



U.S. Department of Agriculture

Office of Inspector General



American Recovery and Reinvestment Act Watershed Protection and Flood Prevention Operations Program – Phase I

**Audit Report 10703-2-KC
September 2010**



U.S. Department of Agriculture
Office of Inspector General
Washington, D.C. 20250



DATE: September 30, 2010

REPLY TO
ATTN OF: 10703-2-KC

TO: Dave White
Chief
Natural Resources Conservation Service

ATTN: Lesia Reed
Deputy Chief
Strategic Planning and Accountability

FROM: Gil H. Harden /s/
Assistant Inspector General
for Audit

SUBJECT: American Recovery and Reinvestment Act - Watershed Protection and Flood
Prevention Operations Program – Phase I

This report presents the results of our audit of the internal controls over the Watershed Protection and Flood Prevention Operations Program funded by the American Recovery and Reinvestment Act of 2009. This report compiles the results of our two previous Fast Reports issued on this subject (dated December 16, 2009, and March 11, 2010). Excerpts from your responses to our Fast Reports (dated January 20, 2010, and March 25, 2010) are incorporated into this report along with the Office of Inspector General's (OIG) position. We have included your September 28, 2010, response as an attachment to this report.

Based on your responses, we have accepted management decision for all recommendations in the report. Please follow your internal agency procedures in forwarding final action correspondence to the Office of the Chief Financial Officer. Please note that Departmental Regulation 1720-1 requires all final action to be completed within 1 year of the date of management decision to preclude being listed in the Department's annual Performance and Accountability Report.

We appreciate the courtesies and cooperation extended to us by members of your staff during this audit.

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Watershed Protection and Flood Prevention Operations Program Phase I

Executive Summary

The American Recovery and Reinvestment Act of 2009 (Recovery Act) was signed into law on February 17, 2009.¹ The purposes of the Recovery Act are to preserve and create jobs, promote economic recovery, and assist those affected most by the recession.² The Recovery Act provided \$145 million to the Department of Agriculture’s (USDA) Natural Resources Conservation Service (NRCS), through its Watershed Protection and Flood Prevention Operations Program (Watershed Operations), to assist State and local governments (project sponsors) with implementing authorized watershed project plans for the purpose of watershed protection, flood mitigation, and water quality improvements. In this first phase of our assessment of NRCS’ use of Recovery Act funds for Watershed Operations, we audited the adequacy of the agency’s controls over the program.

Congress’ enactment of the Recovery Act emphasized the need for accountability and transparency in expending funds. In February 2009, the Office of Management and Budget (OMB) issued initial guidance that required Federal agencies to establish rigorous internal controls, oversight mechanisms, and other approaches to meet the Recovery Act’s accountability objectives.³ According to OMB’s guidance, agencies must develop transparent, merit-based, criteria to guide them in committing, obligating, and expending Recovery Act funds. In addition, Federal agencies should include selection criteria “that have, to the greatest extent, a demonstrated or potential ability to . . . deliver programmatic results . . . [and] achieve economic stimulus by optimizing economic activity and the number of jobs created or saved in relation to the Federal dollars obligated.”⁴

According to the Recovery Act, OIG’s role is to oversee agencies activities and to ensure that they expend funds in a manner that minimizes the risk of improper use. To accomplish this, we are taking a multi-phase approach reviewing Recovery Act-funded Watershed Operations. Our Phase I objectives were to: (1) monitor the development of program guidance and requirements, and (2) evaluate the internal control systems established to ensure the program achieves its objectives, such as selecting and funding projects that meet the Recovery Act’s criteria. Our audit findings are that NRCS should: (1) clarify guidance about when recipients should begin reporting the award of Recovery Act funds, and (2) reconsider its current selection criteria or clarify its project selection methodology to ensure that projects are being funded which align with the Recovery Act’s goals (e.g., creating jobs).

We reported these findings to NRCS’ Chief in two earlier Fast Reports.⁵ In January 2010, NRCS responded to the first report and provided sufficient evidence showing it had taken corrective

¹ Public Law (P.L.) 111-5, dated February 17, 2009.

² Public Law (P.L.) 111-5, Section 3(a)(1) and (2).

³ On February 18, 2009, OMB issued OMB M-09-10: “Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009” and on April 3, 2009, OMB issued OMB M-09-15: “Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009.”

⁴ OMB M-09-15, “Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009,” dated April 3, 2009.

⁵ Issued December 2009 and March 2010.

action by providing specific guidance to its State offices. In March 2010, NRCS responded that the rollback of withdrawn and unused funds identified in the NRCS implementation plan presents an opportunity to focus efforts more on economically distressed areas. As NRCS identifies funds for reallocation, NRCS will prioritize and select any new projects in economically distressed areas to the extent practicable based upon available funding and time remaining to implement the project.

Recommendation Summary

NRCS needs to (1) establish comprehensive procedures that address when the recipient reporting requirements of the Recovery Act begin, (2) reconsider its current selection criteria or provide clarification on the appropriate Recovery Act website and to OMB that details the actual methodology used to analyze and select projects for Recovery Act funding, and (3) justify funding projects (75 totaling \$59 million) where unemployment rates in the project areas are less than the national average instead of projects (45 projects totaling \$97 million) located in areas where the unemployment rate is greater than the national average.

Agency Response

NRCS responded in writing to each of our two Fast Reports and either agreed, or offered further explanation pertaining to our concerns. We summarize these responses in the Finding sections of this report. The Fast Reports and NRCS' responses can be found at http://www.usda.gov/oig/recovery/recovery_reports.htm. On September 28, 2010, NRCS provided a response to the draft final report; NRCS' response is attached as an exhibit to this report.

OIG Position

Based on NRCS' responses, we accept management decision on this report's three recommendations.

Background & Objectives

Background

In response to the current economic downturn, Congress passed the Recovery Act, which included \$145 million for Watershed Operations under the Department of Agriculture's (USDA) NRCS. Through the program, NRCS assists States and local governments (project sponsors) with implementing authorized watershed project plans for the purpose of watershed⁶ protection, flood mitigation, and water quality improvements. The projects can take several years to complete and are owned and operated by the sponsoring organizations and participating individuals. As of September 2010, NRCS provided that it had obligated about \$93 million for 88 projects.

Eligibility criteria for authorized watershed projects include:

- public sponsorship;
- watershed and subwatershed⁷ projects up to 250,000 acres; and
- benefits that are directly related to agriculture, including rural communities, which constitute at least 20 percent of the total project benefits.⁸

NRCS' Watershed Operations also provide technical and financial assistance for authorized projects that have public sponsors which:

- conduct public meetings to assure local involvement;
- obtain all land and water rights and permits required for the installation of works of improvement;
- provide a local share of funds to install improvements; and
- operate and maintain improvements.

Watershed Operations funds that may be available for watershed projects are subject to:

- annual Congressional appropriations;
- State and national resource priorities;
- local funding established for specific project measures;
- completing designs for project measures; and
- NRCS and the project sponsor approving an operation and maintenance agreement.

NRCS groups Watershed Operations projects into four categories:

- land treatment contracts – conservation practices designed to control erosion and sedimentation, or to provide for the proper management of land, water, and natural resources;

⁶ A watershed is the land area drained by a river or stream.

⁷ A subwatershed is a subdivision of a watershed generally corresponding to the area drained by a small tributary or bayou, as opposed to a major river.

⁸ NRCS defines rural as communities with less than 50,000 people.

- mitigation – actions that avoid, minimize, rectify, reduce, eliminate, or compensate for environmental impacts;
- structural repair (i.e., remedial assistance) – correcting problems caused as a result of a mistake by NRCS during installation or as a result of site conditions unknown at the time of installation; and
- new construction – the installation of a new project (e.g., a flood retarding structure).

Objectives

Our audit's objectives were to: (1) monitor the development of program guidance and requirements, and (2) evaluate internal control systems that ensure program objectives are achieved, including whether projects selected for funding met Recovery Act criteria.

Section 1: Project Reporting and Selection

Finding 1: Recipients of Recovery Act Monies Were Not Reporting as Required

Although NRCS issued guidelines to recipients who received awards about their reporting requirements, those guidelines were not sufficiently specific.⁹ OMB requires that recipients report to a designated web site – <https://www.FederalReporting.gov> – the amount of the award, the amount they received, and the amount they spent.¹⁰ If recipients have received or spent no funds, then OMB requires that they report zeroes.¹¹ Reporting no funds received or spent is important because it enables OMB to judge the speed at which funds are being distributed and spent.

NRCS initially directed recipients only to report the amounts they received or spent, but not the amount awarded. Additionally, NRCS made no mention of recipients' obligation to report zeroes if they had received or spent no funds. As a result, recipients were not reporting all of the information OMB required.

We found two cases in which recipients did not correctly report according to OMB's guidelines. The NRCS State office in Minnesota awarded two recipients funds totaling \$420,000, but those funds had not been disbursed by the end of the first reporting period.¹² The NRCS State office did not expect these recipients to report nor did they, as they had yet to receive the actual funds. According to OMB's guidance, these two recipients should have reported the amounts awarded, and then zeroes for the amounts received and spent.

NRCS agreed with us, revised its original position, and issued a bulletin that required recipients to report to <https://www.FederalReporting.gov> the required information.¹³

After our discussion with NRCS' national officials, we issued a Fast Report (December 2009) with the recommendation below.

Recommendation 1

Finalize draft guidance to State offices which corresponds to OMB's requirements, and provide recipients with clear directions on how they are to report to <https://www.FederalReporting.gov> regarding the amount awarded, as well as amounts received and spent.

Agency Response

NRCS issued National Bulletin 130-10-2 (December 18, 2009), to State Conservationists that advised them to notify Recovery Act fund recipients of their responsibility to report awards

⁹ NRCS National Bulletin NB-130-9-4 (September 17, 2009).

¹⁰ Recovery.gov, Recipient Reporting Data Model V3.0 for the Quarter Ended September 30, 2009.

¹¹ OMB Guidance M-09-21, "Implementing Guidance for the Reports on Use of Funds Pursuant to the American Recovery and Reinvestment Act of 2009," Section 2.5 (June 22, 2009).

¹² The first reporting period ended September 30, 2009.

¹³ National Bulletin NM-130-10-2 (December 18, 2009)

at the time of obligation at <https://www.FederalReporting.gov>. State Conservationists were directed to inform recipients of their responsibility for reporting the amount of the award, the amount of funds received, and the amount expended on Recovery Act projects in addition to several other required data elements. NRCS delivered Webinars and forwarded additional guidance to State Conservationists and other staff, which further reinforced the need for compliance with OMB requirements.

OIG Position

We accept management decision for this recommendation.

Finding 2: NRCS Did Not Adequately Consider the Economic Climate of Project Locations Before Recommending Their Selection

Recovery Act funds were intended to promote economic recovery and to preserve and create jobs. Although NRCS stated on the Recovery website¹⁴ and implementation plan¹⁵ that it focused on selecting projects to promote economic recovery in areas most affected by the recession, the factors NRCS actually used to select projects were environmental factors such as flood mitigation, fish and wildlife concerns, and water conservation.

When we discussed this decision with NRCS officials, they stated that they considered the unemployment rates in projects' areas, but that unemployment rates were not a required factor in selecting the projects. They also stated they did not believe the projects would have a significant effect on the local economy. They also explained that the majority of NRCS projects are located in rural areas, which were all considered to be economically distressed. In addition, they said that they did not necessarily target economically distressed areas, but their main objective was to get the projects started quickly in order to create jobs and stimulate the economy. However, they could not provide documents supporting their analyses of the economic need for these projects. We also noted that the latest data NRCS provided to us showed that less than 1 percent of the Recovery Act funds were disbursed.¹⁶

As a result of NRCS' project selection, over a third of the Watershed Operations' Recovery Act funding will not go to counties that were the most economically distressed.

In the table that follows, we summarize NRCS' decisions to fund projects relative to unemployment rates in counties. Specifically, the table shows that NRCS allocated about \$59 million to fund 75 projects in areas where unemployment rates for *all* counties in the project area were *below* the national average—which was 8.1 percent¹⁷—but NRCS *rejected* funding for 45 projects (that would total about \$97 million) in areas where the unemployment rate for *all* counties in the project area exceeded the national average.

	Number of Projects	Total Project Funds
Unfunded projects where unemployment rates in all affected counties were greater than the national average of 8.1 percent	45	\$96,579,696
Funded projects where unemployment rates in all affected counties were below the national average of 8.1 percent	75	\$58,856,500

Table 1: Projects Funded Relative to Counties' Unemployment Rates

¹⁴ Web address – http://www.recovery.gov/Transparency/agency/reporting/agency_reporting5program.aspx?agency_code=12&progplanid=7587

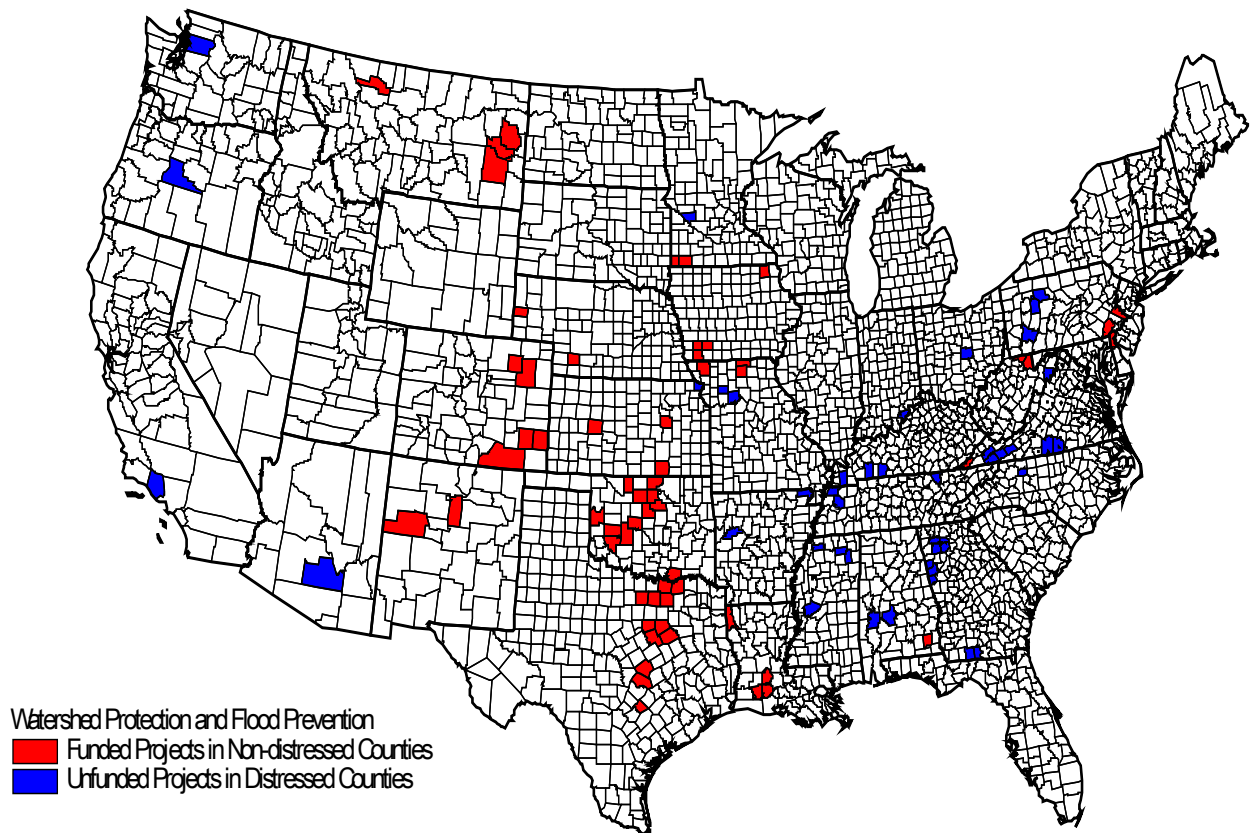
¹⁵ NRCS American Recovery and Reinvestment Act Final Implementation Plan, dated May 15, 2009.

¹⁶ Most current data provided by NRCS was dated September 30, 2009.

¹⁷ Bureau of Labor Statistics, February 2009 data.

The following map shows all counties in the 48 contiguous States, and identifies in **red** the county locations of 75 projects where unemployment rates for all counties in the project area were *below* the national average of 8.1 percent but were funded and identifies in **blue** the county location of the 45 projects where the unemployment rate for *all* counties in the project area *exceeded* the national average but went unfunded.

NRCS
American Recovery and Reinvestment Act
Watershed Protection and Flood Prevention Projects



For example, NRCS rejected a flood prevention project totaling \$1.66 million in an Alabama county even though that county’s unemployment rate was 18.5 percent—more than double the national average. At the same time, NRCS funded a \$4.9 million recreational water quality improvement project near Morgantown, West Virginia, although the county where Morgantown

is located had an unemployment rate of just 3.6 percent.¹⁸ NRCS officials did not provide reasons why projects in economically distressed areas were not selected for funding during the course of our analysis, but did respond to the second Fast Report regarding the projects we inquired about in December 2009.

Recommendation 2

Reconsider NRCS' current selection criteria and replace them with criteria for funding projects in accordance with the specific purposes of the Recovery Act. If new criteria are not developed, provide clarification on the appropriate Recovery Act website and to OMB that details the actual methodology used to analyze and select projects for Recovery Act funding.

Agency Response

NRCS finds that its Watershed Operations project selection criteria are in accordance with Recovery Act's specific statutory mandates, and the methodology it followed appropriately represented in its implementation report. NRCS also added that it believes that rollback of withdrawn and unused funds identified in the NRCS implementation plan presents an opportunity to focus efforts more on economically distressed areas. In particular, as NRCS reviews projects for progress and funds are identified for reallocation, NRCS will select any new projects through its four-step process, but its review will prioritize those projects in economically distressed areas to the extent practicable based upon available funding and time remaining to implement. NRCS will consider different types of information for determining whether an area is economically distressed, including relevant USDA data. The Bureau of Labor unemployment statistics may or may not have relevance to evaluating the economic distress of the rural communities to which NRCS provides service. Once decided, NRCS will notify OIG of the factors it will use to identify economically distressed areas and how it will prioritize, to the extent practicable, new projects accordingly. NRCS will also review this criterion and determine whether any updates to its implementation plan are needed to reflect its incorporation into the process.

OIG Position

We accept management decision for this recommendation. In a subsequent phase of this review, we plan to further evaluate this issue in conjunction with our assessment of agency determinations of Recovery Act program effectiveness.

Recommendation 3

Provide justification for funding projects (75 totaling about \$59 million) where unemployment rates in the project areas are less than the national average instead of projects (45 projects totaling about \$97 million) located in areas where the unemployment rate is greater than the national average.

¹⁸ This project also falls into the adjoining county which had an unemployment rate of 7.3 percent. Both counties were below the national unemployment rate of 8.1 percent.

Agency Response

NRCS followed the applicable statutory, regulatory, and guidance criteria in its selection of watershed operations projects using Recovery Act funds, with emphasis on "projects that can be fully funded and completed with the funds appropriated in this Act, and to activities that can commence promptly following enactment of this Act." Further, no statutory, regulatory, OMB guidance, or NRCS Implementation Plan provision criteria requires, recommends, or even mentions the use of county unemployment data as a project selection criterion.

In contrast, OIG does not mention in its report the specific Recovery Act project selection criteria associated with the funds made available for Watersheds Operations; i.e., that the projects be fully funded and completed with the funds appropriated within Recovery Act timeframes and towards activities that can commence promptly following the Recovery Act enactment.

OIG identified in its report that NRCS did not fund a particular project in an Alabama county that had an unemployment rate of 18.5 percent, double the national average. The Alabama project identified is the Mush Creek Watershed Project that involved a funding request of \$1.66 million for a structural repair. The engineering report had not been completed because it had to secure the required approval from National Headquarters Conservation Engineering Division in order to qualify for approval during Phase 1 or Phase 2 selections. Upon later Engineering approval, Mush Creek Watershed Project was considered for funding in the Phase 3 approval process, but Alabama NRCS officials said they could not obligate the funding by the deadline date of September 30, 2010, thus not meeting a key requirement of Recovery Act funding.

OIG Position

We accept management decision for this recommendation. In a subsequent phase of this review, we plan to further evaluate this issue in conjunction with our assessment of agency determinations of Recovery Act program effectiveness.

Scope and Methodology

We conducted our audit of the Watershed Operations program at NRCS' national office in Washington, D.C.; NRCS' Oversight and Evaluation offices in Fort Worth, Texas, and Beltsville, Maryland; and NRCS' Minnesota State office in St. Paul, Minnesota. We judgmentally selected Minnesota State office because of its proximity to our St. Paul office. In Minnesota, we also visited an NRCS area office in Rochester and two field offices in Lewiston and Worthington. In addition, we interviewed sponsor personnel for the two Minnesota projects.

Our audit covered Recovery Act funding for the Watershed Operations program through December 2009. In September 2009, NRCS had obligated about \$35.5 million in Recovery Act funds for Watershed Operations projects but had disbursed less than \$1 million of the obligated funds to recipients. In September 2010, NRCS provided that it had obligated about \$93 million for 88 projects.

To accomplish our objectives, we reviewed the program's policies and procedures, and the design of its internal controls. We also reviewed management controls that ensure compliance with Recovery Act policies as established by OMB. We interviewed NRCS' national officials and program directors, and program coordinators in the Minnesota State office to obtain their comments on the current resources for Watershed Operations.

In order to monitor NRCS' performance goals established to measure the Watershed Operations program's effectiveness in meeting the purposes of the Recovery Act, we discussed performance measures in our interviews with NRCS national and State officials. We also reviewed performance measures listed in NRCS' Recovery Act Plan and Final Implementation Plan—both specific to Watershed Operations.

To evaluate NRCS' compliance activities pertaining to Recovery Act funding oversight, we interviewed national and State officials about the controls and procedures for projects using Recovery Act funds. We also discussed Watershed Operations compliance reviews with these officials and NRCS' Oversight and Evaluation staff.

To accomplish our objectives, we also:

- Reviewed NRCS' published guidance, instructions, manuals, handbooks, and regulations that detail the controls and procedures over Watershed Operations;
- Obtained and reviewed documents, such as the Recovery Act and OMB guidance, to gain an understanding of the provisions and requirements related to NRCS' Watershed Operations; and
- Obtained unemployment data from the U.S. Department of Labor, Bureau of Labor Statistics for February 2009.

We performed our audit fieldwork from April 2009 through June 2010. 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. During this initial phase, we did not review, analyze, or verify

information in the agency's database and make no representation of the adequacy of the system or the information generated. We plan to perform needed testing during the second phase of our audit.

Abbreviations

ARRA	American Recovery and Reinvestment Act (Recovery Act)
NRCS	Natural Resources Conservation Service
OIG	Office of Inspector General
OMB	Office of Management and Budget
P.L.	Public Law
USDA.....	United States Department of Agriculture
Watershed Operations	Watershed Protection and Flood Prevention Operations Program

USDA'S

NATURAL RESOURCES CONSERVATION

SERVICE RESPONSE TO AUDIT REPORT



Natural Resources Conservation Service
P.O. Box 2890
Washington, D.C. 20013

September 28, 2010

SUBJECT: Natural Resources Conservation Service (NRCS)
Response to the Office of the Inspector General (OIG) Audit
Report 10703-2-KC (2) – American Recovery and Reinvestment
Act (ARRA) — Watershed Protection and Flood Prevention
Operations Program (Watershed Operations) Projects

TO: Gil H. Harden
Assistant Inspector General for Audit
Office of the Inspector General

This memorandum is in response to the draft (OIG) report presents the results of Phase I of the audit of internal controls over the implementation of Watershed Operations projects with ARRA funds. Your draft report is identified as a compilation of the two Fast Reports your office issued in relationship to this audit, and that it includes excerpts from the NRCS response to the Fast Reports along with the OIG position.

NRCS has two substantive concerns with the draft OIG report. The first concern relates to the description regarding how NRCS groups Watershed Projects into four categories, at the top of page 4 of the draft report. OIG defines “structural repairs” as “correcting problems caused by a mistake by NRCS during installation or as a result of site conditions unknown at the time of installation (e.g. a deficiency in NRCS’ original design).” The following is the NRCS definition of Remedial (Structural) Repair at Section 505.20 of the National Watershed Program Manual:

“Remedial assistance is defined as assistance needed to correct problems caused as a result of a mistake or misjudgment by NRCS during the installation of a measure or as a result of latent site conditions unknown to NRCS or the sponsor or land user at the time of installation.”

It is incorrect to refer to circumstances of latent site conditions as an NRCS original design deficiency.

Secondly, NRCS appreciates the excerpts of NRCS responses that have been incorporated into the draft report. However, given the full description provided to the OIG position and the excerpted NRCS response, the draft report does not provide a fair representation of the NRCS analysis or position, and mischaracterizes the NRCS actions under review. Therefore, NRCS requests that the



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NRCS position be provided within the report in addition to the NRCS response to the particular recommendations.

If you require additional information, please contact Lesia Reed, Deputy Chief for Strategic Planning and Accountability, at (202) 720-6297.

Anthony J. Kramer for
Dave White
Chief

cc:

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