011. For these five projects, the timeframes between funding obligation and estimated start of construction ranges from 25 to 36 months.

⁶ Recipients report the amount of jobs created or saved quarterly in the recipient reporting section of Recovery.gov on a project-by-project basis. RUS does not report total numbers to determine the overall number of jobs created or saved.

We also found that Maine's Rural Development office inappropriately funded a WWD Recovery Act project with unexpended funds from previous projects approved for the borrower. State officials claimed that they authorized the rollover of funds because the borrower had already been approved for the funding during the previous underwriting process and this funding would be carried forward for eligible program purposes involving the next project. As a result, RUS' action provided the town of Farmington with an unfair advantage for unused funds by allowing it to use these funds without having to reapply, as would new applicants. This action also violated grant limitation requirements.

Recommendation Summary

In a Fast Report issued on August 31, 2011, we recommended that Rural Development explain on Recovery.gov the time needed to initiate actual construction for each water and waste disposal system project following obligation of funds and this timeframe's impact on the timing of project spending and jobs created. In response, on December 29, 2011, RUS posted the information on the Rural Development Recovery Act website. We are able to accept management decision for this recommendation, due to the subsequent posting of the information on April 5, 2012, on the Recovery.gov website. RUS has informed OIG that the information will continue to be provided to OMB in the weekly Recovery Act Financial and Activity Report and posted on the Recovery.gov website.

We also recommended in a Fast Report,⁷ issued on November 19, 2010, that Rural Development recover the \$79,000 in mislabeled grant funding from the town of Farmington and conduct a review of similar projects. If any discrepancies resulted in funds being due to the agency, as in the case of the town of Farmington, we recommended Rural Development recover those amounts. We are able to accept management decision for these recommendations, based on the response received from the agency on November 30, 2010. In addition, Rural Development notified OIG on April 24, 2012, that, during the week of February 28 to March 3, 2011, they completed a review at the Maine State office of obligations for the past 4 years for all projects where additional funding was authorized to the same borrower. According to Rural Development, no additional instances of unliquidated rollovers of funds occurred in the projects reviewed.

Agency Response

Rural Development and RUS officials generally agreed with our findings and recommendations in the report. They proposed corrective actions from our Fast Reports noted above that should alleviate the cited issues. Excerpts from their responses to our Fast Reports have been incorporated into relevant sections of the report, and a general response to our report content, dated June 1, 2012, is included at the end of this report.

⁷ Fast Report 09703-0001-AT (1), "Controls Over Water and Waste Disposal Loans and Grants – Inappropriate Use of Unexpended Grant Funds" issued November 19, 2010.

OIG Position

Based on Rural Development's and RUS' responses, we accept management decision on all three recommendations in the report.

Background and Objectives

Background

The Rural Utilities Service (RUS), an agency within the Department of Agriculture's (USDA) Rural Development mission area, was established by Public Law 103-354, Federal Crop Insurance Reform and USDA Reorganization Act of 1994, enacted into law on October 13, 1994. RUS administers the Water and Waste Disposal System Loan and Grants Program (WWD) to improve the quality of life and promote economic development in rural America through loans and grants for sewer, storm water, and solid waste disposal systems in rural cities and towns having populations up to 10,000 people.⁸ Loan and grant funds may be used to construct, enlarge, or otherwise improve rural water, sanitary sewage, solid waste disposal, and storm wastewater disposal facilities. RUS delivers the WWD through the 47 Rural Development State offices, as well as area and local offices.

To receive loan assistance, the borrower must be a public entity. This can include municipalities, Indian tribes, and non-profit corporations. Applicants must (1) be unable to obtain the needed funds from commercial sources at reasonable rates and terms; (2) have the legal capacity to borrow and repay loans, to pledge security for loans, and to operate and maintain the facilities; and (3) propose facilities that are consistent with any development plans of the State, multi-jurisdictional area, counties, or municipalities where the project is to be located. All facilities must comply with Federal, State, and local laws, including those involving zoning regulations, health and sanitation standards, and water pollution control. Grants may be made for up to 75 percent of eligible project costs and are available to reduce water and waste disposal costs to a reasonable level for users of the system.

Congress passed the American Recovery and Reinvestment Act of 2009 (Recovery Act), to alleviate the economic crisis facing our country. It designated approximately \$3.8 billion for WWD loan and grant funds (\$2.8 billion in loan funds and \$968 million in grant funds). In May 2009 (updated as of May 2010),⁹ Rural Development issued its implementation plan for Recovery Act funds with goals to:¹⁰

- Provide a 10 percent allocation of funds for investment in persistent poverty counties;
- Increase new or improved services for 1.9 million customers;
- Reduce by 6 percent rural customers' exposure to water-related health and safety hazards (based on projects funded that will remove an identified health and safety hazard); and
- Create or save an estimated 56,000 jobs.

⁸ Water and waste disposal loans and grants are authorized under section 306 of the "Consolidated Farm and Rural Development Act" (Title 7 United States Code 1926), as amended.

⁹ In May 2010, Rural Development published an updated plan, in which the anticipated obligation of funds was reduced to \$3.3 billion due to a change in the subsidy rate between fiscal years 2009 and 2010, as well as reprogrammed loans to grants.

¹⁰ USDA Rural Development American Recovery and Reinvestment Act Implementation Plan, dated May 9, 2009 (updated May 15, 2010).

Congress, in enacting the Recovery Act, emphasized the need for accountability and transparency concerning the expenditure of Recovery Act funds. Further, on February 18, 2009, OMB issued initial guidance that required Federal agencies to establish rigorous internal controls, oversight mechanisms, and other approaches to meet the accountability objectives of the Recovery Act.¹¹ Rural Development issued a plan¹² to guide its implementation of the Recovery Act.

As of September 30, 2011, RUS had obligated \$3.3 billion in loans and grants for 854 WWD projects throughout the United States and its territories.

Objectives

The objectives of our audit were to (1) evaluate control systems utilized to ensure water and waste disposal program objectives are achieved; (2) ensure program participants fully meet eligibility requirements and comply with program requirements; and (3) evaluate whether projects meet the provisions and intent of the Recovery Act.

¹¹ “Initial Implementing Guidance for the Recovery Act,” dated February 18, 2009, and “Updated Implementing Guidance for the Recovery Act,” dated April 3, 2009. More updates have since been issued, including those on December 18, 2009 (M-10-08), March 22, 2010 (M-10-14), and most recently on September 24, 2010 (M-10-34).

¹² “USDA Rural Development American Recovery and Reinvestment Act Implementation Plan,” dated May 9, 2009 (updated May 15, 2010).

Section 1: Recovery Act Issues

Finding 1: Rural Utilities Service Needs to Improve Project Transparency for the Water and Waste Disposal System Recovery Act Projects

Our review disclosed that improvements were needed to ensure the transparency requirement emphasized under the Recovery Act is followed. RUS did not clearly convey to the public through Recovery.gov the additional time it takes to begin actual construction (the time when most jobs are created) once a project is obligated. Without a clear understanding of when project construction begins, the public may misjudge the progress of RUS' water and waste disposal projects in meeting the goals of the Recovery Act. In our review of a sample of 22 projects, we found the Recovery Act's stated goal, to promote economic recovery through the preservation and creation of jobs, has not yet been fully met. This was evident in the 22 WWD projects reviewed that reported less than 20 percent of the actual jobs identified in planning estimates as being created over 30 months after passage of the Recovery Act. Specifically, RUS estimated that 3,384 jobs would be created or saved from our sample projects. However, as of September 30, 2011, recipients reported a total of only 415 actual jobs on Recovery.gov as created or saved (see exhibit C). While recipients report this data quarterly, the totals are not available on Recovery.gov. To obtain the information in total, one would have to review each project and then each quarter of data to obtain the information for the program as a whole. Also, we found that 17 of the 22 sampled projects reported expenditures totaling only \$51.8 million out of \$189 million as of September 30, 2011 (see exhibit B). RUS officials indicated they expect increased numbers in expenditures and jobs created or saved as projects progress.

Our review of a sample of 22 of 429 projects funded in FY 2009 found that many of the projects experienced long periods between the obligation of the funds and actual construction, where the majority of new jobs are created. RUS deems projects "started" at the time loan and/or grant funds are obligated. However, actual project construction could be delayed months or years after obligation, due to preconstruction requirements. With the obligation of funds, a project will have already completed preliminary design, environmental reviews, and assessments. Projects are then ready to proceed to final design and bid.¹³ Yet, there are several time-consuming steps that must be completed after funds are obligated and prior to the start of actual construction which include, but are not limited to:

- Completing the final design and submitting it to RUS, the State health department, and the State public service commission for review and approval;
- Acquiring signed user agreements and collecting tap fees¹⁴ (if new customers are added);
- Acquiring applicable permits from the U.S. Army Corps of Engineers, Division of Highways, Public Land Corporation, or railroads;

¹³ Final design entails final plans and specifications for projects. According to 7 *Code of Federal Regulations* (CFR) 4280.115, final plans and specifications must be reviewed by the agency and approved prior to start of construction. RUS Instruction 1780.72 provides that when competitive sealed bidding is applicable, an invitation for sealed bids is publicly advertised and a firm-fixed-price contract is awarded to the responsible bidder whose bid, conforming to all the material terms and conditions of the invitation for bids, is lowest, price and other factors considered. Competitive sealed bids are the preferred procurement method for construction contracts.

¹⁴ Fees associated with the establishment and connection of water and sewer lines.

- Acquiring any new property and rights-of-way that are needed for the project;
- Conducting an initial RUS compliance review;
- Submitting proposed user rates;
- Purchasing appropriate insurance coverage; and
- Advertising for bids and contract awards.

In our review of 22 of 429 projects, only 3 of the projects (totaling \$33 million) started actual construction within 4 months of the obligation date, the preferred time stated in the Recovery Act.¹⁵ However, construction for 16 other projects (totaling \$103.1 million) started 5 to 30 months after obligation of funds, while the remaining 3 projects (totaling \$52.9 million) had yet to reach the actual construction phase as of November 2011. For these three projects, the timeframes between funding obligation and estimated start of construction range from 30 to 36 months.¹⁶ In one instance, RUS obligated \$22 million in Recovery Act funds for the Atchison County, Missouri, Wholesale Water Commission project in June 2009. Project officials initially estimated that construction for this project would start in February 2011, or over 20 months following the obligation of project funds (see exhibit B). When we contacted RUS officials in November 2011, construction still had not begun for this project.¹⁷

Although we did not question the timeliness of RUS' loan and grant making and processing for water and waste disposal projects, we believe it is critical that RUS be transparent as to the time needed to initiate construction of water and waste disposal projects because of the goals of the Recovery Act. Three of the Recovery Act's stated goals were (1) to preserve and create jobs to promote economic recovery; (2) to assist those most impacted by the recession; and (3) to invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits.

RUS officials contend that, while many Recovery Act projects are focused more immediately on jumpstarting the economy, others, especially those involving infrastructure improvements, are expected to contribute to economic growth for many years. However, RUS agreed that posting additional information on Recovery.gov, as well as the Rural Development website, may assist the general public in better understanding RUS' program, processes, and implementation of the Recovery Act. "Recovery.gov" is the Federal Government's official website for data related to the Recovery Act and a major source of information for the public. Agencies that received Recovery Act funds are required to periodically report financial data on Recovery.gov, including their obligations and expenditures. In the Recovery Act, Congress emphasized the need for Federal agencies to be accountable and transparent in the expenditure of Recovery Act funds.

¹⁵ Section 1602 Preference for Quick-Start Activities.

¹⁶ Our August 31, 2011, Fast Report 09703-0001-AT (2), "Rural Utilities Service Needs to Improve Project Transparency for the Water and Waste Disposal System Recovery Act Projects," found that actual construction for 3 of the 22 projects (totaling \$33 million) started within 4 months of the obligation date, the preferred time stated in the Recovery Act. However, construction for 14 other projects (totaling \$65.8 million) started 5 to 21 months after obligation of funds; while the remaining 5 projects (totaling \$90.1 million) had yet to reach the actual construction phase as of July 22, 2011. For these five projects, the timeframes between funding obligation and estimated start of construction range from 25 to 36 months.

¹⁷ RUS officials have since reported that the project broke ground in December of 2011 and is currently under active construction.

Subsequently, OMB issued guidance¹⁸ that required Federal agencies to establish rigorous internal controls, oversight mechanisms, and other approaches to meet the accountability objectives of the Recovery Act.

RUS did not clearly convey to the public through Recovery.gov the additional time it takes to begin actual construction once funding for a project is obligated. Without a clear understanding of when project construction begins, the public may misjudge the progress of RUS' water and waste disposal projects. We agree with RUS officials that the WWD infrastructure improvements funded will most likely contribute to economic growth in the future. However, a stated goal of the Recovery Act is to promote economic recovery through the preservation and creation of jobs. As a result, we conclude greater transparency through disclosure of project timing is needed, so that the public may fully understand the progress of water and waste disposal projects in meeting all the goals of the Recovery Act.

We issued a Fast Report on August 31, 2011, detailing this issue.¹⁹ The Recommendation from that Fast Report is Recommendation 1 presented below. Rural Development's official response (dated September 13, 2011) to that Recommendation as well as our position are also included below.

Recommendation 1

Explain on Recovery.gov the time needed to initiate actual construction for each water and waste disposal project following obligation of funds and this timeframe's impact on the timing of project spending and jobs created.

Agency Response

In its September 13, 2011, response to our Fast Report, Rural Development stated:

* * * With regard to public concern regarding our progress, the agency has received positive feedback regarding its Recovery Act implementation of water and waste loans and grants. We attribute this to the significant progress made on the RUS water and waste disposal Recovery Act projects, and to our efforts to inform the public of implementation activities. However, we do appreciate [the Office of Inspector General] OIG's desire for additional public information on the timing of our projects and process. While recipients and the communities they serve have a keen understanding of our process, posting additional information on Recovery.gov (as permitted) and our RD [Rural Development] website may assist the general public in better understanding the program, our processes and our Recovery Act implementation.

¹⁸ Initial Implementing Guidance for the Recovery Act, dated February 18, 2009, and Updated Implementing Guidance for the Recovery Act, dated April 3, 2009. More updates have since been issued, including those on December 18, 2009 (M-10-08), March 22, 2010 (M-10-14), and most recently on September 24, 2010 (M-10-34).

¹⁹ Fast Report 09703-0001-AT (2), "Rural Utilities Service Needs to Improve Project Transparency for the Water and Waste Disposal System Recovery Act Projects."

RD is proud of the progress made to date by its Recovery Act water and waste funds recipients. The jobs that will be created or saved through full implementation will be just as critical and relevant to economic recovery as the jobs that have already been created or saved to date. The agency has invested significant resources and effort into tracking and ensuring that projects funded fulfill the intent of the Recovery Act and proceed at a pace that ensures that this critical infrastructure is built properly so as to serve rural communities well into the future. The agency is also committed to providing the public with information regarding implementation and, to that end, will post additional information regarding the program and processes on appropriate Recovery Act web sites.

On December 29, 2011, RUS provided an email to OIG with a link that showed additional information posted to Rural Development's Recovery Act website; however, this information was not reported to Recovery.gov. Following the exit conference on April 24, 2012, the agency provided OIG with information stating that as of April 5, 2012, the information is and will continue to be provided to OMB in the weekly Recovery Act Financial and Activity Report under the major activities tab and posted on the Recovery.gov website.

OIG Position

Based on the information received on April 24, 2012, we accept Rural Development's management decision for this recommendation.

Finding 2: Inappropriate Use of Unexpended Grant Funds

Maine's Rural Development office inappropriately funded a Recovery Act WWD project, with unexpended grant funds from a previous project approved for the borrower. State officials claimed that they authorized the rollover of funds because the borrower had already been approved for the funding during the previous project's underwriting process and this funding would be carried forward for eligible program purposes involving the next project. As a result, RUS' action provided the town of Farmington with an unfair advantage over new applicants by not requiring the town to reapply for unused funds. This also violated grant limitation requirements, which restrict the percentage of grant funds received to a maximum of 75 percent of the total RUS-provided funding for a project.

RUS' policy²⁰ states that any applicant's contributions will be the first funds expended in a project and grant funds will be the last funds expended.²¹ Once projects are completed, this same policy states that grant funds not expended for authorized purposes will be cancelled.²² In addition, RUS' policy²³ limits the percentage of grant funds received to a maximum of 75 percent of the total RUS-provided funding.

According to a Maine Rural Development State official, the town of Farmington is updating its sewer system through a series of projects. In Rural Development's Community Program Application Processing System and the preliminary engineering report, documentation showed that the most recent project, the Tannery Brook Line Improvements Project,²⁴ was designed to replace lines in that system. In August 2009, RUS approved Recovery Act funding for the project that included a \$370,000 grant, a \$131,000 loan, and \$79,000 in applicant contributions.

While tracing these funds back to their source, we discovered that the \$79,000 in applicant contributions were actually unexpended grant funds left over from a prior RUS non-Recovery Act project for the town, where an influent pump station was completed in October 2009. A Rural Development official acknowledged there was approximately \$79,000 remaining in grant funds from the influent pump station project. The Rural Development officials at both the State and area offices subsequently reported this same \$79,000 as applicant contributions available in the Tannery Brook Line Improvements Project's underwriting process. In addition, while reviewing the underwriting for the influent pump station project, we found that it had also utilized \$9,279 in RUS grant funding from another RUS project for this town that was completed prior to the influent pump station project.

The Tannery Brook Line Improvements Project received approximately 73.8 percent²⁵ of its funding through a grant, according to the underwriting documentation. However, when considering all the funding from RUS, including the \$79,000 in unexpended grant funds from the

²⁰ RUS Instruction 1780.45(f)(3), June 4, 1999.

²¹ Rural Development letters of condition for the town of Farmington, dated April 1, 2009, and August 12, 2009.

²² Cancelled grant funds would be returned to the RUS national office for re-obligation to other projects.

²³ RUS Instruction 1780.10, June 4, 1999.

²⁴ This project was selected as part of the statistical sample utilized in this audit. Our audit scope and sample represent loans and grants obligated in FY 2009 with Recovery Act funds.

²⁵ Total Rural Development project funding, according to the documentation, is a loan in the amount of \$131,000 and a grant in the amount of \$370,000, totaling \$501,000. $\$370,000/\$501,000 = 73.8$ percent.

influent pump station project, RUS will actually finance 77.4 percent²⁶ of this project with grant funds, which exceeds the maximum allowable grant funding of 75 percent of total project cost.

We could not determine if this condition was an isolated case or occurred frequently in Maine. Upon discussion with the State office staff, we were informed that this was not the only time the staff rolled forward unexpended grant funds to new projects with the same borrower. However, the Maine State office provided a subsequent response citing that the town of Farmington is the only occurrence that they were aware of where a project's carryover funds were rolled into a new project.

Maine's State office staff believed that they were not violating any RUS regulations, as the applicant had already applied for the previous grant and the funds left over from the previous project would be spent on eligible project expenses, even though the expenses would be for a different project. RUS national office officials agreed with our conclusion that the regulation prohibited the rolling forward of grant funds from previous projects, regardless of whether the projects are for the same borrower. However, RUS national office officials did state that they believed this was an isolated incidence. A RUS national office official further stated the remaining grant funds should have been spent for items within the scope of the previous project, if possible, and if not, should have been de-obligated and returned to RUS for re-obligation. By not cancelling the unused funds for re-obligation at the national office level, Maine's Rural Development State office gave the town of Farmington an unfair advantage over new applicants for the unused funds. This unused funding, if returned to the national office when cancelled, would have been placed in a pool that all applicants nationwide could compete for, rather than being held in the town's account for the next project.

We did not perform an analysis to determine the full extent to which the Maine Rural Development office has rolled forward unexpended grant funding to other new projects or otherwise inappropriately used unexpended grant funds; therefore, we have no conclusions on the overall impact to the program.

We issued a Fast Report dated November 19, 2010, Audit 09703-0001-AT (1), "Controls Over Water and Waste Disposal Loans and Grants – Inappropriate Use of Unexpended Grant Funds." The Fast Report's recommendations and Rural Development's official response to the recommendations and our positions are included below.

Recommendation 2

Recover the \$79,000 in rolled over grant funding from the town of Farmington.

Agency Response

In its November 30, 2010, response, Rural Development provided:

²⁶ Total Rural Development project funding, including the grant funding from the prior project, raises the total project cost to \$580,000, with a total grant amount of \$449,000 (\$370,000 for this project in addition to \$79,000 from the previous project). $\$449,000/\$580,000 = 77.4$ percent.

* * * We agree that it was an error for the loan specialist in the State office to use the remaining grant funds from a previously funded project in the underwriting for the Tannery Brook phase of sewer improvements. It was also an error to refer to the remaining grant dollars as applicant contribution. The State office was directed to, and has, contacted the town of Farmington to inform them that they will not be able to utilize the \$79,000 of grant funds remaining from the 2009 Influent Pump Station project for the Tannery Brook Project.

The town of Farmington has subsequently requested that the \$79,000 be utilized on the 2009 Influent Pump Station project to install a [Supervisory Control and Data Acquisition], SCADA system. The SCADA computer system was included in the original scope, but not included in the bid, due to concerns by the community regarding sufficient funding.

* * * 7 CFR 1780.45(f)(1) does permit remaining funds to “be used for eligible loan and grant purposes, provided the use will not result in major changes to the facility(s) and the purpose of the loan and grant remains the same.” Eligible items include, but are not limited to, reasonable items within the original project scope that will insure the system will operate more efficiently.

The proposed SCADA system on the influent pump station would enhance the operational efficiency of the plant and, therefore, is an appropriate use of the remaining funds. If approved, the funds would not be returned to the Government. None of the remaining funds will be used for the Tannery Brook Project or any other project. * * *

The proposed SCADA system on the influent pump station would enhance the operational efficiency of the plant and, therefore, is an appropriate use of the remaining funds. If approved, the funds would not be returned to the Government. None of the remaining funds will be used for the Tannery Brook project or any other project. * * *

OIG Position

We accept Rural Development’s management decision for this recommendation.

Recommendation 3

Perform a review of grants approved by the Maine State office to determine the extent to which funds from one project have been rolled over to another project and correct any discrepancies noted. If any discrepancies result in funds being due to the agency, as in the case of the town of Farmington, we recommend Rural Development recover those amounts.

Agency Response

In its November 30, 2010, response, Rural Development provided:

* * * [T]he Rural Development State office has indicated that this occurrence is an isolated incident. To confirm, RUS will review loan and grant assistance provided in Maine over the past two years (FY 09 & FY 10) and to determine whether other similar instances exist. * * *

On April 24, 2012, Rural Development provided the following additional information:

During the week of February 28 to March 3, 2011, a senior national office staff member completed a field visit to the Maine State office. During that time, obligations from the past 4 years were reviewed. Both electronic records in the automated processing system, [Community Program Application Program] CPAP, and paper case files were reviewed on every project for which a subsequent project or additional funding was authorized to the same borrower. The review group consisted of a total of 10 borrowers other than Farmington. No additional instances of unliquidated rollover of funds were present in any of the cases reviewed. In addition, the review revealed that training was held for all Community Program staff on April 7, 2010, emphasizing that funds should not be carried over from one project to another project with the same borrower and should not be considered part of the applicant's contribution on a new project. * * *

Based on the files reviewed, the construction tracking reviewed, and the documented training conducted, the Agency determined that the Farmington case was an isolated incidence and has not been repeated. * * *

OIG Position

We accept Rural Development's management decision for this recommendation.

Scope and Methodology

RUS was allocated \$3.8 billion in Recovery Act funds for WWD. Our audit work focused on RUS' management controls over WWD direct loans and grants funded through the Recovery Act.

We conducted fieldwork at Rural Development's national, State, and area offices. Exhibit D contains a list of the locations of the 17 State offices and 20 area offices visited during our audit. We also visited borrower/grantee locations and project sites, as deemed necessary, to complete our audit work. We conducted our fieldwork between October 2009 and November 2011.

Using RUS' universe of \$1.5 billion in Recovery Act obligations as of September 30, 2009, we statistically selected and reviewed 22 of 429 WWD projects. The 22 projects totaled \$189 million in loan and grant obligations under the Recovery Act for the water and waste disposal loan and grant program. The sampling methodology used is detailed in exhibit E.

To accomplish our objectives, we:

- Reviewed regulations, policies, procedures, and other guidance concerning the administration of the water and waste disposal system loan and grant program and the Recovery Act, to include, but not limited to, 7 CFR 1780, "Water and Waste Loan and Grant Program" (6/1999); RUS Instruction 1780, "Water and Waste Loan and Grant" (9/2003); RUS Bulletin 1780-26, "Guidance for the Use of Engineers Joint Contract Documents Committee Funding Agency Edition Documents of Water and Waste Projects with RUS Financial Assistance" (9/2003); "Rural Development Recovery Act Implementation Plan" (5/2009); "Rural Development Water and Waste Review Guide" (10/09); Rural Development Internal Audit Process - E-mail description (10/2010) and Report (9/2009); OMB Memorandum M-09-10, "Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009" (2/2009); OMB Memorandum M-09-21, "Implementing Guidance for the Reports on Use of Funds Pursuant to the American Recovery and Reinvestment Act of 2009" (6/2009); and OMB Memorandum M-10-34, "Updated Guidance on the American Recovery and Reinvestment Act" (9/2010).
- Reviewed internal and external reports, to include, but not limited to, Rural Development Management Control Reviews; State Internal Reviews; USDA Performance and Accountability Report; Government Accountability Office report; Recovery Act - Project Selection and Starts Are Influenced by Certain Federal Requirements and Other Factors; and OMB Program Assessment Rating Tool, and USDA OIG hotline.
- Interviewed RUS national, State, and area offices, and project officials regarding WWD and the Recovery Act controls and activities.
- Analyzed agency and borrower/grantee loan and grant files and other records, reports, correspondence to assess program aspects concerning eligibility, underwriting, distribution of Recovery Act funds, bidding and construction processes, disbursement of funds, compliance activities, and performance goals.
- Performed onsite reviews of borrower/grantee project sites.
- Reviewed and evaluated Rural Development's and program recipients' Recovery Act activities reported on Recovery.gov.

In many instances, we were not able to review bidding, construction, and/or disbursement of funds, as some projects had not fully progressed to these phases. We plan to more fully review these areas in the next phase of our audit work. Exhibit D documents the list of 22 projects and provides the status of project progress during our review.

We conducted this performance audit 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.

Exhibit A: Summary of Monetary Results

Finding	Recommendation	Description	Amount	Category
2	2	Rollover of Unexpended Grant Funds	\$79,000	Questioned Costs – Recovery Recommended
TOTAL			\$79,000	

The above table contains columns to identify the finding number, recommendation number, description of error, program dollar amount impacted, and OIG management tracking classification associated with the monetary results from the report's findings.

Exhibit B: Recovery Act Funds Obligation Dates, Amounts, Construction Dates, Expenditures, and Elapsed Time

State	Project	Total RUS Funding	Obligation Date	Actual Construction Start Date	Estimated Construction Start Date	Expenditures Per Recovery.gov ¹	0-4 Months from Obligation to Construction ²	5-30 Months from Obligation to Construction ³	30-36 Months from Obligation to Construction ⁴
AL	City of Thomasville	\$15,199,000	May 2009	Nov 2011		\$0		30	
ID	City of Dubois	\$964,000	Jul 2009	Aug 2010		\$841,960		13	
IN	Town of Montezuma	\$5,542,000	Jun 2009	Oct 2010		\$3,943,348		16	
IN	Twin Lakes Regional Sewer District	\$22,112,000	Jul 2009	Aug 2011		\$2,078,190		25	
KY	Garrison-Quincy-KY-O-Heights Water District	\$1,227,500	Aug 2009	Jun 2010		\$971,973		10	
LA	Town of Jonesville	\$205,000	Jun 2009	Jan 2010		\$132,915		7	
ME	Town of Farmington	\$501,000	Aug 2009	Sep 2010		\$332,147		13	
MI	City of Hancock	\$4,000,000	Jul 2009	Apr 2011		\$1,779,912		21	

¹ Recovery.gov recipient reporting data as of September 30, 2011.

² For consistency among categories, actual or estimated start of construction dates were measured based on months.

³ See footnote 13.

⁴ Estimated, as of November 2011. See footnote 13.

Exhibit B – Continued

State	Project	Total RUS Funding	Obligation Date	Actual Construction Start Date	Estimated Construction Start Date	Expenditures Per Recovery.gov ⁵	0-4 Months from Obligation to Construction	5-30 Months from Obligation to Construction	30-36 Months from Obligation to Construction ⁶
MO	Atchison County Wholesale Water Commission	\$22,000,000	Jun 2009		Dec 2011	\$0			30
MS	Clara Water Association, Inc.	\$555,800	May-2009	May-2010		\$555,800		12	
MS	Mt. Comfort Water Association, Inc.	\$1,624,000	May-2009	Oct-2009		\$1,435,118		5	
ND	North Central Consortium-Radar Hill	\$3,019,900	May-2009	Oct-2009		\$3,019,900		5	
NM	Village of Ruidoso Downs	\$1,000,000	Jun-2009	Jul-2009		\$0	1		
NY	Town of Volney	\$964,500	Jun-2009	Apr-2010		\$949,016		10	
OK	Roland Utility Authority	\$3,080,600	Jun-2009	Sep-2010		\$2,277,001		15	
OR	Netarts-Oceanside Sanitary District	\$20,995,000	Jul-2009	Oct-2010		\$4,757,256		15	
VT	Town of St. Johnsbury	\$3,100,000	May-2009	Sep-2009		\$2,974,381	4		

⁵ Recovery.gov recipient reporting data as of September 30, 2011.

⁶ Estimated, as of November 2011.

Exhibit B – Continued

State	Project	Total RUS Funding	Obligation Date	Actual Construction Start Date	Estimated Construction Start Date	Expenditures Per Recovery.gov ⁷	0-4 Months from Obligation to Construction	5-30 Months from Obligation to Construction	30-36 Months from Obligation to Construction ⁸
OR	City of Hood River	\$22,976,300	Sep-2009	Mar-2011		\$8,811,676		18	
WA	City of Shelton	\$28,857,000	Sep-2009	Jan-2010		\$16,790,343	4		
WV	City of Elkins	\$29,075,000	May-2009		May-2012	\$0			36
WV	Big Bend PSD	\$1,800,000	May-2009		Feb-2012	\$0			33
WV	City of War	\$180,300	May-2009	Feb-2011		\$180,300		21	
TOTAL		\$188,978,900				\$51,831,236			

The above table contains a listing of the 22 sampled projects, where projects are located, total RUS funding, funding obligation date, actual or estimated start date for construction, and elapsed time from the obligation date to the start or estimated start of construction.

⁷ Recovery.gov recipient reporting data as of September 30, 2011.

⁸ Estimated, as of November 2011.

Exhibit C: Number of Jobs

Project	Projected Number of Jobs Created ³⁵	Number of Jobs Created ³⁶
City of Thomasville	338.4	0
City of Dubois	22.4	3.4
Town of Montezuma	92.4	17.79
Twin Lakes Regional Sewer District	338.3	30.92
Garrison-Quincy-KY-O-Heights Water District	81.1	3.12
Town of Jonesville	7.0	0.26
Town of Farmington	8.9	1
City of Hancock	61.2	7.25
Atchison County Wholesale Water Commission	336.6	0
Clara Water Association, Inc.	8.5	11.46
Mt. Comfort Water Association, Inc.	24.8	13.55
North Central Consortium-Radar Hill	47.7	26.83
Village of Ruidoso Downs	61.2	0
Town of Volney	14.8	8.8
Roland Utility Authority	47.1	28
Netarts-Oceanside Sanitary District	347.3	35.68
City of Hood River	351.5	90
Town of St. Johnsbury	47.4	8.5
City of Shelton	643.5	128.86
City of Elkins	444.8	0
Big Bend PSD	36.7	0
City Of War	22.4	0
TOTAL	3,384	415.42

The above table contains the name of each sampled project and the estimated and actual jobs created or retained between February 17, 2009, and September 30, 2011. Jobs created or retained are reported by recipients each quarter on the Recovery.gov website. In some cases, we contacted RUS State officials or recipients to confirm the number of jobs created; however, we did not confirm all of these figures.

³⁵ Figures were provided by RUS' national office. These figures are multiplier-based and were included in the project summaries for each project. The multiplier was based on so many jobs per millions of project dollars and was Departmentwide.

³⁶ Recovery.gov recipient reporting data as of September 30, 2011, based on full-time equivalents.

Exhibit D: State and Area Offices Reviewed

	State	State Office Location	Area Office Location
1	AL	Montgomery, AL	Camden, Alabama
2	ID	Boise, ID	Blackfoot, Idaho
3	IN	Indianapolis, IN	Covington, Indiana
4	IN	Indianapolis, IN	Covington, Indiana
5	KY	Lexington, KY	Morehead, Kentucky
6	LA	Alexandria, LA	Jonesville, Louisiana
7	ME	Bangor, ME	Lewiston, Maine
8	MI	East Lansing, MI	Gladstone, Michigan
9	MO	Columbia, MO	St. Joseph, Missouri
10	MS	Jackson, MS	Hattiesburg, Mississippi
11	MS	Jackson, MS	Starkville, Mississippi
12	ND	Bismarck, ND	Bismarck, North Dakota
13	NM	Albuquerque, NM	Las Cruces, New Mexico
14	NY	Syracuse, NY	Watertown, New York
15	OK	Stillwater, OK	McAlester, Oklahoma
16	OR	Portland, OR	Corvallis, Oregon
17	OR	Portland, OR	Redmond, Oregon
18	VT	Montpelier, VT	St Johnsburry, Vermont
19	WA	Olympia, WA	Olympia, Washington
20	WV	Morgantown, WV	Elkins, West Virginia
21	WV	Morgantown, WV	Beckley, West Virginia
22	WV	Morgantown, WV	Beckley, West Virginia

Exhibit E: Sampling Methodology and Results

Objective

This sample was designed to support OIG Audit 09703-0001-AT. The objective was to determine whether loans/grants awarded using Recovery Act funds complied with applicable laws and agency procedures.

Audit Universe and Sample Design

Our universe consisted of 429 loans and grants obligated under the Recovery Act as of September 30, 2009. The universe list was obtained by the audit team from RUS. The loans or grants were spread over 48 States (there were none in Colorado or Wyoming) and Puerto Rico. To meet the audit objectives, the audit team chose to execute a stratified sample with 6 high-dollar projects in a census stratum and 16 projects selected with equal probability from the 423 projects in the second stratum. We had no prior results for WWD to use in sizing the sample. We expected a sample of 22 projects would support projections satisfying the following combination of conditions: a zero percent expected error rate, a 90-percent desired confidence level, and a desired upper error limit of about 13 percent for a stratified sample.³⁷

Table 1: Summary of the universe and sample design counts

Stratum	Stratum Description	Universe: Number of Loans or Grants	Sample: Number of Loans or Grants
Stratum I	Top six loans or grants based on dollar award value.	6	6
Stratum II	All remaining loans and grants	423	16
TOTAL		429	22

³⁷ This combination means that if we found no exceptions to a criterion, we could be 90-percent confident that the error rate in the population did not exceed 13 percent. There would be a 10-percent risk that the error rate exceeded 13 percent. Any criterion for which we observed errors would have either a higher upper limit or a lower confidence level.

Abbreviations

CFR.....	Code of Federal Regulations
FY	Fiscal Year
OIG	Office of Inspector General
OMB	Office of Management and Budget
Recovery Act	American Recovery and Reinvestment Act of 2009
RUS.....	Rural Utilities Service
SCADA.....	Supervisory Control and Data Acquisition
USDA.....	Department of Agriculture
WWD	Water and Waste Disposal System Loan and Grants Program

**USDA'S
RURAL UTILITIES SERVICE
RESPONSE TO AUDIT REPORT**



United States Department of Agriculture
Rural Development

DATE: June 1, 2012

TO: Gil Harden
Assistant Inspector General for Audit

FROM: Jonathan Adelstein /s/
Administrator
Rural Utilities Service

SUBJECT: Final Report on Rural Utilities Service's Controls over the Water and Waste Disposal (WWD) System Recovery Act Projects
Audit # 09703-0001-AT

The Rural Utilities Service appreciates the opportunity to review the draft report dated May 31, 2012 regarding your oversight activities related to the water and waste disposal system program implementation of the funding received through the American Recovery and Reinvestment Act of 2009, P.L. 111-5, (Recovery Act). We are pleased that the report reconfirms that the program has effective controls in place, and that the timeliness and application processing actions taken in regard to Recovery Act funding is not in question.

Through the Recovery Act, the water and waste disposal loan and grant program provided \$3.261 billion for 854 projects in 50 states. The Rural Utilities Service is proud of the progress made to date by its Recovery Act water and waste funds recipients. Much progress has been made toward construction of this much-needed rural infrastructure.

As of May 25, 2012, ninety-three percent of the 836 remaining projects¹ funded are at the point of bid, or beyond. This represents 90%, or \$2.83 billion of the WWD Recovery Act funds awarded. We are pleased that in 203 recipient communities where projects are complete, the public is already receiving the benefits of new or improved infrastructure, and in 461 additional recipient communities the public can witness active construction in progress. (including the Atchison County, MO project noted in the report for which construction started in December 2011.)

As noted in the report, the Agency has addressed the two primary concerns raised through the audit and is pleased that we have reached management decision on all accounts.

¹ Twenty projects were deobligated at the request of recipients after September 30, 2010.

Information copies of this report have been distributed to:

Administrator, RUS

ATTN: Agency Liaison Officer

Government Accountability Office

Office of Management and Budget

Office of the Chief Financial Officer

Director, Planning and Accountability Division

To learn more about OIG, visit our website at
www.usda.gov/oig/index.htm

How To Report Suspected Wrongdoing in USDA Programs

Fraud, Waste, and Abuse

In Washington, DC 202-690-1622

Outside DC 800-424-9121

TDD (Call Collect) 202-690-1202

Bribes or Gratuities

202-720-7257 (Monday–Friday, 9:00 a.m.– 3 p.m. ET)



The U.S. Department of Agriculture (USDA) prohibits discrimination in all of its programs and activities on the basis of race, color, national origin, age, disability, and where applicable, sex (including gender identity and expression), marital status, familial status, parental status, religion, sexual orientation, political beliefs, genetic information, reprisal, or because all or part of an individual's income is derived from any public assistance program. (Not all prohibited bases apply to all programs.) Persons with disabilities who require alternative means for communication of program information (Braille, large print, audiotape, etc.) should contact USDA's TARGET Center at (202) 720-2600 (voice and TDD). USDA is an equal opportunity provider and employer.