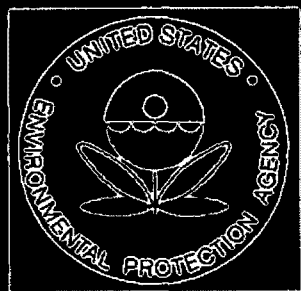


350R98011



OFFICE OF INSPECTOR GENERAL

AUDIT REPORT

Region 2's Deobligation And
Closeout of Construction Grants

January 20, 1998

E1FWF7-02-0011-8100037

Inspector General Division
Conducting the Audit:

Eastern Audit Division
Boston, Massachusetts

Region Covered:

Region 2

Offices Involved:

Office of Policy and
Management

Division of Environmental
Planning & Protection

Division of Enforcement
and Compliance Activities

Office of Regional Counsel



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY

OFFICE OF THE INSPECTOR GENERAL
EASTERN AUDIT DIVISION
JOHN F. KENNEDY FEDERAL BUILDING
BOSTON, MASSACHUSETTS 02203-0001

NEW YORK OFFICE:
290 BROADWAY
NEW YORK, NY 10007-1866

January 20, 1998

MEMORANDUM

SUBJECT: Audit Report of Region 2's Deobligation and Closeout of
Construction Grants
Assignment No. E1FWF7-02-0011-8100037

FROM: Paul D. McKechnie *Paul D. McKechnie*
Divisional Inspector General
Eastern Audit Division

TO: Jeanne M. Fox
Regional Administrator
Region 2

Information Resources Center
EPA (2104)
2104 SW
JAN 22 1998
20460

Attached is our report entitled Region 2's Deobligation and Closeout of Construction Grants. Our overall objectives were to determine whether the Region: (1) identified and deobligated actual and potential construction grant funds in a timely manner, (2) implemented a successful closeout strategy to meet Agency goals, (3) issued timely draft and final determination letters, and (4) resolved grantee disputes in a timely manner. We appreciate the cooperation we received from your staff in conducting this audit. The report contains important findings and recommendations regarding the subject area.

Action Required

In accordance with EPA Order 2750, you, as the action official are required to provide this office a written response to the audit report within 90 days of the final audit report date. For corrective actions planned but not completed by your response date, reference to specific milestone dates will assist this office in deciding whether to close this report. We have no objections to the further release of this report to the public.

Should you have any questions about this report please contact me or Herbert Maletz, Audit Manager at (212) 637-3058.

Attachment

[This page intentionally left blank.]

EXECUTIVE SUMMARY

PURPOSE

The purpose of this audit was to determine if Region 2:

- Identified and deobligated actual and potential construction grant funds in a timely manner.
- Implemented a successful closeout strategy to meet Agency goals for completing all construction grants.
- Issued timely draft and final determination letters so that grants could be closed out and excess funds deobligated.
- Resolved grantee disputes or appeals effectively and in a timely manner.

BACKGROUND

EPA is responsible for overall program management of the Construction Grants Program. The State water pollution control agencies or the US Army Corps of Engineers (COE) handle most day-to-day administrative duties through delegation agreements with EPA. EPA Regional offices retain some project-related decision authorities not legally delegable. Eligible activities funded by construction grants include facility plans (Step 1), plans and specifications (Step 2), and the building of a treatment plant (Step 3).

Construction grants are funded from no-year appropriations and remain available to the program until expended. Since 1972, the Agency awarded over \$50 billion in grants for wastewater treatment projects. Regional Grants Administration Offices manage grants awarded to municipalities to fund construction of wastewater treatment plants. EPA's policy is to close out such grants promptly so

that funds not needed on one project can be deobligated and reallocated to finance other projects.

EPA's August 27, 1992 Financial Closeout Policy for Assistance Agreements emphasized closing out projects and promptly deobligating unliquidated obligations. Closeout of grants is an essential function of prudent grants administration and regions should develop procedures to address this policy. The policy stated that closeout should occur within six months of the last grant action (i.e. final audit resolution, OIG screenout, administrative completion, appeal decision). Administrative completion was a key milestone where administrative aspects have been completed, final payment requested, eligible costs determined, grant conditions satisfied and audit requested. Excess balances should be deobligated at this point.

Regional grants administration branches process deobligations, and delegated State agencies assist in managing construction grants. States may be fully, partially, or non-delegated. New York is fully delegated and responsible for processing administrative completions, audit resolutions, and closeouts. New Jersey is partially delegated and EPA does not make initial allowability determinations. New Jersey submits the administrative completion package to Region 2 which processes audit resolutions and closeouts. Puerto Rico and Virgin Islands administrative completion responsibilities are not delegated.

In November 1993, the Senior Leadership Council designated completion and closeout of the construction grant program an Agency-level weakness. This program still involved billions of dollars and there was a fear this was not universally recognized and might result in loss of resources to properly complete the program.

RESULTS-IN-BRIEF

In recent years Region 2 has initiated many steps to reduce its backlog of construction grants and deobligate a portion of the unpaid funds. Although efforts were made to improve controls or improve compliance with existing controls, we identified areas of repetitive problems where further improvements can be made.

Four OIG audits of Region 2's construction grant deobligation efforts during the past 15 years disclosed material weaknesses. Based on the Region's promises to take action to correct these weaknesses, the OIG closed out these audits. However, the same conditions found in 1982 continued to surface in 1989, 1990 and 1991. We strongly believe that strong top management efforts are needed to resolve this long-standing problem. The specific findings follow:

1. Region 2 has not effectively reviewed construction grants to determine the viability of unexpended grant obligations and did not promptly deobligate unneeded funds. The Region's inadequate control system, lack of priority, poor coordination, and failure to follow Agency guidelines contributed to this condition. As a result, EPA accumulated idle funds of more than \$70 million for the projects reviewed which could have been used to fund other priority projects, State administration grant and special appropriation projects, or could have been deposited into the State Revolving Fund.
2. Region 2 will not meet the Agency's goal of completing and closing out its construction grants by the end of fiscal year (FY) 1997. Also, the Region may not close out certain grants by its own projected date of FY 2000. In addition to the approximately 127 Step 3 grants projected to miss the Agency's target

date, an additional 50 Step 1 and 2 grants will also miss the date. The Region did not give the highest priority and coordination between program offices to achieve more timely closeouts. As a result, millions of Federal dollars of unexpended grant amounts remain obligated unnecessarily, and personnel cannot be reassigned to other areas.

3. The Region's issuance of proposed and final determination letters (FDL) to resolve audit issues was untimely. Although Agency guidance required FDL issuance within 90 or 150 days of the final audit report, the average time for the cases sampled was 358 days. While the resolution process lingered, millions of dollars of Federal funds remained unnecessarily obligated and projects could not be closed.
4. The Region's resolution of grantee disputes has been untimely. Cases have remained unresolved for close to 10 years, and targeted dates for actions leading to the Regional Administrator's decision were continuously revised. Resolution was delayed because initial conferences were not always scheduled and personnel did not prepare timely program memoranda. As a result, cases are reassigned to new attorneys and program personnel and continue to remain open and excess funds can not be deobligated.

RECOMMENDATIONS We recommend that the Regional Administrator

1. Require the Grants and Water Program Branches to conduct a management control review to evaluate the controls for reviewing unexpended obligations and promptly deobligating unneeded funds. Specifically:

- a. Review the grants cited and initiate prompt deobligation actions.
 - b. Determine whether additional funds could be deobligated from other grants.
 - c. Develop specific Regional policies and procedures.
 - d. Designate a specific person to coordinate deobligation efforts between the Branches.
 - e. Implement periodic review meetings and evaluations between various Branch personnel to increase monitoring of unexpended balances.
2. Require the Grants and Water Program Branches to give a higher priority to the expeditious closeout of all Step 1, 2, and 3 construction grants. Specifically:
 - a. Determine whether additional resources or other actions are needed.
 - b. Designate a specific person to coordinate closeout efforts between the Branches.
 - c. Initiate regular meetings between the program offices to discuss actions needed.
3. Require the program offices to place a higher priority on the audit resolution process and eliminate the bottlenecks for preparation of final determination letters.
4. Instruct the Office of Regional Counsel and Water Programs Branch to implement an action plan to accelerate the dispute resolution process and eliminate

the backlog. Timely actions and commitments must be made and accomplished.

REGION 2 RESPONSE and OIG EVALUATION The Region agreed with many of our recommendations, but disagreed with the significance of certain conclusions mainly in the area of construction grant closeouts. After evaluating the Region's comments that disagreed with our report, our position remains unchanged. Their response has been summarized at the end of each finding and other comments were inserted in the body of the report. The complete response has been included as Appendix 1. An exit conference was held with representatives of Region 2 on October 29, 1997.

TABLE OF CONTENTS

EXECUTIVE SUMMARY	i
-------------------------	---

CHAPTERS

1	INTRODUCTION	1
	Purpose	1
	Background	1
	Scope and Methodology	6
	Prior Audit Coverage	8
2	IMPROVEMENTS NEEDED IN TIMELY DEOBLIGATION OF CONSTRUCTION GRANT FUNDS	9
	Background and Criteria	10
	Unpaid Balances Remained Obligated	11
	Examples of Untimely Deobligations	13
	Inactive Projects Should be Reviewed	15
	Internal Controls	18
	Other Control Weaknesses	18
	Conclusion	20
	Regional Response	21
	OIG Evaluation	22
	Recommendations	25
3	INCREASED EMPHASIS NEEDED TO MEET GRANTS COMPLETION/CLOSEOUT STRATEGY	27
	Background and Criteria	28
	Region 2 Must Accelerate Closeouts	29
	Step 3 Grants	30
	Grant Untimely Closed Out	34
	Step 1/2 Grants	35
	Duplicate Audit Requests	38
	Screened Out Projects Remained Open	39
	Conditional Administrative Completions	41
	GICS Information	42
	Other Factors Affecting Closeouts	42

**Deobligation/Closeout
of Construction Grants**

	Conclusion	43
	Regional Response	44
	OIG Evaluation	45
	Recommendations	51
4	AUDIT RESOLUTION PROCESS WAS UNTIMELY	53
	Criteria	53
	Analysis of Resolution Untimeliness	54
	Regional Response	56
	OIG Evaluation	57
	Recommendations	57
5	LENGTHY DISPUTE/APPEAL PROCESS DELAYED CLOSEOUTS	59
	Background	60
	Current Disputes Inventory	60
	Status Reports	63
	Untimely Program Memoranda	63
	Other Factors	63
	Regional Response	67
	OIG Evaluation	68
	Recommendations	68

EXHIBITS

1	Schedule of Unliquidated Balances	69
2	Schedule of FDLs Issued or Unresolved	72
3	Additional Examples of Untimely Dispute Appeal Resolution	75

APPENDICES

1	Region 2's Response to the Draft Report.	77
2	Abbreviations	99
3	Distribution.	101

CHAPTER 1

INTRODUCTION

PURPOSE

We performed an audit of Region 2 construction grant closeout efforts and deobligation of excess funds. Our specific objectives were to determine whether the Region:

- o Identified and deobligated actual and potential construction grant funds in a timely manner.
- o Implemented a successful closeout strategy to meet Agency goals for completing all construction grants.
- o Issued timely draft and final determination letters so that grants could be closed out and excess funds deobligated.
- o Resolved grantee disputes or appeals effectively and in a timely manner.

BACKGROUND

Regional Grants Administration Offices manage grants awarded to local municipalities to fund construction of wastewater treatment plants. EPA's policy is to close out construction grants promptly so that funds not needed on projects can be deobligated and reallocated to finance other treatment works projects.

EPA is responsible for overall program management of the Construction Grants Program. The State water pollution control agencies or the US Army Corps of Engineers (COE) handle most day-to-day administrative duties through delegation agreements with EPA. EPA Regional offices retain some project-related decision authorities not legally

delegable. Eligible activities funded by construction grants can include facility plans (Step 1), plans and specifications (Step 2), and the building of a treatment plant (Step 3). No new Step 1 and 2 awards were issued after December 29, 1981 and all such projects should have been completed by September 30, 1985.

Construction grants are funded from no-year appropriations and remain available to the program until expended. Since 1972, the Agency awarded over \$50 billion in grants for wastewater treatment projects. The EPA Administrator's 1988 Needs Survey Report to Congress assessed the capital investment required to build or improve municipal wastewater treatment facilities. The report estimated that \$68 billion was needed for wastewater projects nationwide.

Delegation to States

Although EPA's regional grants administration branches process all deobligations, delegated State agencies assist in managing construction grants. States may be fully delegated, partially delegated, or non-delegated. New York is fully delegated and responsible for processing administrative completions, audit resolutions, and project closeouts.

Although the State submits a grant amendment to the Region to deobligate funds, Region 2 is not free of all deobligation responsibility. The Region must process amendments and reduce unliquidated obligations in EPA's financial records. Also, the Region must review all unliquidated obligations semiannually and certify whether they are still valid.

New Jersey is partially delegated and EPA does not make initial allowability determinations. The State submits the administrative completion package to Region 2 which processes audit resolutions and closeouts. Puerto Rico and Virgin Islands administrative completion responsibilities are not delegated. Region 2 is responsible for initiating all grant amendments to deobligate unneeded funds.

Criteria

An October 15, 1984 Office of Water and Inspector General memorandum established policies for auditing grants with unresolved claims. If the claim was clearly separable, the grantee should submit a final payment request contingent on resolution of the claim. EPA should then adjust the grant to estimate Federal exposure, proceed to audit, and closeout the balance of the grant. Another October 15, 1984 memorandum emphasized expeditious grant completion and closeout. Regions should notify grantees to submit final payment requests within 90 days or the last request will be considered the final request, and deobligate unexpended funds.

EPA's August 27, 1992 Financial Closeout Policy for Assistance Agreements emphasized closing out projects and promptly deobligating unliquidated obligations. Closeout is an essential function of prudent grants administration and regions should develop specific procedures to address this policy. The policy stated that closeout should occur within six months of the last grant action (i.e. final audit resolution, OIG screenout, administrative completion, appeal decision). Administrative completion was a key milestone where all administrative aspects of the project have been completed, final payment requested, eligible costs determined, grant conditions satisfied and audit requested. All excess balances should be deobligated at this point.

In November 1993, the Senior Leadership Council designated completion and closeout of the construction grant program an Agency-level weakness. This program still involved billions of dollars and there was a fear that this was not universally recognized and might result in a loss of resources to properly complete the program. Without such resources, the closeout process could slow down to an unacceptable pace and result in a loss of institutional knowledge, records, and ability to manage over an extended period.

In 1996, the Office of Management and Budget (OMB) again

recommended that completion/closeout of the construction grant program should be declared a material weakness citing "the closeout schedule continues to slip and millions of dollars in ineligible costs are not being reimbursed for reuse on other high priority state clean water projects..." The Agency shared OMB's concern and elevated it to an Agency level material weakness in the 1996 Integrity Act report.

Of the more than \$50 billion total EPA construction grants awarded, 1,085 grants (\$12 billion) remained open at the end of fiscal year (FY) 1996. The 1990 Construction Grants Completion/ Closeout Strategy was developed to expedite closeout so resources could be reallocated. It established goals of administratively completing all projects by FY 95 and closing out all grants by FY 97.

Region 2 Progress

Prior to Region 2's recent reorganization the Grants Administration Branch (GAB) and Water Management Division (WMD) had responsibility for construction grant completion/closeout and deobligation of unneeded funds. The GAB/WMD FY 95 update projected 58 closeouts. However, WMD's tracking system only noted 32 due to (i) inadequate or missing New Jersey project documentation, and (ii) the prolonged New York disputes process.

WMD's September 21, 1995 memorandum noted its FY 96 beginning inventory of 138 New York and New Jersey Step 3 grants (GAB's October 19, 1995 memo stated 151 grants) and 111 Puerto Rico and Virgin Islands grants. WMD planned to administratively complete all New York non-Modification/

Replacement construction grants by FY 97. The memorandum provided the following information:

<u>FY</u>	<u>Closeouts</u>	
	<u>Commitment</u>	<u>Performance</u>
93	79	80
94	74	79
95	58	27 projected
	(reduced to 32)	
96	39	

Region 2's FY 94 Integrity Act Assurance Letter indicated 366 open construction grants (182 Step 1 and 2, and 184 Step 3 projects). The FY 95 Assurance Letter indicated 262 open grants (151 New York/New Jersey, 111 Puerto Rico/Virgin Islands) since 109 Step 1 and 2, and 32 Step 3 projects were closed and \$26 million deobligated. New Jersey and New York Step 3 projects were reduced from 1,600 to 134 (NJ 58, NY 76), and Step 1 and 2 universe was reduced from 700 to 75 (as of September 30, 1995). Because of the difficult projects, lengthy appeals process, and reduced resource levels, the Region reflects a 2000 end date.

The FY 96 Assurance Letter noted 44 Step 3 closeouts. The remaining 239 Step 3 projects includes 112 administratively completed projects (47 to be completed during FY 97. The Region also anticipated completing the 68 Step 1 and 2 projects ready for closeout by the end of the calendar year.

On July 21, 1996 Region 2 formally implemented its reorganization to an integrated, multi-media approach to environmental planning, compliance and program activities. Responsibility for New York and New Jersey grants was assigned to the Division of Environmental Planning and Protection (DEPP), Water Programs Branch - Construction Grants Section. However, the Division of Enforcement and Compliance Assistance (DECA), Water Compliance Branch was given responsibility for the Caribbean grants.

SCOPE AND METHODOLOGY

We performed this audit according to the *Government Auditing Standards* (1994 Revision) issued by the Comptroller General of the United States as they apply to program audits. Our review included tests of the program records and other auditing procedures we considered necessary. No other issues came to our attention which we believe warranted expanding the scope of the audit.

To accomplish our objectives we reviewed payment records and interviewed Region 2 officials where focus was primarily on the Grants and Contracts Management Branch (GCMB), Water Programs Branch (WPB - Construction Grants Section), Water Compliance Branch (WCB - Caribbean Section), Office of Regional Counsel (ORC), and Financial Management Division (FMD). We also reviewed records and interviewed New York State Department of Environmental Conservation (NYSDEC) and New Jersey Department of Environmental Protection (NJDEP) officials.

To evaluate the timeliness and effectiveness of regional grant deobligation and closeout actions, we judgmentally selected open and recently closed New York, New Jersey, Puerto Rico and Virgin Islands projects. Our review focused on grants with the largest unliquidated balances. We reviewed EPA orders, directives, regulations, policies, and procedures related to construction grant closeout strategies, deobligations of unneeded funds, audit resolution, dispute and appeal process, information management and other tracking systems.

We further evaluated deobligation and closeout efforts by reviewing Integrated Financial Management System (IFMS) and Grants Information Control System (GICS) grant payment and unpaid balance reports, unpaid obligation records, NYSDEC and NJDEP records, OIG audit files, final determination letters (FDL), and ORC files. We interviewed appropriate FMD, ORC, GCMB, WPB and WCB personnel

to determine their roles and responsibilities. We also interviewed NYSDEC's Fiscal/Grants Management Unit and NJDEP's Municipal Wastewater Assistance Unit personnel.

For the grants selected, we reviewed payment and project files and discussed the grant status with State and regional officials to identify any idle funds. We also identified procedures for processing administrative completions and grant closeouts to determine when funds are deobligated from administratively complete grants.

To determine unliquidated balances which could be potentially deobligated, we reviewed the January 2, 1997 IFMS Monthly Construction Grant Summary Report. Because of incorrect obligation data, Finance provided a revised IFMS report dated March 1, 1997. We also considered the grantee's final payment request, grant official's determination of allowable costs, audit results, and any grantee appeals. The following amounts were considered potentially eligible for deobligation:

- (a) the excess of an outstanding grant award over the grantee's final payment request; and
- (b) disallowed amounts not appealed by the grantee.

We conducted our survey from February 20 to May 11, 1997 and initiated an in-depth review from May 12 to June 15, 1997. As part of our evaluation we reviewed the Region's FY 94 to 96 Federal Managers Financial Integrity Act (FMFIA) Assurance Letters. These reports did not identify any material weaknesses or vulnerabilities pertaining to construction grant deobligations or closeouts.

**PRIOR AUDIT
COVERAGE**

The OIG has issued the following five audit reports pertaining to Region 2's untimely deobligation of construction grant funds. Reports **E1VW2-01-0029-21443** (August 12, 1982) and **E2FWP0-02-0041-0400001** (October 20, 1989) disclosed that substantial unliquidated obligations in Region 2's construction grant program had not been timely deobligated.

Report **E1AME9-11-0041-0100523** issued September 1990 (Management of Unliquidated Obligations in Administratively Complete Construction Grants) disclosed that Region 2 had 38 grants with more than \$40 million needing deobligations. These grants had been administratively completed for an average of 34 months. Report **E1AME9-11-0041-1100426** issued September 1991 (Management of Unliquidated Obligations in Construction Grants that have not been Administratively Completed) identified 17 grants with more than \$58 million of deobligable or potentially deobligable funds.

Also, OIG's August 29, 1986 Review of Region 2's Construction Grant Closeout Procedures (**E1CW4-02-0144-61424**) disclosed (i) inaccurate construction grant information recorded in GICS, (ii) grants screened out by the OIG were not timely closed, (iii) grants completed for several years were held open for extended periods of time, and (iv) insufficient NJDEP staffing to eliminate backlog.

In all instances the OIG closed out these audits based on the promised actions to be implemented.

CHAPTER 2

IMPROVEMENT NEEDED IN TIMELY DEOBLIGATION OF CONSTRUCTION GRANT FUNDS

Region 2 needs to improve its timeliness in identifying and deobligating excess construction grant funds. We identified more than \$63 million that was unpaid, and not timely deobligated. In addition, approximately \$7.5 million of recently deobligated amounts could have been accomplished many years earlier. The grants with balances that could be deobligated had been administratively complete an average of 76 months when we finished our fieldwork. The Region's failure to deobligate unneeded construction grant funds has been a continuous problem since 1982.

These conditions were caused by Region 2 generally waiting until the project was ready for final closeout before deobligating unneeded funds, instead of deobligating them earlier. Specific factors were (i) the Region's inadequate control system, (ii) lack of priority given to deobligation efforts, (iii) inadequate or reduced Regional and State personnel with construction grants knowledge, (iv) inadequate coordination between Water, Grants, Regional Counsel (ORC) and Finance officials, (v) lack of regional policies outlining specific responsibilities and methods for accomplishing deobligations, and (vi) missing grant files.

As a result, more than \$70.5 million, that could have been used to fund other priority construction projects, remained idle (See Exhibit 1 for details) and needed work has been delayed. Such funds could have also been recently used for State administration of construction grant and Special Appropriation projects, or could have been deposited into the State Revolving Fund.

Background and Criteria

EPA's policy has been that unneeded construction grant funds should be taken from overfunded projects as soon as possible and made available for other projects. The Handbook of Procedures for Construction Grants states, "Project reviewers are to be alert for legitimate opportunities to reduce grants, since recovered funds, after being returned to EPA, are reallocated to the State for funding other projects on the State's project priority list." Also, grant decrease requests are generally initiated by the Agency, not by the grantee. Moreover, the Financial Management Manual requires prompt adjustment obligations upon the occurrence of any event which increases or decreases such obligation.

After the State or COE completes the final inspection and certifies that the project is functioning properly, the grantee submits a final payment request. The State, COE or EPA reviews the request and recommends the final payment amount. The grant should now be adjusted to deobligate any excess funds and forwarded to the OIG for audit. If the grant is not audited (screened out) it should be closed out. If audited, all issues should be resolved, any remaining excess funds deobligated, and the grant closed out.

EPA's policies and procedures require that unneeded funds be deobligated during the administrative completion step. The Administrator's November 22, 1982 memorandum stated:

We should make the most effective use of EPA construction grant funds and ensure that they not lay idle as invalid, unpaid obligations for projects where they are no longer required . . . The identification, and subsequent deobligation, of funds that will not, or need not, be spent is an important management responsibility . . . You should consider deobligating funds for projects when . . . the final reimbursement request was less than the grant amount.

The General Accounting Office (GAO) defines deobligation as an Agency's cancellation or downward adjustment of previously recorded obligations. Region 2 generally followed a policy of not deobligating funds until projects were closed, instead of when grantees submitted final payment requests and projects were administratively completed.

**Unpaid Balances
Remained Obligated**

We analyzed IFMS reports as of March 1, 1997 to determine Region 2's open construction grants with unpaid balances, and found 159 projects which exceeded \$50,000. Some projects have not reached the administrative completion stage.

<u>State</u>	<u>#of Grants</u>	<u>Total Unpaid</u>
New York	52	\$189 million
New Jersey	27	23 million
Puerto Rico	75	71 million*
Virgin Islands	<u>5</u>	<u>17 million</u>
Total	<u>159</u>	<u>\$300 million</u>

*Includes projects awarded in 1992 or thereafter.

Besides these 159 grants, there were an additional 80 grants in New York (27), New Jersey (26), Puerto Rico (26), and Virgin Islands (1) with individual unpaid balances of less than \$50,000. This significant amount of Federal funds remained unpaid for as long as 20 years.

From the 159 grants with large unpaid balances, we reviewed 35 projects either under construction, administratively complete, audited, or appealed. Our review disclosed that 26 of the 35 grants reviewed had actual or potential unpaid

funds exceeding \$63 million that could be deobligated (see below, with more detail in Exhibit 1). Also, in four of these grants more than \$7.5 million were recently deobligated that had been lying idle for substantial periods (See Exhibit 1). Therefore, approximately 60 percent of the unpaid balances reviewed (\$110.9 million) were potentially deobligable. Based on this sample, there are potentially millions of additional dollars that may be deobligable for grants not reviewed.

<u>State</u>	<u>Reviewed</u>		<u>Potential Deobligation</u>	
	<u>Grants</u>	<u>Unpaid Balance (in millions)</u>	<u>Grants</u>	<u>Amount (in millions)</u>
NY	15	\$ 79.2	12	\$49.7
NJ	11	11.2	8	9.1
PR	7	4.2	6	4.2
VI	2	16.3	0 (*)	0 (*)
Total	35	\$110.9	26	\$63.0

(*) Does not include \$10 million applicable to the Mangrove Lagoon Facility discussed later in this chapter.

Deobligation Policy Not Consistent with Agency Guidance

Region 2's deobligation policy was not consistent with Agency guidance that EPA should make the most effective use of grant funds and ensure they do not lay idle as invalid, unpaid obligations no longer needed. EPA's Administrator has urged regions to deobligate funds when the final reimbursement was less than the grant amount. Although Region 2 officials acknowledged that unneeded construction grant funds should be timely deobligated, they indicated and our review disclosed this was not always a high priority.

The New Jersey Department of Environmental Protection's (NJDEP) policy was not to deobligate funds until projects were closed out. Its Standard Operating Procedures Manual states that if excess grant funds remain, they will be removed after audit resolution when all appeals have been resolved.

EPA's deobligation policy is clear, and unneeded funds should be promptly deobligated because funds are badly needed for other projects. Unneeded funds should not be confused with questioned or appealed amounts. There is no uncertainty regarding the excess of an outstanding grant award over the grantee's final payment request, and there is no uncertainty regarding disallowed amounts not cited in the grantee's final appeal. These funds are not being contested and clearly not needed for the originally obligated grant. Region 2 should work with New Jersey officials to ensure they promptly deobligate unneeded funds.

In prior reviews Region 2's reason for not deobligating funds until project closeout was to avoid possible grantee appeals. Also, personnel concentrated on awarding and monitoring new grants, rather than deobligating funds. The Region's response to OIG report 0100523 (September 1990) reported "it is working with its States and Territories to prepare a policy during the first quarter of FY 91 to deobligate unneeded grant funds upon administrative completion." However, this policy has not been established or implemented. The Region should have deobligated unneeded funds as well as performed these other functions, and management should have been alerted if resources were insufficient to accomplish these tasks.

Although its policy is to generally wait until the project is closed before deobligating funds, the Region previously got requests for deobligations, particularly from NYSDEC. However, the Region would generally not process grant amendments to deobligate unneeded funds.

Examples of Untimely Deobligations

Region 2 has not always promptly deobligated funds. These four examples illustrate the need for timely review and deobligation of excess funds.

Nassau County (grant 891-09) was awarded on September 30, 1980 and administratively completed on June 29, 1987. The current unpaid balance is \$3,276,651. We believe that at least \$3,137,150 could be deobligated (\$139,501 could be set-aside to resolve a dispute). NYSDEC officials also agreed that \$3,137,150 could be deobligated. Although NYSDEC certified a grant decrease of \$3,137,150 six years ago, Region 2 refused to process it. Also, the September 1990 OIG audit report identified the same \$3,137,150 that could have been deobligated since June 29, 1987. We do not believe it was prudent management to tie up these funds for 10 years because of potential contingencies.

The City of Auburn (972-01) was awarded on December 1, 1976 and administratively complete on June 30, 1988. The last payment was September 3, 1986 and the grant currently has an unpaid balance of \$1,065,865. Based on an OIG audit a bill for collection (BFC) for \$141,054 was sent to the grantee on March 21, 1991. It was appealed and the Regional Administrator's March 21, 1995 decision reduced the \$141,054 bill by \$49,385. However, it wasn't until February 27, 1997 (after our audit started) that \$1,065,865 was deobligated (more than 10 years since the last payment).

Cape May (661-07) was awarded on December 28, 1984 in the amount of \$26,855,648 (subsequently amended to \$28,628,685). It was administratively completed on September 28, 1990, final payment was made on March 7, 1995, and an unliquidated balance of \$2,453,828 remains. In 1995 one issue involving innovative costs of \$171,000 was appealed to NJDEP. The Region should have set-aside the \$171,000 until the matter was resolved and deobligated the remaining \$2,282,828 in March 1995 (26 months ago).

The PRASA-Anasco Trunk Sewer (120-08) was awarded in the amount of \$2,941,870 on March 9, 1987 (grant was increased by \$2,968,259 on September 30, 1988) and administratively completed on September 29, 1992. On

September 15, 1992 the grant was reduced by \$905,503 and a final payment of \$187,418 was processed on May 21, 1994. As a result, \$2,942,169 is potentially deobligable (\$2,941,870 has been unpaid since March 9, 1987 - 10 years).

The Region's response to the draft report indicated the project was closed on July 9, 1997, but provided an inaccurate project chronology (date of award, grant amounts, etc.). On September 15, 1997 we discussed this matter with the Grants Specialist and inquired why IFMS showed \$2,941,870 outstanding while the response asserts only \$299 remained. The Specialist discovered a March 9, 1987 grant amendment (more than 10 years ago) to cancel this grant and deobligate \$2,941,870. However, this cancellation and deobligation was not reported to Finance or action was not taken in 1987 to correct this situation. For 10 years IFMS and Agency records erroneously showed \$2,941,870 obligated. This error should have been corrected when the Region submitted their required annual certification of grant obligations. As a result of the draft report, on September 17, 1997, the Agency's records were corrected to eliminate the \$2,941,870.

**Inactive Projects
Should be Reviewed**

Financial disbursement activities should be reviewed regularly to determine whether excess funds could be released from inactive or completed projects. If the grantee does not expeditiously initiate and complete the project, 40 CFR 30.903 through 30.905 allows grants to be terminated or annulled.

One example of a possible inactive grant was **Perth Amboy** (435-02). The \$3,211,243 grant was awarded on September 26, 1985 and the only payment made (\$250,310) on January 14, 1991 (64 months after award). Since 1991 no payment activity has occurred for 76 months. OIG's September 30, 1991 audit report indicated three contracts would be awarded by March 1991 and work completed by October 1992.

However, the grantee has not completed the work or requested reimbursement. Therefore, we believe the unliquidated balance of \$2,960,933 could be potentially deobligated. Although Water Programs Branch personnel believe this project was active they could not provide any reason for the lack of progress.

The Virgin Islands Mangrove Lagoon (C780013-04) awarded September 28, 1984 (\$11,134,058) was another possible inactive grant. The 100% award was to design and construct a treatment facility, collector and inceptor sewers, force mains and an ocean outfall. The last payment was February 10, 1988 and excess funds of \$10,081,348 remained.

Throughout 1989 and 1990 the Region notified the grantee about delays which violated the grant regulations and the September 27, 1985 Consent Decree, and threatened to terminate the grant. These documents required completion of plans and specifications by January 1, 1986 and facility operations by July 1, 1988. Final plans and specifications have not been submitted and the grantee's September 1988 report stated "the status of final plans and specifications is uncertain at this time." A Regional engineer also stated the Region considered terminating the grant and deobligating the excess \$10,081,348. Another 1990 memorandum stated that due to delays, the project's construction costs will escalate.

The Consent Decree included construction of the Mangrove Lagoon Regional Facility. The grantee failed to construct it and a March 1991 motion was filed to enforce the Decree. On December 29, 1994 an Amended Consent Decree outlined specific revised construction dates. For example, design contract award was March 31, 1995 and complete bid document submission was March 31, 1996. The Region's current target closeout date is September 30, 2001.

Although we are not considering this grant as a current candidate for potential deobligation, we believe this 13 year old project could have been managed more effectively. It had many problems since inception and could have been terminated. Regional personnel cite the Consent Decree for not terminating the grant or deobligating the funds. We question whether the Facility will be built or efficiently operated since the Amended Consent Decree deadlines have been modified twice (additional 12 months). As a result, more than \$10 million has been idle since 1988. If construction commences, additional Federal funds due to these delays may be necessary. Meanwhile the Virgin Islands residents have been deprived of adequate wastewater treatment services for 13 years.

Unilateral
Deobligations

EPA's August 21, 1990 Project Acceleration Initiatives stated that when a final payment was made, with the possible exception of set-aside costs involving pending claims, all other monies should be immediately deobligated. The grantee should be notified that set-aside monies remain for a specified period, and if claims are not timely resolved, such funds will be deobligated and the grant closed. Deobligation of set-aside funds can be accomplished by a unilateral amendment.

When the grantee did not take appropriate action, the Region should unilaterally close out the project and deobligate excess funds. This Initiative allows the deobligation of excess funds when grantees do not request timely deobligation action. Grantees should be given adequate notice where unilateral deobligation would be considered and accomplished. Such action would be a last resort to get the grantee to act on projects with significant excess funds. However, Region 2 has been reluctant to use the unilateral deobligation option when projects with large unpaid balances have been significantly delayed. This reluctance is due to the time and effort involved and potential legal ramifications. We believe this is a viable option and should be used when necessary.

Internal Controls

The Federal Managers' Financial Integrity Act (FMFIA) requires that internal control standards be followed when establishing and maintaining internal control systems. The objectives of an internal control system include (1) assets are safeguarded against waste, loss, unauthorized use, and misappropriation, and (2) revenues and expenditures are properly recorded and accounted so that accounts and reliable financial reports may be prepared and accountability of assets maintained. We reviewed internal controls and procedures related to our objectives, but not controls associated with inputting and processing of IFMS and GICS information.

The Region's FY 94, FY 95 and FY 96 FMFIA Assurance Letters did not identify any material weaknesses or vulnerabilities. However, we believe that the Region's inconsistency in deobligating funds was a material weakness in internal controls. OMB Circular A-123 defines a material weakness as a specific instance of noncompliance with FMFIA which would (1) impair the fulfillment of an Agency component's mission; (2) deprive the public of needed services; (3) violate statutory or regulatory requirements; or (4) significantly weaken safeguards against waste, loss, unauthorized use or misappropriation of funds. The Region's failure to timely deobligate unneeded construction grant funds, deprives the public of funds that could be recommitted to other badly needed projects, and improved water quality that these projects would bring. We therefore believe that the Region should include construction grant deobligations as a material weakness in its FY 97 Assurance Letter.

Other Control Weaknesses

1) Lack of Written Procedures

Prior OIG reports and Grants and Water Branch personnel disclosed there were no written Regional procedures

regarding (i) deobligation of funds, (ii) roles and responsibilities of individuals involved in deobligation/closeout activities, (iii) conditional administrative completions, (iv) unilateral terminations, and (v) program office coordination with Finance.

Written procedures evidence practices followed to comply with EPA regulation and policy. They provide management with tools to coordinate and control activities of subordinates and identify and anticipate problem areas. Procedures are also used to evaluate management practices and ascertain the degree in which internal control is exerted over operations. Lack of written procedures could have contributed to the untimely deobligation of funds and other conditions. The lack of written procedures has been a continuing problem. For example, a 1982 OIG Report (21443) recommended that Region 2 implement formal written procedures to ensure funds were promptly deobligated.

2) Higher Priority,
Increased Resources,
Improved Coordination

Region 2 must accelerate its deobligation of unnecessary funds by giving this a higher priority and providing increased resources. Currently, one grant specialist is responsible for various construction grant completion/closeout and deobligation efforts. Although this individual is doing a good job, she needs additional resources to more timely complete

these tasks. We strongly believe that another full time employee (FTE) would provide a great benefit in accelerating the identification and deobligation of idle funds.

The Water Programs Branch has one person responsible for New York grant activities and another person for New Jersey activities. These individuals have conflicting grant responsibilities (including dispute resolution). Although the delegated States have various responsibilities, the two EPA individuals cannot effectively handle all their functions and effectively monitor the States without additional assistance

from other individuals with construction grant knowledge. In addition, the Water Compliance Branch has only 0.4 FTE assigned to direct Caribbean construction grant activities. This individual can not effectively handle the Puerto Rico deobligation area in addition to other activities.

There could be better coordination between the grants specialist and Water Program Branch individuals. The specialist must receive complete and timely closeout and deobligation data from Branch and State officials to timely prepare data to be entered into GICS and IFMS.

As a result of these analyses, Region 2 must give this area a higher priority, provide additional resources, and increase the coordination and cooperation among the Grants and Water Branches.

Conclusion

Four OIG audits of Region 2's construction grant deobligation efforts during the past 15 years disclosed material weaknesses. Based on the Region's promises to take action to correct these weaknesses, the OIG closed out these audits. However, the same conditions found in 1982 continued to surface in 1986, 1990 and 1991. We strongly believe that strong top management efforts are needed to resolve this long-standing problem. It should be noted that Region 2's response to OIG Report E1VW2-02-0029-21443 (August 12, 1982) was **"Please be assured that the Region and the States are pursuing deobligations and terminations more aggressively than ever before."** We do not believe this is the case.

The Region's various control system weaknesses contributed to the conditions noted. Agency policies for expediting deobligations were not followed in the grants we reviewed. If Agency policies had been followed, at least \$63 million of potentially unneeded construction grant funds could have

been deobligated, and an additional \$7.5 million could have been deobligated in a more timely manner.

Regional Response

The Region's September 11, 1997 response to the draft report stated that the approximately \$70 million available for deobligation was misleading. For more than five years New Jersey deobligations were essentially put on hold pending a Headquarters decision regarding Camden and Cape May appeals. This appeal related to deobligation of excess grant funds based on low bid construction costs and affected a number of grantees.

The Region believes projects not having reached administrative completion should not be included in the \$300 million unpaid balance since "excess balances should be deobligated at the administrative completion stage." The response indicated that some New York projects had been recently closed and amounts deobligated. Also, the Region believes there may be as much as \$40 million in "potential" obligations owed to New York grantees based on current disputes and other information.

The response stated that New York grantees may submit their administrative completion package prior to finalized costs (i.e. construction contractor problems). Since the grantee may have more costs to submit, funds are not deobligated. Also, if an appeal is likely, funds are not deobligated since grantees often added additional amounts almost up to closeout. If claims are valid, Region 2 has paid them.

Region 2 does not consider any project to be inactive until all construction, audit and appeals are completed and would not terminate a grant until such time. The Region also does not believe unilateral deobligations are appropriate. In addition, the Region disagreed that construction grant deobligations should be deemed a material weakness since construction grants closeout is already an Agency material weakness.

Regarding recommendations 2-1, 2-3, and 2-5, the Region agreed to conduct a review of all construction grants with unliquidated obligations to determine if any deobligation actions can be taken. Deobligations will be processed as appropriate. Regarding recommendation 2-2 to implement Region policies, the response stated that EPA Headquarters has already issued a grants closeout policy addressing unexpended funds, and unilateral deobligations are inappropriate. The Region believes recommendation 2-4 is unnecessary since meetings are held to discuss "potential project closeouts," and grant dispute issues.

OIG Evaluation

Although we do not believe any statements were misleading, we clarified certain matters in the report. Our review disclosed approximately \$63 million potentially available for deobligation. We also found approximately \$7.5 million (i.e. Wanaque Valley) recently deobligated which could have been accomplished many years earlier. Recent additional deobligations might reduce the \$63 million and increase the \$7.5 million, but the total of \$70 million would remain.

The Region's assertion that New Jersey grant deobligations were on hold pending a Headquarters decision does not deal with our audit results. This issue concerned low bid construction contract deobligation costs. Our audit concerned the Region not deobligating excess funds at the administrative completion stage. Page 3 of the Region's response correctly states that in accordance with EPA's Final Closeout Policy for Assistance Agreements dated August 27, 1992, excess balances (unliquidated obligations) should be deobligated at the administrative completion stage.

The comment on Page 4 of the response regarding New York projects closed out after the audit commenced and \$8.7 million deobligated strengthens the OIG position.

Specifically, six New York and New Jersey grants identified in Exhibit 1 (Irondequoit, Auburn, Westchester, Woodstock, Leroy, and Little Egg Harbor) were closed between February

and June 1997 and \$8.7 million was deobligated. We had identified the specific \$8.7 million for these six grants that should have been deobligated at the administrative completion stage or many years prior to FY 97.

To determine Region 2's construction grant's unpaid balances, we used the IFMS monthly summary report. This shows unpaid balances, and includes pre-administrative completion projects. We recognize that additional reimbursements may be forthcoming. However, we are concerned that the Region does not consider any project to be inactive until all construction work, audits and appeals are completed and therefore would not terminate a grant until such time. The Region must constantly monitor grants unnecessarily delayed where payment requests have not been submitted for many years. Such projects may be candidates for termination or scope changes and could result in deobligation of unneeded funds. Region 2 has previously terminated grants and two current "active" grants are in process of being terminated prior to administrative completion.

Grants can be terminated or annulled if no substantial progress is made without good cause (40 CFR 30.903 through 30.905). Also EPA's policies and procedures require that unneeded funds be deobligated during various stages of completion. For example, the EPA Administrator's November 22, 1982 memorandum to the Regional Administrators discussed deobligation of funds that will not, or need not be spent prior to, during, or after construction was complete. Also, OIG's September 1991 report disclosed \$60 million that could be deobligated for Region 2 construction grants not administratively completed.

Region 2's unique policy of continuously allowing grantees to claim additional Federal funds not previously claimed indicates a weakness in administering construction grants. Continuously allowing grantees to submit costs many years

after administrative completion, the audit process, final determinations, and the appeal process is not a sound management practice and contributes to untimely closeouts.

We disagree with the Region that it is unnecessary to include construction grant deobligations as a material weakness since closeouts are already an Agency material weakness. We strongly believe Region 2 should include deobligations as a material weakness in Assurance Letters and FMFIA reports.

We are pleased that the Region will conduct an overall review of all construction grants to determine if any deobligation actions can be taken. We are also pleased that at the exit conference the Assistant Regional Administrator agreed to carefully review the OIG identified idle funds and deobligate unnecessary funds immediately. However, additional actions are needed to address the OIG concerns. Periodic reviews should be commenced to review completed projects which have not been closed for at least six months, and minimum obligation balances should be estimated to release at least a portion of the unexpended obligations. It is also imperative that specific timeframes for initiation of reviews and determination of actions be established.

Regarding recommendation 2-2, we strongly believe that specific Regional procedures and policies are needed regarding unexpended grant obligations. The Region promised to implement such procedures in response to prior audits. Also, Headquarter's August 27, 1992 Final Closeout Policy for Assistance Agreements emphasized the importance of closing out projects and deobligating unliquidated obligations timely. It requested that Regional Procedures be developed to implement the policy requirements.

We recognize that periodic meetings may discuss project closeout issues. However, these meetings mainly discuss the grants in the dispute process and are not documented. We believe those meetings should be expanded to discuss

unexpended grant balances and areas where funds could be deobligated. These meetings should be documented and distributed to all attendees

Recommendations

We recommend that the Regional Administrator require the Grants and Water Program Branches to:

- 2-1 Evaluate effectiveness of its controls for reviewing unexpended obligations, make necessary changes, and promptly deobligate unneeded funds. Specifically, review grants cited and take necessary actions to deobligate unneeded funds.
- 2-2 Develop and implement specific Regional policies and procedures for reviewing and monitoring unexpended obligations, and determining requirements for deobligating unneeded or idle funds. Also, consider using alternative procedures (i.e. unilateral deobligations) when necessary. These procedures should include project management control reviews to determine whether additional funds could be deobligated from other projects not part of this review.
- 2-3 Consider designating a specific individual to coordinate reviewing open projects and unexpended balances. Special emphasis should be given to projects completed, but not closed for six months.
- 2-4 Initiate and document periodic review meetings between the two Water Branches and Grants personnel to increase monitoring of unexpended construction grant balances. Also, evaluate construction grant fund balances on completed or inactive projects on a semiannual basis.
- 2-5 Estimate minimum obligation balances necessary to expedite the release of unexpended obligations. By

using these estimates, future obligation balances can then be retained and excess funds reprogrammed.

- 2-6 Establish timeframes that will serve as a benchmark for accomplishing the above actions.

CHAPTER 3

INCREASED EMPHASIS NEEDED TO MEET GRANTS COMPLETION/CLOSEOUT STRATEGY

Although Region 2 has made significant progress to reduce its backlog of open construction grants, increased emphasis is still needed. We found that approximately 127 Step 3 projects did not meet the Agency's goal of administratively completing grants by the end of FY 95 or closing out all grants by the end of FY 97. The Region may not close out certain grants by its own projected date of FY 2000. Also, approximately 50 Step 1 and 2 grants will neither meet the Agency's nor Region's targeted closeout dates.

This condition was caused by such factors as the (i) highest priority not always given to project closeouts especially Step 1 and 2 grants, (ii) inadequate level of communication and coordination between program personnel, (iii) incomplete administrative completions which did not accurately represent the grantee's final claim, (iv) duplicate audit requests and OIG screenout process, (v) inconsistent GICS and IFMS data, (vi) turnover of experienced construction grant program personnel, (vii) complexity of the remaining projects, and (viii) lengthy dispute/appeal and final determination processes.

As a result, millions of Federal dollars of unexpended grant amounts remained unnecessarily obligated. These funds could have been used to fund other eligible projects, thereby creating a positive environmental impact. Also, personnel assigned to the closeout process could have been reassigned to new assignments. In addition, the Agency goal to timely close out this program is in jeopardy.

Background and Criteria

The Office of Water's October 1990 Strategy for Closing Out The Construction Grant Program addressed delays, review and approval of plans and specifications, timely change order submission, and the administrative completion process. The Office of Water's January 18, 1991 Project Acceleration Initiatives Work Book reissued policies for expediting grant closeout with operational problems, unresolved claims, and delayed final payment requests.

The Work Book described State actions to ensure grants were administratively completed in a timely manner. One action would withhold payments until administrative completion progress was made; another action would identify the latest date that a final payment request would be accepted. It also suggested a final date be identified for all change orders to be submitted. The Work Book further suggested that States notify grantees that all change orders must be submitted within 90 days of construction completion. Any increased change order costs submitted after this date would not be allowable, except those resulting from meritorious claims.

The recent OIG audit strategy allowed program officials to close many projects without requesting an audit and expedited scheduling and completing necessary audits. EPA's FY 1996 Integrity Act Report stated that Regions and States should develop revised projections consistent with the new OIG audit strategy. The Report also expressed concern about Region 2's slippage in the rate of progress and problems including resolving audit findings and disputes. Therefore, Assistant Administrators will work with Regional counterparts "to increase priority and attention devoted to administrative completions, audit and dispute resolution, and closeouts."

A Joint November 25, 1996 Office of Administration and Resources Management, Office of General Counsel, and Office of Water memorandum requested the Region 2

Administrator's personal attention to completion/closeout of construction grants and accelerate current closeout plans. It stated that a "significant" number of Region 2 projects would not meet the Agency's goals of administratively completing all projects by the end of FY 95 and closing out all grants by the end of FY 97. Region 2 estimated that 127 projects would miss that goal including 51 Puerto Rico projects.

The memorandum indicated Region 2 had one quarter of the nationwide projects which would miss the FY 97 goal. Therefore, the Region "needs to devote more management attention and/or resources" in the water program, grants administration and regional counsel offices where audit resolution, grantee dispute and other closeout work is done. It advised the Region to make use of the OIG's Strategic Plan and to prevent and resolve disputes.

**Region 2 Must
Accelerate Closeouts**

Region 2's Annual Report on Internal Controls dated November 24, 1989 cited the closeout process as a weakness requiring corrective action. The Report stated:

The Agency needs to accelerate the closeout of construction grants projects so that unexpended balances can be redirected to improve environmental protection. Current projections of closeouts into late 1990's will exceed delegated state agencies' ability to manage the closeout process, and opportunities to use grant balances for additional wastewater treatment will be lost.

Region 2's Assurance Letters consistently indicated that particular emphasis was placed on grant closeouts since OMB proposed this material weakness. The Letters stated it "places the highest priority on closing screened out or audited projects so that the deobligated funds can be reallocated for further use." The Region has given construction grant closeouts increased effort. However, additional attention is

required if the Agency's goal of timely closeout is to be realized.

EPA's FY 96 Integrity Report disclosed that 5,860 construction grant projects remained to be closed at the end of FY 90. The Report also noted the number of projects remaining to be closed at the end of FY 94 through 96.

EPA's Post 1997 Construction Grants Closeout Strategy also estimated the pre-92 closeouts remaining at the end of FY 1997 through FY 2000. Our comparison of Region 2's pre-92 closeouts to the nationwide totals showed that from FY 1994 to FY 2000, the Region's percentage of open projects when compared to the nationwide universe **dramatically increased every year from 16 to 52 percent**. This percentage increase was most dramatic for FYs 1997-2000 as illustrated by the following schedule:

<u>Projected Closeouts Remaining</u>			
<u>End of FY</u>	<u>All Regions</u>	<u>Region 2</u>	<u>Percent of Total</u>
1997	503	123	25%
1998	230	84	37%
1999	129	60	47%
2000	60	33	52%

This pattern clearly shows that while other regions have accelerated their grant closeouts, Region 2 has not kept pace. It has to accelerate its closeout of construction grants if the Agency is to attain its goal.

Step 3 Grants New Jersey

We reviewed New York and New Jersey Step 3 closeouts projected for FYs 96 and 97 which were still open as of April 15, 1997. Seven of the 18 New Jersey grants projected for closeout in FY 96 were still open. For two grants

(Camden 708-02 and Cape May 661-07), the Region revised the projected closeout date from FY 96 to FY 98.

The Region had not taken timely action to close out the Camden grant. The OIG issued the final audit report in July 1996 and requested the Region's proposed audit determination by October 1996. As of April 15, 1997 we had not received the Region's determination. On the Cape May project, the grantee's revised final payment request was appealed to NJDEP. The status of the 1995 appeal remained unchanged as of the cut-off date of our review.

For the remaining five grants, the Region's revised targeted closeout date was FY 97. On Neptune Township (410-01) a contributing factor to the revised projection was the delay in issuing the final determination letter (FDL). The draft FDL was submitted to the OIG in February 1996 but not finalized until March 1997. The East Rutherford (296-01) closeout was delayed because project files could not be located. Finally, regarding three Hudson County grants (399-06, 18 and 22), the Region issued its FDL in September 1996 but the grants remained open at the time of our audit cut-off.

For FY 97, 14 of the 19 New Jersey State Specific Strategy grants initially projected for closeout remained open. At the time our field work was finished, it was unlikely that all 14 specific grants would be closed by the end of FY 97. However, other grants projected for a subsequent year closeout might be substituted. The Region's own projections revised six closeout dates to FY 98 or FY 99. Camden (708-09), Stockton (396-01) and Pine Beach (505-03) are estimated to be closed in FY 98. Ocean County (714-04 and 356-01), and Keansburg (583-02) are estimated to be closed in FY 99. It is also unlikely all remaining eight grants will be closed by the end of FY 97. For example, Camden (708-06) and Middlesex (637-01) have been appealed to Headquarters and generally such appeals are not decided expeditiously. Our review of the Region's recent submission disclosed that

nine specific New Jersey grants targeted for FY 97 closeout are now projected for closeout in FY 98 or FY 99.

We also reviewed New York closeouts projected for FYs 96 and 97. For FY 96, only two of the 15 grants projected for closeout were open and were projected for FY 97. The Region's closeout strategy did not indicate any reason for the delay. On the Alexandria grant (1265-02), the strategy assumed the grantee would not appeal the FDL. Our review did not disclose any appeal, therefore there appeared to be no impediment to its timely closeout. We found a similar situation with the other New York City (713-05) grant.

For FY 97, nine of 20 grants projected for closeout were open at the time of our audit cut-off. It is unlikely that all nine would be closed by the end of the fiscal year since the projected date for three grants was revised to FY 98. These grants (Glens Falls 1279-04, Huntington 1040-04 and Tri-Municipal 948-03) were under appeal with a decision expected in FY 97 (no appeal to Headquarters was anticipated). For four New York City grants (392-03, 07, 09 and 10), the OIG's February 1996 audit report requested a Regional response by May 1996, but had not been received by May 31, 1997. The Region's strategy stated the audit would be resolved in 1996. Also, closeout of Whitestown (1194-02) was delayed pending the appeal of the Region's determination. The Region's recent submission indicated eight specific grants open as of September 30, 1997 are now projected for closeout in FY 98.

Puerto Rico and Virgin Islands

During FY 96, Region 2 closed six Puerto Rico and Virgin Islands grants. As of March 1, 1997, Region 2's closeout universe of Puerto Rico and Virgin Island Step 3 grants consisted of 70 projects awarded between 1964 and 1992 (60 were awarded prior to 1990). The targeted closeout dates for the 70 grants range between September 30, 1997 and September 30, 2001 (53 are not expected to meet the Agency's FY 97 closeout date). In fact, 32 projects are not

expected to be closed before FY 2001. The following five grants were awarded more than 10 years ago and are scheduled for closeout in 2001:

<u>Grant #</u>	<u>Award Date</u>	<u>Admin. Complete</u>	<u>Target Closeout</u>	<u>Status</u>
C72121-03	6/30/76	12/20/88	9/30/01	Screened
C72094-13	9/30/80	9/29/92	9/30/01	Screened
C72120-06	9/28/84	12/06/89	9/30/01	Screened
C78013-04	9/30/84	6/30/00	9/30/01	Redesign
C72100-10	9/30/85	3/01/89	9/30/01	Screened

Certain Puerto Rico and Virgin Islands active projects have not proceeded as timely as expected. Currently, 17 pre-1992 projects awarded since 1979 are not administratively complete (unpaid balances exceeding \$30 million) and have been in process for as long as 17 years.

Between FY 93 and FY 96 Region 2 awarded 39 additional construction grants (in excess of \$50 million). Targeted completion dates range between three and five years from the award, and targeted closeout dates between four and seven years. Based on prior experience it is doubtful that these targeted dates will be met.

In fact, the Region's September 12, 1997 status report submitted to Headquarters confirmed that targeted administrative completion and closeout dates had been extended for 30 (77 percent) of the 39 grants from eight months to two years. For example, grant C72122-10 (Sabana Grande) originally planned to be closed on March 30, 2000 has been extended to September 30, 2002. In another example (grant C72086-15-, Arecibo) the original projected closeout date was also shifted two years (from March 30, 1999 to March 30, 2001).

Problems have also surfaced on post-1992 awards which will impede timely completion and closeout. For example, certain

FY 94 and 95 awards have not started construction or contracts not awarded, and bids have not been received or have been cancelled. Regional management and particularly the Water Compliance Branch must give a higher priority and devote additional resources to significantly reduce its project backlog.

**Grants Untimely
Closed Out**

Region 2 did not always close grants in a timely manner. The following is one example.

Caguas 82-01 (82-00) was awarded on December 29, 1972 to construct intercepting sewers, force main pumping stations, and a secondary water pollution control plant. The last payment was made on April 2, 1986 (project was 99% complete) and no action had been taken until January 26, 1994 (8 years later). Also, certain appropriations have been unpaid since 1982. Although, the Region believed the grant would be administratively completed in FY 92, it was not completed until September 30, 1993. At this point the Caribbean Municipal Programs Branch recommended a decrease of \$5,087,634 and a bill for collection (BFC) for \$102,289 (excess amount).

It wasn't until January 26, 1994 (4 months) that the Region initiated Amendment 4 (decreased \$5,087,634) and sent a BFC. The February 2, 1994 audit request was screened out on December 11, 1995. As of April 16, 1997 (more than 16 months since screenout), the grant remained open and \$102,289 had not been deobligated. On April 18, 1997, the Accounting Operations Section Chief acknowledged that \$102,289 should have been deobligated when the 1994 payment was received. The targeted closeout date is September 30, 2000 and the status is "File Search Pending." As a result, this 1972 grant is expected to be closed 28 years later (2000). In addition, OIG's September 1991 report alerted the Region that these idle funds should be deobligated. The response to the draft report indicated the project was closed on June 25, 1997.

Step 1 and 2 Grants

As of April 15, 1997, GICS listed 56 Region 2 Step 1 and 2 construction grants (NY-16, NJ-21, PR-19) awaiting closeout with a Federal share of approximately \$129 million. These grants were awarded between 1974 and 1981 and administratively completed between 1982 and 1994 (53 projects administratively completed prior to March 11, 1991). Region 2 and State officials stated that Step 1 and 2 closeouts were a low priority since emphasis was given to Step 3 grants. GICS indicated New York targeted closeout dates for their 16 projects between 1991 and July 27, 1996. Similar data was not available for New Jersey and Puerto Rico. As a result, a majority of these 56 projects remained open for approximately seven years since administration completion. In addition, more than \$2.5 million was unpaid and potentially available to be deobligated.

As of September 30, 1995, Region 2 reduced its inventory of over 700 projects to 75. Although the Region's FY 96 Assurance Letter had committed to closing the remaining 68 Step 1 and 2 projects by December 31, 1996, 56 projects remain open. Many projects remained open subsequent to September 30, 1997 because certain project files could not be found.

New Jersey Grants

As of April 15, 1997, 21 New Jersey Step 1 and 2 grants awarded between 1973 and 1981 and administratively completed between 1978 and 1990 remained open. Under the delegation agreement NJDEP was responsible for managing grants through the administrative completion stage. Since all Step 1 and 2 grants have reached administrative completion, Region 2 is responsible for all remaining closeout activities.

While Region 2 has missed its goal of closing all Step 1 and 2 grants by December 31, 1996, officials have targeted all remaining grants for closeout during FY 97. Based on the

following status of the 21 grants, we believe it unlikely that all will be closed by the end of the fiscal year.

<u>Status</u>	<u>No. of Grants</u>	<u>Unpaid Obligations</u>
Closeout anticipated by May 31, 1997	5	\$ 0
Status not known	8	27,512
Revised outlay report not submitted	3	39,907
Action needed to close out	3	132,340
Headquarters appeal	2	196,362
Total	<u>21</u>	<u>\$396,121</u>

Although Regional officials are trying to close out five New Jersey grants by May 31, 1997, actions could have been taken much earlier. For example, Evesham (463-01) reached administrative completion on September 30, 1988 (no funds remaining). Regional officials stated that Step 3 closeouts have been their priority, although that would not preclude closing out Step 1 and 2 grants.

Closing all the remaining 16 grants by September 30, 1997 is questionable. Two Camden grants (678-01 and 708-04) were appealed to Headquarters. Three Hudson grants (399-01, 581-01, and 582-01) were delayed because the Region did not impose deadlines to submit revised outlay reports. The status of eight projects could not be provided (Linden-Roselle - 299-02, Patterson - 586-01, Wanaque - 390-01, Wyckoff - 783-01, Hamilton - 383-03, Hudson - 399-04, Rahway - 681-02, and Wayne - 393-05). Certain grant files were missing and additional data will be needed to proceed with closeout. Finally, three grants could be closed (Essex Union - 686-01, Somerset - 529-01, and Cape May - 661-02).

New York
Grants

NYSDEC officials have also stated that Region 2 has given a low priority to closing out Step 1 and 2 projects. NYSDEC's April 7, 1997 memorandum indicated 16 open projects with four that could be closed by the end of FY 97. The remainder

would stay open until related Step 3 disputes get resolved. Also, one project (1167-01) was a PCB grant and no action was required. These grants were awarded between 1976 and 1981 and administratively completed by 1993. The NYSDEC official had no knowledge of Region 2's goal of closing all Step 1 and 2 grants by December 31, 1996 or even by September 30, 1997. He stated this could not be accomplished since several grants were under appeal.

Eight of the remaining 11 grants have been appealed with no indication that they will be resolved before the end of the fiscal year. Three grants also remain open because of related Step 3 grants. A NYSDEC official stated their policy was not to close Step 1 and 2 grants until related Step 3 grants were closed. One indication of the low priority for Step 1 and 2 closeouts was that during FY 96 only three New York projects (same grantee) were closed.

Puerto Rico Grants

Region 2 had 25 open Puerto Rico Step 1 and 2 grants based on February 20, 1997 information given to the OIG. However, on February 25, 1997 (after our audit commenced) the Region closed six projects leaving 19 grants awarded between 1974 and 1980 (all administratively completed prior to March 1991). We recognize that these closeouts were ongoing prior to our review. These Step 1 and 2 grants were given a low closeout priority. In fact, the Region has not provided target closeout dates or even listed these grants in its Closeout Universe sent to Headquarters.

We do not believe that all 19 remaining grants will be closed by the end of this fiscal year since certain files cannot be located. It should be noted that some of these grants have large unpaid balances. For example, San Sebastian (130-02) awarded March 2, 1977 in the amount of \$455,588 has \$211,970 unpaid. Also Mayaquez (120-02) awarded June 28, 1976 in the amount of \$827,324 has \$131,284 unpaid. To expedite the closeout process to get on track with the Agency's goal, the Water Compliance Branch must give

greater priority to closing these grants and deobligating unneeded funds.

The Region's response to the draft report stated that the Step 1 and 2 inventory was reduced to 25 (Puerto Rico - 5, New Jersey - 8 and New York - 12). Also, the Region will develop specific procedures to address the missing files. However, the October 14, 1997 Step 1 and 2 GICS listing shows 30 open projects (Puerto Rico - 6, New Jersey - 11, New York -13). It appears that this error was due to the Region double-counting five grants closed on August 21, and 22, 1997.

During FY 97 the Region closed 39 Step 1 and 2 grants (33 after our audit was initiated). Specifically, all 19 of the PRASA Step 1 and 2 closeouts were completed after February 25, 1997 (almost five months into the FY) and 12 were closed in the last 40 days of the FY. We strongly believe that additional resources directed to closeouts would have and still could expedite the process.

**Duplicate
Audit Requests**

Region 2's inadequate controls over audit requests and screenouts contributed to closeout delays. The Grants Administration Branch (GAB) periodically submitted duplicate (in some cases triplicate) Puerto Rico audit requests to the OIG. The OIG acknowledged each initial audit request.

The following are five examples:

<u>Grantee</u>	<u>Grant#</u>	<u>Dates Submitted</u>
Cayey	118-08	10/28/92 & 10/17/94
Anasco	120-08	10/28/92 & 10/17/94
Bayamon	103-04	4/6/92 & 10/17/94
Santa Rosa	103-12	4/11/94 & 10/17/94
Ricon	100-12	10/28/92 & 4/11/94 & 10/17/94

We also found New Jersey and Puerto Rico audit requests

submitted for grants previously audited or screened out. For example, a June 20, 1994 OIG memorandum to the Chief, GAB discussed the inability to reconcile Puerto Rico grants. It mentioned the San Juan Land Outfall's (96-05) October 23, 1992 audit request that was audited in 1985 (Report 51473 issued September 12, 1985 with \$350,000 questioned costs). After many OIG attempts, the Regional Puerto Rico audit request inventory still does not reconcile with our records.

Region 2's projected closeout submissions to Headquarters consistently listed PRASA grant C72094-12 (Carolina) as pending N8 (originally estimated for June 30, 1997 with a target closeout for January 31, 1998). Its September 12, 1997 submission listed this grant as "abandoned" with a target N8 of June 30, 1998 and closeout for January 31, 1999. The Region previously claimed this grant was administratively complete in 1992 and requested an audit on April 6, 1992. It is currently being audited by the OIG.

Screened Out Projects Remain Open

The OIG has screened out numerous construction grants. The OIG Policy requires audit requests to be screened out within two years except for Mega grantees (i.e. Puerto Rico). All other grantees were either screened out or assigned for audit within this period. The Region must promptly resolve the audit issues and issue an FDL. If the grantee does not dispute the FDL the project should be promptly closed.

When the OIG screened out requests, memoranda were provided to Regional and State personnel identifying specific projects. However, in many instances these screen-out memoranda were lost. Therefore, beginning in 1993 we gave each memorandum a specific State code number so personnel would know which screened out projects were missing. The Region's inadequate control over screen-out memoranda and their untimely submission to Water Branch personnel adversely affected closeouts.

New York,
New Jersey
Screenouts

After an audit request is screened out EPA's August 27, 1992 "Financial Closeout Policy for Assistance Agreements" states that grants should be closed out within six months of the last grant action (i.e. OIG screenout). We judgmentally sampled 14 New York and New Jersey grants screened out between 1994 and 1996 to determine whether they were promptly closed. As illustrated by the schedule below, four of these projects (24 percent) remained open between 25 and 39 months after the screenout dates with \$2.9 million unpaid.

<u>Grantee</u>	<u>Grant No.</u>	<u>Screenout Date</u>	<u>Months Open</u>	<u>Unliquidated Obligations</u>
Suffolk Co.	709-02	1/14/94	39	314,000
Cape May	661-02	3/14/94	37	96,000
Cape May	661-07	3/13/95	25	2,454,000
Rochester	745-03	3/23/95	25	14,000
				<u>\$2,878,000</u>

The last two grants (Cape May and Rochester) have been appealed which would preclude closeout until the issues are resolved. However, Suffolk and Cape May (661-02) are not under appeal and should have been closed within six months of the screenout date rather than remaining open for at least 39 and 37 months. For Cape May, GICS shows a September 25, 1990 administrative completion date, but the audit request was not made until March 13, 1994 (3½ years later).

Although Region 2 closed 10 of the 14 grants sampled, we found that none were closed within the six month period specified in the Headquarters policy. The closeouts ranged between 9 and 35 months from screenout date (average of 23 months). For example, Leroy, NY (735-01) was screened May 5, 1994 and closed February 3, 1997 (35 months later).

Puerto Rico
Screenouts

Although many Puerto Rico audit requests were screened out prior to December 12, 1995, 41 still remain open. Water Branch personnel stated that these projects continue to remain

open because of prior "conditional administrative completions" and missing files. These 41 grants remained open for more than 17 months since OIG screenout and have unpaid funds of approximately \$5 million. For example, the OIG screened out Cayey (118-09) on April 14, 1994. As of April 14, 1997 (36 months) the project remained open.

The Region has not complied with the Financial Closeout Policy that grants should be closed out within six months of the OIG screenout date. Also, many of these screened out projects have large unpaid balances which could be deobligated.

**Conditional
Administrative
Completions**

Region 2 officials claimed that certain administrative completions were "conditional" (not fully complete) and the completion packages did not accurately represent the grantee's final claims. The Region could not determine which grants were conditionally completed. Program officials also stated that no one followed up "conditional" Puerto Rico cases in the OIG inventory. Grants and Water Branch officials indicated "conditional" completions have severely hampered closeout actions. We concur, and believe activities in this area were inconsistent with Agency policy.

Our recently completed Region 1 survey of construction grants disclosed "conditional" administrative completions were effectively handled. When the grantee submitted a conditional final payment, a specific amount was set aside to cover potential reimbursement requests (i.e. litigation). Remaining amounts, less the set aside, were deobligated at the conditional administration completion date. Region 1's "conditional" completions did not impede grant closeouts.

During FY 97, Region 1 also implemented additional closeout/completion procedures. One individual from the Municipal Assistance Unit (Office of Ecosystem Protection) was assigned to coordinate the construction grant phaseout strategy. Monthly meetings instituted with the audit

coordinator, Office of Administration and Resources Management, and program staff discussed all aspects of the phaseout strategy. Subsequent conversations and OIG meetings identified the grant universe and audit request and report dates. Status reports of meetings were distributed to the phaseout strategy team. The Region also provided a management position in the Grants unit, and identified grants management as a concern in their FY 96 Assurance Letter.

We believe Region 2 should consider such an approach to accelerate closeouts.

**GICS
Information**

Although the GICS national database stores historical grant information, the data was not always consistent, correct, and timely updated. GICS and IFMS financial data are not reconciled and officials acknowledge long-standing discrepancies between the two systems. For example, on September 15, 1983, NYSDEC informed Region 2 of grant data discrepancies. The State noted that four of the five discrepancies occurred in EPA financial records rather than GICS. As a result of various discrepancies over the years users cannot rely on the data integrity.

We have constantly informed program personnel of errors in GICS especially incorrect grant listings in the OIG inventory. Although errors have been significantly reduced for New York and New Jersey they still persist for Puerto Rico and the Virgin Islands. For example, on May 14, 1997 we informed Grants personnel of GICS errors in the Puerto Rico OIG universe which still included December 1995 screenouts.

**Other Factors
Affecting Closeouts**

The Region must continue to accelerate its efforts to complete and close out remaining construction grants. To accomplish this task in an effective and timely manner, greater communication and cooperation between the various program offices is necessary. Specifically the grants specialist must receive complete and accurate closeout packages which have been adequately reviewed by the two

Water Branches. Also, additional personnel with construction grant knowledge should be assigned at least on a part-time basis to assist the people currently working in this area. We recognize that some very complex projects remain open in Region 2. However, complex projects are being closed in a timely manner in other EPA regions.

The Region's untimely audit resolution and dispute resolution process significantly affected closeouts. We discuss these issues in Chapter 4 and 5 of this report.

Conclusion

EPA's Post 1997 Construction Grants Closeout Strategy (April 23, 1997) acknowledged that 84 percent of the 5,860 grants open at the end of FY 90 had been closed by FY 96. However, estimates indicate that 498 pre-1992 projects will remain open as of the September 1997 closeout goal date. The number of projected open Region 2 projects (123) represents 25 percent of the nationwide total of 498. Region 2 also estimates 84 grants will be open at the end of FY 98 (37 percent of the Agency universe), 60 at the end of FY 99 (47 percent), and 33 at the end of FY 2000 (52 percent).

Region 2 projected closeout of 62 Step 3 grants in FY 97. As of April 15, 1997, only 24 grants were closed as follows:

	<u>NJ</u>	<u>NY</u>	<u>PR/VI</u>	<u>Total</u>
Projected	15	17	30*	62
Actual	1	7	16	24

However, subsequent to completing our fieldwork, the Region accelerated Step 3 closeouts. As of June 13, 1997, 44 grants were closed (NJ-5, NY-11, PR/VI-28). (29 of 44 closeouts were completed after our audit commenced.) The response to the draft report indicated 54 closeouts as of August 18, 1997.

	<u>NJ</u>	<u>NY</u>	<u>PR/VI</u>	<u>Total</u>
Projected	15	17	31*	63
Actual	10	12	32	54

*The response stated the PR/VI commitment is 32.

To comply with Agency directives, the Region must accelerate closeout of the remaining New York, New Jersey and Puerto Rico Step 1, 2 and 3 grants. Headquarters Final Closeout Policy for Assistance Agreements requires grant closeout within six months of the last grant action. This effort must be given a higher priority, and we as well as Headquarters strongly believe that additional regional resources are needed to expedite the closeout process. Increased cooperation and coordination between the two Water Branches, Grants, and NYSDEC and NJDEP personnel will be needed to meet the Agency's goals.

Regional Response

The response indicated that Headquarters review of Region 2's Closeout Plan concluded that most regions would miss the FY 97 closeout goal, and that Region 2's closeout plan was reasonable. It cited programmatic and external considerations unique to Region 2 including the OIG screen out process, conflicts between allowing grantees to submit additional documents versus the desire to expeditiously resolve the dispute, and specialty law firms.

The Region believes that increases in the inventory of grants awaiting closeout are due to the OIG's reluctance to make a determination on audit criteria. It stated that the OIG abandoned the mega-audit concept in 1995 and new criteria were established (December 11, 1995 memorandum to Region 2).

The response indicated 41 Puerto Rico pre-1992 closeouts remained and the OIG identified 28 of these for audits. Also, the Region noted that the draft report mentioned 14 of 19 New Jersey grants projected for closeout remain open, but

should read "14 out of 15 per the table on page 38." As of July 27, "nine of the 14 had been closed with the remaining five on target for closeout by the end of FY 97."

The Region indicated that additional evaluations of most Puerto Rico "conditional" administrative completions (N8) must be conducted. It is directing resources to review change orders not previously submitted and research issues involving inadequate documentation. The Region is also developing a report to identify conditional administrative completion projects which will be issued to notify program offices of projects needing further action prior to closeout.

The response stated that the Region is on target to meet its FY 97 closeout commitments, and reduced the Step 1 and 2 inventory to 25 projects. Finally, the Region believed it always met/or exceeded its project closeout commitments from FY 93 to FY 96.

Regarding the recommendations, the Region believes dedicating additional resources to grant closeout is not necessary. Also, there is "excellent coordination among those involved in construction grant management," but will develop a strategy addressing missing files. In addition, the Region did not believe it should give a higher priority to closing Step 1 and 2 projects.

OIG Evaluation

Although Region 2 generally met its original or revised commitments, it is very clear that Headquarters expected increased closeouts. Headquarters personnel periodically visited the Region and expressed concerns regarding closeouts. For example, a June 1994 Headquarters Office of Water meeting with Region 2 Water Management and Grants Administration discussed projects in process, administratively completed stage, and resolution and dispute phase.

The official was concerned that the Region would not meet Agency closeout goals. He cited NYSDEC's loss of

qualified staff, large grants under construction, and OIG mega-grantee audits to be resolved. Also, many New Jersey grantees were reluctant to submit final outlay reports and believed they were entitled to additional monies from other grant deobligations. Because of other priorities, excess funds could not be deobligated timely. The official was very concerned with the Region's plan to issue new Puerto Rico grants while Headquarters was trying to close out the program.

On April 15, 1997, a Headquarter's Office of Water official discussed recent Region 2 visits and additional closeout problems. He stated that the Region prematurely entered N8 codes to meet commitments, and these "conditional" administrative completions should have been but were not promptly resolved. He had concerns with PRASA closeouts because of long-standing problems, and the disputes backlog. He did not believe the Region allocated enough personnel to resolve issues and close out grants. He mentioned discussions where Region 2 might detail experienced program personnel to reduce the backlog, but it did not materialize. Finally, he expressed concerns that the recent Region 2 reorganization "knocked everything back a couple of squares" and moving

grant responsibilities into the enforcement area was not helping to close out grants.

The National Program Director's May 27, 1997 memorandum to the Deputy Regional Administrator (DRA) outlined his March 12, 1997 review of Region 2's construction grant program. He stated that it "appears that the New York and New Jersey programs are making steady progress in closing out the old Title II program but will need about three more years to complete the job. Close out plans are dependent on retaining staff expertise . . . and renewed progress in resolving grantee disputes . . ." (emphasis added). He mentioned the accelerated plan to try to close out Puerto

Rico grants by the end of 1999, but it would require "increased resources, management attention, and cooperation from the OIG." Also, the current plans for closing out the program appear reasonable, but he was concerned that responsibility for program closeout is spread across four Regional organizations. Therefore, the Director recommended that the DRA's "personal attention" is needed to assure that the close out plan is achieved. In particular, additional resources may be needed to assure that the Puerto Rico plan is achieved."

The March 12, 1997 trip report mentioned many key concerns:

- Whether the Region has sufficient resources and expertise to meet its close out plan.
- The number of grantee disputes, particularly in New York, which will need to be decided.
- The accelerated plan for Puerto Rico may be difficult to achieve without additional resources.
- The need to get the Commonwealth of Puerto Rico to take necessary steps to meet the latest Regional plan. This will require close management and support.
- The large number of Puerto Rico grant awards since 1991 which will require Region 2's management attention for several years into the future.

A September 29, 1997 discussion, with the Headquarters official noted the Region's recent commitment updates and closeouts. He reiterated prior concerns regarding Puerto Rico conditional completions, and the need for additional Regional resources for closeouts. He was concerned that the recent update showed a slippage of nine projects. He stated the

Region expected 119 projects to miss the FY 97 closeout date, but the update showed 128 projects.

Also, the November 25, 1996 memorandum from the Assistant Administrators for Water, Administration and Resources Management, and General Counsel to the Regional Administrator (RA) expressed closeout concerns. Region 2 needed to devote more management action and resources to construction grant completion/closeouts both to Regional activities and dealings with the States and Corps of Engineers. Also, the Region needed to use the OIG's strategic plan for completing construction grant audits (particularly in Puerto Rico) by the end of FY 98, and more timely resolve disputes. The memorandum requested the RA's "personal attention to completion/closeout of the construction grants program" and to "accelerate current closeout plans."

Based on the Region's response we made appropriate modifications and clarifications. We recognize the Region knew that it would not meet EPA's goal for closeout of all grants by the end of FY 97. Headquarters April 23, 1997 memorandum concluded that most regions would miss the target date for pre-1992 construction grants but Region 2 would have 25 percent (123 grants) of the 503 grants that would remain open (see Section- Region 2 Must Accelerate Closeouts). Therefore, Headquarters officials were highly concerned about the slow pace of Region 2's closeouts.

When the Agency declared Construction Grants Close Out a material management control weakness, the OIG implemented a revised audit strategy that focused on the most vulnerable grants. In December 1995, in line with the OIG strategy, the Eastern Audit Division screened out approximately 40 Puerto Rico projects administratively completed many years earlier. These mega-audit grants were not covered by the two year audit time frame. We do not understand the Region's comment (page 11 of the response),

“As a result, the Region recommended that the OIG prepare a written Policy on the audit criteria for the construction grants program.”

Region 2 may have some unique programmatic and external considerations, but most of their concerns are also found in other regions. The same law firms represent grantees in other regions, and allowing grantee submittal of additional documentation is a nationwide problem. Also, the OIG screen out process and mega-audit concept were used in all regions. Despite all these factors the other Regions showed greater success in grant closeout.

The Region originally projected 58 construction grant closeouts for FY 95. However, its May 1995 mid-year report submitted to the Office of Water significantly reduced this projection to 32 closeouts based on certain factors (i.e. loss of New Jersey records, New York disputes taking longer than anticipated). Another Regional document showed 33 closeout commitments for FY 95.

As previously noted, the individual FY 97 closeout commitments changed. Also, Region 2's Water Management Division's September 21, 1995 memorandum to the Office of Wastewater Management committed 19 New Jersey and 20 New York grants (total of 39) for closeout which is seven more than the number mentioned in the response. However, the August 1996 State Specific Strategy update reduced the previous 39 closeout commitment to 32 (New Jersey reduction of 4, New York reduction of 3 closeouts).

Although the Region met its revised FY 97 commitment for New Jersey and Puerto Rico, it missed it for New York by two closeouts. We noted that 47 of the 62 FY 97 closeouts occurred after our audit commenced and in the last eight months of the year. Also, we do not agree that 41 pre-1992 Puerto Rico projects were awaiting closeout and the OIG identified 28 for audits. In fact, the Region's September 12,

1997 submission to Headquarters indicated 42 pre-1992 Puerto Rico Step 3 grants awaiting closeout and 12 additional ones not administratively complete (total of 54 open grants). In addition, the OIG has not identified 28 grants for audit. The September 12, 1997 submission also erroneously lists 14 Puerto Rico grants in the OIG inventory. Therefore, the Region's contention that it has a "potential universe of only 13 pre-1992 grant awards to be closed out" is incorrect.

The audit report correctly states that as of April 15, 1997, 14 of 19 specific New Jersey grants projected for closeout remain open. Prior projections to Headquarters listed 19 specific New Jersey grants it expected to close during FY 97. As of September 30, 1997, nine specific grants remained open, but substituted grants were closed. However, a subsequent FY 97 projection reduced the commitment to 15 closeouts.

We believe the planned development of a report to identify "conditional" administrative completions would be useful. However, if it had been done five years ago it would have been beneficial in closing grants more timely. For example, while many Puerto Rico "conditional" administrative completions were in the OIG inventory, the Region could have taken further action. Consequently, when screenouts occurred, the Region could have immediately closed them, rather than having them sit idle for additional years.

We are pleased that the Region will develop a strategy addressing the missing files problem. However, specific procedures to address this long standing problem could have been previously developed. We hope that the planned strategy will be timely developed and implemented.

The OIG and EPA Headquarters strongly believe that additional Region 2 resources and efforts are needed to expedite the closeout process. In fact, on September 8, 1997, the Deputy Regional Administrator told OIG Headquarters

personnel that a key reason for the Region 2 backlog of construction grant closeouts was a lack of Regional resources.

Recommendations

We recommend that the Regional Administrator instruct the Grants and Water Branch program offices to review the construction grant completion/closeout strategy and:

- 3-1 Pay closer attention to expediting grant closeouts by providing additional resources. Consider temporarily detailing personnel with construction grant knowledge to help current personnel, and assigning an individual to coordinate program offices activities.
- 3-2 Conduct an evaluation of all open “conditionally” administratively completed grants and determine any pending issues (i.e. change orders). This evaluation should be completed for New York, New Jersey, and Puerto Rico projects. Also, future “conditional” administrative completion issues should be identified and promptly resolved.
- 3-3 Initiate and document regular program office meetings to discuss (i) actions initiated or to be initiated, (ii) specific closeout problems, (iii) projects in OIG inventory, (iv) missing or incomplete files, (v) State activities, (vi) revised targeted dates and justifications, and (vii) OIG audit results. Regular communication and coordination will be beneficial in accelerating closeouts.
- 3-4 Give a higher priority to closing out the remaining Step 1 and 2 grants and deobligate unneeded funds during FY 98.

[This page intentionally left blank.]

CHAPTER 4

AUDIT RESOLUTION PROCESS WAS UNTIMELY

The Region's audit resolution process was untimely. Proposed and final determination letters (FDLs) were issued later than required by Agency guidance. The Region did not follow the required Agency guidance, and did not aggressively pursue resolutions until an audit report was scheduled for the overdue listing in the OIG Semi-Annual Report. The Region also did not give audit resolution a high priority. As a result, a total of \$37,893,378 remained unliquidated longer than it should have. Potentially, all or part of this money could have been reallocated for use on other construction projects thus having an even greater environmental impact.

Criteria

EPA Order 2750, Management of EPA Audit Reports and Follow-up Actions, states in Chapter 4, Resolution of External Audits (Assistance Projects), that the Action Official must issue a final determination within 150 days of the final audit report date for audits with questioned costs below \$100,000; or provide the Divisional Inspector General for Audit a proposed determination within 90 days of the final audit report date for audits with questioned costs equal to or greater than \$100,000. Also, the Director, Grants Administration's August 27, 1992 memorandum, Final Closeout Policy for Assistance Agreements, required regional offices to comply with EPA Order 2750 regarding timely audit resolution.

**Analysis of Resolution
Untimeliness**

During Fiscal Years 1996 and 1997, there were 16 construction grant audit reports (covering 28 grants) issued by the Office of Inspector General (OIG) for which either FDLs were issued or the reports remained unresolved. FDLs were issued for ten reports, only proposed determination letters were sent in three, and no letters were sent in the remaining three. Once proposed determination letters are sent by the Region, the OIG reviews them within a few days and advises the Region of its acceptance or rejection. In most cases, the letters are accepted as written and should not require much time to issue final determination letters. In a few instances, needed revisions are discussed with Regional staff.

The average time for the entire resolution process for these 16 reports, as of May 25, 1997, was 358 days. This amount will increase once all the remaining FDLs are issued. The timeframe range for ten instances with issued FDLs was 161 to 636 days. The timeframe range for the six instances where no FDLs had yet been issued was 104 to 1,116 days.

The delay in the process appeared to occur at both the preparation of the proposed and final determination phases. The average time it took for a proposed letter to be sent to OIG for review was 212 days. The average time between the submission of a proposed letter and the issuance of a final determination letter was 179 days. (See Exhibit 2)

The following are two representative examples of this untimeliness and the magnitude of the related unliquidated obligations:

The OIG issued a report (4300034) on May 4, 1994 for four grants given to the Ocean County Utilities Authority. On September 14, 1995, the Region sent a proposed determination letter to the OIG for review (498 day later).

The OIG concurred with this letter on September 20, 1995. As of May 25, 1997, 618 days passed without an FDL issued. No explanation has been provided for this lapse of time.

There were \$1,721,089 in unliquidated costs associated with these four grants which were lying idle.

The OIG issued report 6100096 on February 5, 1996 for four New York City Department of Environment Protection (NYCDEP) grants for the Oakwood Beach treatment facility. As of May 25, 1997 (475 days), a proposed determination was yet to be sent to the OIG. There were \$15,334,737 in unliquidated costs associated with these four grants.

There were also \$5,468,448 in unliquidated costs for reports where FDLs had been issued. For example, though an FDL was issued on August 26, 1996 to Westchester County (Mamaroneck), there were \$1,653,220 in unliquidated costs still available as of May 25, 1997. No explanation was provided for not deobligating these funds.

The untimeliness issue is not restricted to the past two years. The Region has historically taken much longer than the timeframes cited in EPA Order 2750 to issue FDLs. For example, OIG report 3100374 (September 14, 1993) pertained to six grants awarded to NYCDEP (North River). The Region did not issue its FDL until September 21, 1995, over two years later. While this resolution involved several grants, the response did exemplify the Regional pattern of lengthy time needed to issue an FDL.

In conclusion, the Region's audit resolution process was untimely, both at the proposed and final determination phases, and funds remained idle that could have been more beneficially used for other construction projects.

Regional Response

The Region in its response acknowledged that a number of resolutions took longer than their targeted 180 days but stated that its audit resolution rate compared favorably to other regions. In addition, it provided various factors it believed contributed to the length of the process, including:

- the number, magnitude and complexity (mega audits) of the audits issued;
- the enormous dollar amounts reviewed and questioned;
- the complexities caused by diverse issues raised; and
- only one State (New York) fully delegated and providing proposed audit resolutions.

The Region also noted that two determination letters had recently been issued and two or three more might be issued by September 30, 1997. This will leave only two pending audits, one awaiting State review, and the other for which a determination will be issued in the first quarter of FY 1998.

The Region further stated that it is working to increase the Section 205(g) Management Assistance Grant for New York and New Jersey. The additional funds will maintain a higher level of staffing and assure adequate funding for managing projects up to administrative completion.

Finally, in response to our recommendation, the Region stated it had been reviewing its audit resolution process and was committed to timely audit resolution. It also stated that ORC does not generally participate in the audit resolution process.

OIG Evaluation

Though there is an acknowledgement by the Region that untimeliness does occur, it should be reemphasized that the Region uses a 180 day target. As previously noted, EPA Order 2750 sets 90 or 150 day limits for determination letters. Consequently, Regional resolutions are inherently untimely.

It also should be noted that the presented Regional audit resolution rates are misleading because the data includes all types of audit resolutions and our report deals only with construction grants.

Finally, since ORC personnel only participate in the audit resolution process on a case by case basis, we have modified our recommendation. In addition, we want to reemphasize the second part of the recommendation (which the Region did not address in its response). A higher priority needs to be placed on the timely resolution of audit reports and the deobligation of funds.

Recommendation

We recommend that the Regional Administrator instruct Water Programs Branch and other appropriate personnel to:

- 4-1 Analyze its audit resolution process to determine the bottlenecks that are slowing the process down. In addition, a higher priority needs to be placed on timely resolution of audit reports, and to deobligate funds of \$5,468,448 associated with the 10 issued FDLs.

[This page intentionally left blank.]

CHAPTER 5

LENGTHY DISPUTE/APPEAL PROCESS DELAYED CLOSEOUTS

Region 2 has not always resolved construction grant appeals in a timely manner. Most disputes have lingered in the Office of Regional Counsel (ORC) for many years before decisions were rendered. Initial conferences have not always been scheduled to discuss disputed areas and Water Branch personnel have not prepared timely program memoranda. Also, certain grant dispute files were incomplete and written chronologies of important actions (i.e. meetings and conversations; information requested, received or not received; followup actions) were not always maintained.

This condition was caused by such factors as (i) inadequate resources and emphasis given to the disputes/appeals process, (ii) inadequate communication and coordination between program offices and ORC, (iii) non-compliance with Regional disputes procedures, (iv) manual status report data does not reconcile with computerized tracking system, (v) loss of construction grant expertise, and (vi) grantees represented by speciality law firms.

Untimely resolution of disputes further delay closeout of the award until the action is settled. As a result, some cases have been under appeal for close to 10 years and resolution is still pending. These projects remained open and were reassigned to different attorneys or program personnel. Also, excess funds have not been deobligated. As disputes continue to linger, there may be a tendency to drop certain issues or settle them for amounts less than originally contemplated.

Background

Region 2's Assistance Disputes Procedures dated June 4, 1986 describe the roles and responsibilities of program personnel. ORC is responsible for docketing, monitoring and reporting the status of dispute appeals, and notifying the Assistant Regional Administrator for Policy and Management and the Water Management Division (WMD) of the dispute filing. ORC must also issue bimonthly status reports indicating the appeal date, summary of issues and status, and anticipated date for Regional Administrator's (RA) decision.

According to these procedures, Region 2's goal is to generally resolve each appeal within 120 days of receipt if no informal conference is held, or within 120 days after the date of the conference. The ORC attorney must notify the appellant of the right to an informal conference, and a deadline for receipt of documentary evidence and written argument if no conference is requested. WMD and/or Grants personnel must provide ORC with written comments on the appeal "within 45 days after the informal conference or receipt of the appellant's submission supporting its appeal, whichever is later." Finally, based on WMD's comments, ORC will prepare the recommended decision for the RA.

In August 1992 the Region created two positions currently in the Construction Grants Section of the Water Programs Branch (WPB) to facilitate more timely dispute resolution.

Current Disputes Inventory

Although the Region's written procedures established a goal of 120 days (4 months) to resolve each appeal, this goal was

rarely met. In fact, most open disputes have remained unresolved for more than four years.

During FY 93, 50 disputes/appeals were in the Region's inventory and 18 were resolved, leaving an ending balance of 32 projects. Between FYs 94 and 96, the Region reduced their dispute/appeal inventory to the following 17 projects:

<u>Grantee</u>	<u>Grant #</u>	<u>Date of Appeal</u>	<u>Months in Process (1)</u>
Rockland Co	744-08	05/13/90	85
Rockland Co.	744-02/13	07/10/90	83
Tri-Municipal Co.	948-03	01/12/92	65
Amherst	618-02/03	08/07/92	58
Huntington	040-04	12/09/92	54
Moodna Basin	954-01	01/21/93	53
Rockland Co.	744-09	01/23/93	53
Glens Falls	279-04	03/08/93	51
Niagara Co.	707-02	03/19/93	51
Niagara Co.	707-01	10/20/93	44
Nassau Co.	891-05/12	01/04/95	29
Landis Sewerage	461-02	07/07/95	23
NYCDEP	1100-1/3/4	10/19/95	20
Rockland Co.	744-14	10/18/95	20
Morristown	376-22	04/17/96	14
Nassau Co.	1139-03	06/14/96	12
Wanaque Valley	390-06	10/28/96	7

(1) Date of Appeal to June 1, 1997

Reconsiderations

In addition, to these 17 active disputes, Region 2 also has to resolve 15 Petitions for Reconsideration. These petitions include 13 Nassau County disputes (filed between 1989 and 1992 and resolved between 1992 and 1996) and two Amherst disputes (filed between 1989 and 1990 and resolved in 1992 and 1993).

Resolution of the Nassau County Petitions has been delayed and the Water Management Decision (WMD) memoranda submission dates has been continuously revised, presently showing the targeted date as January 21, 1997. Both Amherst Petitions have seen little Region 2 activity. Since June 1993, ORC status reports for Docket No. 02-89-AD13 indicates ORC is awaiting a response to the grantee and scheduling preliminary discussion with Grants personnel. Regarding Docket No. 02-90-AD26 the next action is Awaiting WMD. Therefore, Region 2 has 32 active disputes and requests for reconsiderations in its inventory. This total does not include disputes resolved by the Region, but subsequently appealed to Headquarters where they have lingered for many years (i.e. Ocean County 372-03, Camden County 708-04).

NYSDEC Concerns

Region 2's untimely resolutions have affected delegated State activities. For example, NYSDEC's Deputy Commissioner's February 24, 1987 letter to Region 2's Deputy Administrator stated that its Grants personnel historically presumed that Regional disputes would be settled within a year and those reaching Headquarters within a second year. However, some "larger issues have been under appeal since the late 1980s and were to be resolved as long as five years ago." Of the 20 projects with appeals pending some will be owed additional funds, and others might result in substantial recoveries. Continuing delays have made it almost impossible to estimate project increases/decreases and closeouts.

NYSDEC has committed 17 and 18 Step 3 closeouts in FYs 97 and 98 and another 21 over the following three years (17 Step 1 and 2 projects also remain). However, NYSDEC must reduce Grants staff from eight persons to three. Thus, closeout projections cannot be met when disputes are not settled, and reduced staff cannot handle an increased workload. The Deputy Commissioner concluded "it is imperative that EPA give a high priority to rendering appeals decisions." Region 2 concurred that numerous appeals

present a problem to EPA and NYSDEC in managing funds and staffing needed to close the construction grants.

Status Reports

Program offices have not always complied with Regional Assistance Dispute Procedures. Although the procedures require ORC to issue bimonthly status reports indicating information and target dates, reports were not always issued on a bimonthly basis and were discontinued in October 1996. They were replaced by a Disputes Resolution Schedule prepared by Water Programs Branch (Construction Grants Section). Although the Schedule provides targeted action dates, it is virtually useless because most information was eliminated. Also, targeted dates were constantly revised and commitments were rarely met. ORC personnel advised that due to untimely decision memoranda from the Construction Grants Section, the planned effort for construction grant appeals has accordingly been reduced by 50 percent.

Until recently Status Reports were periodically submitted. These reports provided the date of appeal, attorney and program contact persons, grant number, audit report number, disputed amount, issues, current status, and targeted action dates. Our review of the December 1, 1994 to October 17, 1996 reports and ORC files disclosed limited activity to bring projects to timely closure. For example:

Rockland County (No. 02-90-AD13) - The July 10, 1990 appeal involved cost allocation issues. An informal conference was held on October 11, 1991 (15 months after appeal was filed) and additional documentation was provided. All status reports listed the Next Action as "Awaiting WMD Review." On March 15, 1993 WMD issued a technical memorandum for one grant involved. On November 20, 1996 the Water Programs Branch issued another memorandum for the same grant. The review of the second grant was targeted for December 1996. The appeal has not been resolved as of May 1, 1997 (almost seven years)

and the latest targeted date of January 30, 1997 has not been met.

Rockland County (No. 02-90-AD17) - The appeal was filed on May 13, 1990 and the December 1, 1994 status report indicated that the informal meeting was held in April 1991. However, the grantee's attorney's March 15, 1993 letter informed ORC that an informal conference had never been scheduled. Also, the letter indicated it was unlikely that the appeal would be resolved until the summer of 1993. The issues were similar to the above dispute and the Next Action for all the status reports was "Awaiting WMD Review." The appeal has not been resolved as of May 1, 1997 (seven years) and the latest target date of March 30, 1997 has not been met.

Tri-Municipal (No. 02-92-AD06) - The appeal was filed on January 12, 1992. Each of the status reports stated that additional information was received on March 30, 1994 and ORC was awaiting WMD's determination since that date. The appeal has not been resolved and is targeted for FY 98.

We found many other examples of untimely dispute-appeal resolutions (See Exhibit 3 for details).

Untimely Program Memoranda

Progress could not be made to resolve grantee disputes until Water Branch (formerly WMD) personnel provided a detailed program memorandum which adequately outlined all issues. ORC personnel and status reports have indicated that untimely memoranda have significantly contributed to delayed resolutions. Water Branch personnel acknowledged that due to other priorities, this area was not given enough attention.

Although ORC has overall responsibility for resolving disputes, in actuality the process is controlled by the Grants and Water program offices. Since most disputes involve

technical areas, construction grant program personnel must review the disputed areas and provide ORC with a technical memorandum of their review results. After receiving the memorandum, ORC can prepare the dispute decision for the RA's approval. ORC expressed frustration with the program personnel's failure to meet their commitments for providing adequate technical decision memoranda.

One example where untimely and continuously revised technical memoranda delayed resolution was Nassau County (02-90-AD03). On January 19, 1990 the grantee appealed the Region's final determination and an informal conference was held on March 14, 1990. ORC could not proceed until WMD prepared a technical memorandum. WMD did not prepare the memorandum until June 16, 1994 (almost 4½ years since the appeal). Between June and December 1994, ORC messages to WMD requested additional information, explanations, clarifications, and corrections. For example, a December 14, 1994 message stated "we need to maintain consistency with the DDO decision unless we have a reason to revise it. Let me know what the correct numbers are. Unfortunately, these issues are delaying finalizing this document."

On December 15, 1994 ORC wanted additional discrepancies explained and on December 22, 1994 a revised technical memorandum was sent to ORC. Between December 1994 and April 1995 additional clarifications were necessary and ORC's frustration was clearly evident with such statements as "He finally provided me with a copy of his revised memo", "I found another far reaching mathematical error in the revision", "I have attached my millionth draft of this decision", "Here is the trillionth draft of 361-01", and "The December 22nd version changes everything but administrative costs." Finally, the RA decision was issued on April 20, 1995 (more than five years since the appeal).

Other Factors

No Informal Conferences or Chronological Logs

Our review of ORC files and discussions with appropriate personnel disclosed that informal conferences had not been held for many disputes. ORC personnel believed that holding informal conferences would be a waste of time if Water Branch personnel did not followup with a timely and complete program memorandum. We recognize that untimely program memoranda was the main factor for delayed resolutions, but believe timely informal conferences should have been scheduled to clarify the disputed issues.

In many instances ORC personnel did not maintain complete and organized files or chronological logs showing dates of important actions, meetings, conversations, requests and/or receipt of grantee or Water Branch information. Although this did not materially offset the delays, we believe that complete and organized files are necessary to assure that ORC and program personnel effectively monitored the individual projects. Also, complete files would be necessary if the matter went to trial.

Status Report Reconciliation with Adtracs

Status report information did not always reconcile with the ORC tracking system (Adtracs). For example, the FY 97 Disputes Resolution Schedule as of October 17, 1996 listed 16 disputes while Adtracs listed 19 disputes. Also, the date of the appeal differed between the two systems. For example:

	<u>Adtracs</u>	<u>Status Reports</u>
Rockland County (02-90-AD17)	5/3/90	5/13/90
Tri-Municipal (02-92-AD06)	1/23/92	1/12/92
Rockland County (02-93-AD02)	2/22/93	1/23/93
Niagara County (02-93-AD04)	3/22/93	3/19/93
Rockland County (02-95-AD05)	10/19/95	10/18/95

Adtracs also did not account for the 15 reconsideration cases returned to Region 2 for resolution. When they were returned to the Region, the attorney should have completed a form for the revised information to be input into the system.

**Loss of Experienced
Personnel and Specialty
Law Firms**

As resolutions linger in the dispute process they become more difficult to resolve. Over the years personnel with construction grant expertise have left the Agency or been reassigned to other areas. The current cases have been reassigned to different attorneys or program personnel. When a case is transferred, the new individual must review the files and get up to speed on the specific matters. In some cases, inadequate or incomplete case files have delayed this process.

Another factor causing delays are the specialty law firms that represent some grantees. These firms are very knowledgeable of the construction grant regulations, and Regional officials spend considerable effort in analyzing each point under consideration. Although these same firms represent grantees located in other regions, those disputes have been generally resolved in a more timely manner than in Region 2.

Regional Response

The response noted numerous factors contributing to the Region's lengthy disputes/appeals process, and grantees have been given every opportunity to submit additional information to support these claims. Also, ORC and WPB agreed that disputes were not progressing as expected and ORC had little control over WPB production of memoranda. Therefore, it was inefficient for ORC to maintain bi-monthly status reports containing the required information.

The response indicated that the Adtracs system could not accommodate disputes before the Region for reconsideration. However, ORC will inquire whether Adtracs can be revised to accommodate this information, and will continue to

include reconsideration cases in the bimonthly status report. The Region believed it has made considerable progress in reducing its disputes, and will review the current inventory to determine whether these can be resolved more expeditiously.

OIG Evaluation

We acknowledge the factors contributing to timely resolution of disputes/appeals and the increased number of resolutions between 1993 and 1996. However, more needs to be done to eliminate the backlog as well as new disputes that will arise in the future. We are pleased that the issuance of the bimonthly status reports will be resumed showing all cases (including reconsiderations). This will allow management to monitor cases that are not moving to closure as expected.

Regarding our recommendation to implement a plan to accelerate the dispute resolution process, review of the current inventory to determine which can be resolved expeditiously is a good first step. However, after the review is completed, an action plan with commitment deadlines should be initiated outlining responsibilities for both offices.

Recommendation

We recommend that the Regional Administrator instruct ORC and Water Programs Branch personnel to:

- 5-1 Implement a joint plan to accelerate the dispute resolution process. This effort must contain a greater commitment by both offices to eliminate the case backlog. Increased Water Branch actions are clearly needed to provide complete and timely program memoranda, and dates can not be constantly revised. In addition, ORC must initiate timely informal conferences, maintain adequate files with chronological logs of actions, and adequately document all meetings and conversations.

NEW YORK
SCHEDULE OF UNLIQUIDATED BALANCES

EXHIBIT I
PAGE 1/3

		Award	Adm. Compl	Last Payment		Cumulative	Unliquidated	Potential	N8 Date To
Grantee	Grant #	Date	(N8) Date	Date	Grant Amt	Payments	Balance	Deobligation	May 1, 1997
							Per IFMS		(MONTHS)
NYCDEP (Oakwood)	C360392-07	09/30/87	09/27/95	05/26/94	\$80,247,971	\$65,554,320	\$14,693,651	\$13,224,286	19
NYCDEP (North River)	C361100-03	09/28/79	07/26/94	08/31/94	\$227,821,362	\$206,739,260	\$21,082,102	\$13,295,704	33
NYCDEP (North River)	C361100-04	09/30/80	06/30/93	12/26/91	\$272,598,442	\$250,226,309	\$22,372,133	\$5,381,646	46
IronDeQuit Bay	C360500-01	12/10/69	09/30/96	01/06/97	\$40,388,685	\$35,583,622	\$4,805,063	\$4,805,063	7
Rochester PWD	C360715-02	07/29/77	12/09/93	09/23/93	\$23,851,289	\$21,313,674	\$2,537,615	\$2,400,257	40
Rochester PWD	C360745-03	06/30/81	03/31/93	02/07/97	\$139,893,635	\$139,879,364	\$14,271	\$14,271	49
Nassau Co	C360891-09	09/30/80	06/29/87	04/14/94	\$7,582,258	\$4,305,607	\$3,276,651	\$3,137,150	118
Auburn (Step 2)	C360972-01	12/21/76	06/30/88	09/03/86	\$1,154,161	\$88,296	\$1,065,865	\$1,065,865	106
Suffolk Co	C3601036-03	09/30/77	02/09/96	07/10/96	\$20,556,460	\$16,596,278	\$3,960,182	\$3,960,182	14
Town of Amherst	C360618-03	06/30/75	06/09/89	09/29/89	\$7,761,719	\$5,831,092	\$1,930,627	N/A	94
Westchester Co	C360908-06	09/30/88	09/12/96	09/19/94	\$66,958,888	\$65,305,668	\$1,653,220	\$1,653,220	7
Clinton Co	C361171-02	09/08/83	N/A	10/15/96	\$23,526,782	\$22,883,768	\$643,014	N/A	
Glens Falls	C361279-04	09/30/84	02/23/90	11/20/91	\$15,286,854	\$14,830,839	\$456,015	N/A	86
Woodstock	C360799-04	09/30/81	12/31/92	10/16/96	\$10,136,774	\$9,688,431	\$448,343	\$448,343	52
Leroy	C360735-01	05/16/75	07/31/92	05/21/93	\$959,196	\$674,244	\$284,952	\$284,952	57
Totals					\$938,724,476	\$859,500,772	\$79,223,704	\$49,670,939	
Average months delayed									52

NEW JERSEY
SCHEDULE OF UNLIQUIDATED BALANCES

EXHIBIT 1
PAGE 2/3

							Unliquidated			N8 Date To
			Admin Compl	Last Pymt		Cumulative	Balance	Potential	Delayed	May 1, 1997
Grantee	Grant #	Award Date	Date (N8)	Date	Grant Amt	Outlays	Per IFMS	Deobligatio n	Deobligatio n	(MONTHS)
Bernards S.A.	C340382-01	09/30/81	08/18/87	03/18/88	\$13,577,213	\$12,575,718	\$1,001,495	\$729,620	\$0	116
Parsippany	C340587-02	05/07/76	09/28/88	08/17/88	\$9,108,502	\$8,302,210	\$806,292	\$806,292	\$0	103
Middlesex County	C340637-01	08/30/76	07/19/89	06/13/94	\$77,232,210	\$76,738,248	\$493,962	\$0	\$0	93
Cape May County	C340661-07	12/28/84	09/28/90	03/07/95	\$28,628,685	\$26,174,857	\$2,453,828	\$2,282,828	\$0	78
Ocean County	C340372-03	05/27/76	10/09/90	12/05/91	\$48,086,604	\$46,804,856	\$1,281,748	\$968,349	\$0	79
Little Egg Harbor	C340579-02	06/30/81	03/31/97	04/21/88	\$1,263,894	\$949,725	\$314,169	\$314,169	\$0	108
Pine Beach	C340505-03	09/30/82	12/31/86	10/01/84	\$2,203,388	\$1,605,660	\$597,728	\$597,728	\$0	151
Keansburg MUA	C340583-02	09/30/82	12/19/88	01/01/89	\$5,965,394	\$5,573,670	\$391,724	\$391,724	\$0	100
Bridgewater TWP	C340638-02	09/30/80	N/A	10/18/96	\$9,294,644	\$8,424,125	\$870,519	\$0	\$0	
Perth Amboy	C340435-02	09/26/85	N/A	01/10/91	\$3,211,243	\$250,310	\$2,960,933	\$2,960,933	\$0	
Wanaque	C340434-01	09/30/80	12/84	12/10/84	\$3,663,600	\$3,663,600	\$0	\$0	\$656,392	112
TOTALS					\$202,235,377	\$191,062,979	\$11,172,398	\$9,051,643	\$656,392	
Average months delayed										104

**PUERTO RICO
SCHEDULE OF UNLIQUIDATED BALANCES**

**EXHIBIT I
PAGE 3/3**

			Admin Compl	Last Pymt		Cumulative	Unliquidated			N8 Date To
Grantee	Grant #	Award Date	Date (N8)	Date	Grant Amt	Outlays	Balance Per IFMS	Potential Deobligation	Delayed Deobligation	May 1, 1997 (MONTHS)
Puerto Nuevo	C720096-06-02	06/30/80	09/21/84	05/05/91	\$14,514,864	\$14,078,813	\$436,051	\$436,051	\$0	151
San Antonio Comm.	C720102-11-1	09/29/88	12/29/92	10/23/91	\$1,400,860	\$1,145,144	\$255,716	\$255,716	\$0	52
Anasco Trunk Sewer	C720120-08	03/09/87	09/29/92	05/21/94	\$5,004,626	\$2,062,457	\$2,942,169	\$2,942,169	\$0	55
Camuy Hatillo	C720126-08-02	09/07/83	09/29/92	03/24/94	\$1,374,987	\$1,151,923	\$223,064	\$223,064	\$0	55
Botijas	C720200-02-1	09/30/80	05/07/96	07/13/93	\$100,448	\$100,448	\$0	\$0	\$1,714,017	42
Caguas	C720082-01/00	12/29/72	09/30/93	04/02/86	\$5,100,280	\$4,997,991	\$102,289	\$102,289	\$5,087,634	132
Carolina	C720094-12	09/29/79	06/30/97	06/01/83	\$4,968,332	\$4,722,159	\$246,173	\$246,173	\$0	133
SUBTOTAL					\$32,464,397	\$28,258,935	\$4,205,462	\$4,205,462	\$6,801,651	
				VIRGIN ISLANDS						
Dept. of Public Works	C780013-04	09/28/84		02/10/88	\$11,134,058	\$1,052,710	\$10,081,348	*	*	
Gov't of Virgin Islands	C780025-01	09/29/89		07/15/96	\$7,933,657	\$1,764,325	\$6,169,332			
SUBTOTAL					\$19,067,715	\$2,817,035	\$16,250,680			
TOTALS					\$51,532,112	\$31,075,970	\$20,456,142	\$4,205,462	\$6,801,651	
Average months delayed										89

		ALL CONSTRUCTION GRANTS EITHER with FDLs						Page 1/3
		ISSUED IN FYs 96 and 97 or STILL UNRESOLVED						
		(AS OF MAY 25, 1997)						
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)
				Proposed		Final		
			Final Report	Determination	Days to	Determination	Days to	Total Days
Grantee	Report No.	Grant Number	Date	Date	Issue (e-d)	Date	Issue (g-e)	to Issue
Ocean County UA	4300034	C340372-03	5/4/94	9/14/95	498	not issued	618*	1116*
		C340372-08						
		C340356-01						
		C340371-01						
Neptune SA	5100407	C340410-01	7/10/95	11/30/95	143	3/28/97	493	636
Rochester PWD	7100010	C360715-02	10/15/96	2/20/97	128	3/25/97	33	161
New York City - Oakwood Beach	6100096	C360392-03	2/5/96	not issued	475*	not issued	475*	475*
		C360392-07						
		C360392-09						
		C360392-10						
PRASA - Bayamon	6100102	C720103-03	2/5/96	5/20/97	470	not issued	5*	475*
Camden County MUA	6100255	C340708-02	7/25/96	not issued	304*	not issued	304*	304*
		C340708-09						

		ALL CONSTRUCTION GRANTS EITHER with FDLs						Page 2/3
		ISSUED IN FYs 96 and 97 or STILL UNRESOLVED						
		(AS OF MAY 25, 1997)						
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)
				Proposed		Final		
			Final Report	Determination	Days to	Determination	Days to	Total Days
Grantee	Report No.	Grant Number	Date	Date	Issue (e-d)	Date	Issue (g-e)	to Issue
New York City -	7100111	C360402-03	2/10/97	not issued	104*	not issued	104*	104*
Owls Head		C360402-04						
Suffolk County	7100091	C361036-02	1/9/97	5/20/97	131	not issued	5*	136*
Hudson County UA	5100231	C340399-05	3/28/95	9/25/95	181	9/4/96	345	526
		C340399-06						
		C340399-18						
		C340399-22						
Westchester County -	6100076	C360908-06	12/6/95	3/12/96	97	8/27/96	168	265
Mamaroneck								
Wanaque Valley RSA	6100127	C340390-06	3/11/96	9/19/96	192	9/30/96	10	203
Monroe Township MUA	5300032	C340423-01	9/18/95	2/29/96	164	6/28/96	120	284
		C340423-02						

		ALL CONSTRUCTION GRANTS EITHER with FDLs						Page 3/3
		ISSUED IN FYs 96 and 97 or STILL UNRESOLVED						
		(AS OF MAY 25, 1997)						
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)
				Proposed			Final	
		Final Report		Determination	Days to	Determination	Days to	Total Days
Grantee	Report No.	Grant Number	Date	Date	Issue (e-d)	Date	Issue (g-e)	to Issue
Gibbsboro	5100404	C340871-01	7/10/95	10/31/95	113	3/29/96	150	263
Morristown	5100410	C340376-02	7/10/95	11/13/95	126	2/20/96	99	225
Johnstown/Gloversville	5200020	C360878-03	6/15/95	10/16/95	123	2/12/96	119	242
Liverpool Pump Station	5100270	C361200-05	4/10/95	8/31/95	143	2/12/96	165	308
* As of 5/25/97								

ADDITIONAL EXAMPLES OF UNTIMELY
DISPUTE/APPEAL RESOLUTIONS

1. Amherst (No. 02-92-AD13) - The August 7, 1992 appeal regarded execution of change orders and other issues. The grantee requested and received an extension to the early December 1992 to submit its request for review of the July 17, 1992 determination. On December 9, 1992 the grantee's attorney submitted a detailed Request for Review and a prompt informal conference. Our review of ORC's files and discussions with the attorney in charge did not disclose any actions since December 1992, not even an informal conference. All status reports noted ORC was awaiting WMD's memorandum. Action dates were revised from FY 95 to 96 to 97 to 98. The appeal has not been resolved and the revised target date is FY 98.
2. Town of Huntington (No. 02-92-AD19) - The appeal was filed on December 9, 1992. An informal conference was held on March 16, 1993 and documentation submitted. Status reports from December 1, 1994 to the present indicated revised dates for WMD's memorandum. On December 1, 1994 WMD revised its submission date to no later than (NLT) July 30, 1995 and the RA decision during FY 96. On January 3, 1994, ORC informed the grantee that it was "currently handling a large backlog of disputes." Therefore, "we are unable to properly review and evaluate the information submitted", but will handle the appeal expeditiously. On December 23, 1994, ORC again informed the grantee that its decision will "be issued no later than September 30, 1996, but we will make every effort to issue it late in 1995 or early in 1996. In early 1995 EPA's letter assured the grantee that the decision will be issued ASAP. Subsequent reports continued to revise WMD's submission to August 30, 1995, June 30, 1996, August 30, 1996, and finally August 15, 1997. The RA decision date was also revised. No memoranda has been received to date.
3. Moodna Basin (No. 02-93-AD01) - The appeal was filed on January 21, 1993, and an initial conference was not held. However, a recent Water Branch schedule lists an April 15, 1993 informal conference. WMD's schedule for document submission was constantly revised from NLT May 30, 1995, August 30, 1995, May 30, 1996, FY 97 and currently FY 98. The RA determination was revised to FY 98.

-
4. Glen Falls (No. 02-93-AD03) - The appeal was filed on March 8, 1993 and on April 5, 1993 ORC acknowledged receipt. Status reports from 1994 to October 1996 state an informal entrance conference will be held during FY 95. As of January 1997 no informal conference has been held. The WMD submission of its technical memorandum and the RA decision has been continually revised from May 1995 to September 1998.
 5. Niagara (No. 02-93-AD04) - The appeal was filed on March 19, 1993 and documentation was received in May 1993. WMD constantly revised dates for submitting their memorandum from FY 96 to 98. The RA decision was also revised from FY 96 to 98. There has not been an informal conference to date.
 6. Niagara (No. 02-93-AD09) - The appeal was filed on October 20, 1993 and documentation was submitted. The last action was a January 24, 1994 grantee letter requesting a meeting to clarify issues. WMD's dates for memorandum submission were revised from September 30, 1995, to FY 97 and finally FY 98. The RA decision was similarly revised from FY 96 to FY 98. There has not been an informal conference to date.

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
REGION II

DATE: SEP 11 1997

SUBJECT: Draft Audit of Region II's
Deobligation and Closeout of Construction Grants
Draft Audit No. E1FWF7-02-0011

FROM: Herbert Barrack 
Assistant Regional Administrator for Policy and Management

TO: Paul D. McKechnie
Divisional Inspector General for Audit
Eastern Division

Region II's detailed response to the above-referenced Office of Inspector General (OIG) draft audit dated July 3, 1997 is provided in the attachment to this memorandum. This is a significant audit and our response reflects our careful review and consideration of all of the comments and recommendations made by your office. In general, we believe the report fails to recognize the unique circumstances in Region II that have impacted the construction grants closeout program. In particular, the report ignores the number and complexity of the grants awarded in this region, the huge dollar value of these grants, and the fact that grants continued to be awarded in Puerto Rico after 1992 thus continuing to add to the inventory of grants needing closeout. Additionally, the report fails to discuss the delay in closeouts caused by the OIG holding projects in its audit inventory beyond its own policy for a two-year timeframe for screening out projects.

As was made clear during the course of the audit, but was not reflected in the report, Region II has a closeout strategy in place that has been approved by EPA's Office of Water, and we have consistently met or exceeded our annual closeout commitments for each of the past four years. We are continuing to implement this strategy and to effectively monitor the status of all grants awaiting closeout. The Agency has acknowledged that its initial FY 1997 goal (which is cited in this report) for closeout of all grants could not be met. Our strategy is consistent with the overall Agency approach, but by failing to acknowledge this, the report lacks a critical context for its discussion of Region II's closeout program.

With respect to the OIG's comments on the lack of timely deobligations of funds, we have identified a number of factual and interpretive areas where we disagree with the statements made in the report. We plan, however, in partnership with our delegated states, to conduct a review of all construction grants with unliquidated balances to determine if any deobligation actions can be taken. Additionally, we have identified progress made in the audit resolution process and in reducing the inventory of audits under appeal. We will look at these two components of the overall closeout program to see if further progress can be made.

I would like to thank your office for accommodating our request to extend the response date for this draft audit. If you have any questions, please let me know or have your staff contact Scott Opis, Policy, Planning and Evaluation Branch, at (212) 637-3699.

Attachments

cc: Herb Maletz, OIG

**Region II Response to Draft Audit of
Region II's Deobligation and Closeout of Construction Grants**

Chapter 1 - Introduction

Background Section (page 1)

- The description of how the construction grants program works does not include information on the range of activities carried out by EPA. Additionally, statements in the report imply that the States manage most of the day-to-day administrative duties in Puerto Rico and the Virgin Islands. This should be modified to reflect the fact that the construction grants programs in Puerto Rico and the Virgin Islands are not fully delegated.
- The report notes on page 2 that EPA's closeout policy calls for excess balances to be deobligated at administrative completion. In New Jersey however, deobligation of excess balances upon administrative completion has been precluded by a provision in the New Jersey State Priority System since fiscal year (FY) 1982, which calls for a one-time adjustment of the grant amount, up or down, as soon as bids are received based on the low bid construction cost.

This policy of certifying only one grant amendment after the initial award eliminated increases for construction cost overruns, i.e., change orders, which occur in all projects. Thus, the "excess balances" referred to by OIG represent the only contingent funds available for change orders unless underruns in other line items (e.g., engineering, legal, administrative) result in unexpended dollars. In the event an EPA audit disallowed any previously reimbursed costs, eligible change orders could then be claimed, where needed, to substitute for the ineligible amounts.

As the results of an audit are unknown until a final determination letter is issued, the Region can never know at the time of administrative completion how much the grantee's final claim may need to be increased. Grantee appeals of State or EPA audits also extend these uncertainties. It is only after the final audit and appeal processes are complete that unliquidated obligations can be positively identified.

- The second paragraph on page 4 should be modified to reflect the fact that the 1,086 grants and \$2 billion identified as remaining open at the end of FY 1996 are national numbers. Further, the report should provide the specific value of grants awarded in Region II and the current correct amount of unliquidated balances that are not associated

with active, ongoing projects.

Scope and Methodology Section (page 6)

- Although the OIG characterized the Puerto Rico and Virgin Islands grants as problematic, it failed to contact representatives of U.S. Army Corps of Engineers (USACE) during the course of the audit. We believe that such consultation with USACE would have added balance to the review since the USACE is a major participant in the administration of the construction grants program in the Caribbean.
- The OIG describes on page 6 that its review focused on grants with the largest unliquidated balances. However, the OIG does not use a consistent nor clear definition of unliquidated balances. For example, the OIG defines balances on both active construction projects and administratively complete projects as "unliquidated." We believe that balances for active projects should not be classified as unliquidated because they are not available for deobligation. Their inclusion by the OIG gives an inaccurate view of the status of deobligation activity in Region II.
- In its December 11, 1995 screen-out memorandum (regarding Puerto Rico construction grants), the OIG asked EPA Region II to ensure that all outstanding issues were resolved before proceeding with grant closeout. We are working to meet the OIG's request, and we believe that this report should be modified to reflect that the Region must now conduct additional evaluations of most, if not all, previously rendered conditional administrative completions (N8) of Puerto Rico Aqueduct and Sewer Authority (PRASA) grants. To accomplish this, we are directing resources to review change orders that may not have been submitted at the time of the N8, and to research issues involving inadequate documentation to ensure that PRASA can be reimbursed for eligible costs.
- On the last line of page 6, WPD should read WPB.

Chapter 2 - Improvements Needed in Timely Deobligation of Construction Grant Funds

On page 9 of the report, the OIG states "We identified more than \$63 million that was unpaid, and not timely deobligated. In addition, approximately \$7.5 million of recently deobligated amounts could have been accomplished many years earlier." These statements are misleading since they imply that approximately \$70 million was available for deobligation. Our information indicates that this is not the case (see discussion on unpaid balances below).

The OIG also states on page 9 that "such funds (\$70.5 million) could have been used for State administration of construction grant and special appropriation projects." Legislation for the use of Title II deobligations for State administration of construction grants has not been continuously in place. Specific language permitting the use of deobligated funds for State administration of special appropriation grants was not provided until passage of the FY 1997 Appropriations Act. Therefore this statement is misleading.

Also on page 9, the OIG states "The Region's failure to deobligate unneeded construction grant funds has been a continuous problem since 1982." For more than five years, deobligations of New Jersey construction grants were essentially put on hold pending a final EPA Headquarters decision on appeals by the Camden and Cape May County Municipal Utilities Authorities. These Authorities objected to the provisions in the New Jersey Department of Environmental Protection's (NJDEP) priority system which required deobligation of excess grant funds based on the low bid construction cost. This practice affected a number of grantees with a combined total of nearly \$25 million in deobligations proposed by NJDEP.

Region II concurred with NJDEP on this matter in a March 23, 1988 decision. However, the Region was obliged to suspend all such grant decrease actions until EPA Headquarters completed its review (see memorandum dated September 25, 1991). This proved to be the proper course of action because the final decision on May 29, 1992 declared that grant funds representing the federal share of allowable costs incurred within the scope of a project may not be deobligated.

Unpaid Balances Remained Unobligated Section (pages 11-12)

- It is not clear what data sources were used for the OIG's analysis of "Region 2's open construction grants with unpaid balances," nor is it clear which grants comprise the 159 projects reviewed by the OIG. We believe that the information in the report misrepresents the status of unpaid obligations in the Region. For example, projects which have not yet reached the administrative completion stage should not be included in the \$300 million total indicated in the chart on page 11 of the report. In accordance with EPA's Final Closeout Policy for Assistance Agreements dated August 27, 1992, excess balances (unliquidated obligations) should be deobligated at the administrative completion stage.

Prior to administrative completion the project is still active, meaning construction is still

taking place and therefore costs are still being incurred. Furthermore, one year after initiation of operation of the treatment facility, the grantee must certify to EPA that the facility is meeting project performance standards. Only then can EPA take any action to deobligate funds and refer the grant to the OIG for audit.

- \$57 million characterized by the OIG as unpaid balances is being used for active ongoing projects in the Caribbean. The chart on page 11 distorts this situation. For example, the chart identifies 75 projects in Puerto Rico and 5 projects in the Virgin Islands that have unpaid balances. Although all of the monies awarded under the grants may not have been paid out, 38 of the identified projects were awarded in 1992 or thereafter. These 38 Puerto Rico projects, which are under construction, account for over \$41 million in unliquidated balances. Further, two of the five Virgin Islands projects are also under construction and those two active projects account for an additional \$16 million in unliquidated balances. Of the three remaining Virgin Islands' projects, one was administratively completed on September 30, 1996 with no outstanding balance, one is due to complete construction during FY 1997, and the third was recently let for bid.
- The OIG stated "We also found that in four of these grants more than \$7.5 million were recently deobligated that had been lying idle for substantial periods.... Therefore, approximately 60 percent of the unpaid balances reviewed were potentially deobligable." We believe that the OIG should provide information on the methodology used to calculate the 60 percent potentially deobligable figure because the numbers used in the report are misleading and confusing.
- The OIG identifies \$63 million of potential de-obligations for 26 of 35 grants it reviewed. However, the OIG lists the Virgin Islands grants as being both included and excluded from that figure. The OIG should clarify this statement to avoid confusion.
- Although the OIG cites several projects which may be potentially deobligated, Region II staff had previously reported that some of the New York projects identified had already been closed out and therefore should not have been included in the analysis (please see attached list). These eight projects, which were administratively complete and had no outstanding appeals, provided a total of \$8,712,882 in deobligated funds.
- It should be emphasized that New York State is a fully delegated State program and that EPA Headquarters has accepted the Region/State Specific Strategy for grant closeout. Most of the projects appearing on the OIG's list have already been scheduled for closeout by the New York State Department of Environmental Conservation (NYSDEC).
- Moreover, a review of New York State (NYS) projects, which constitute \$49 million of the \$63 million the OIG found not timely deobligated, indicated that there are \$40 million in potential obligations. Thus, the \$63 million should be reduced by \$40 million due to the potential obligations in NYS. A breakdown of the \$49 million identified by the OIG is as follows:

\$13 million could be deobligated by the end of FY 1997
23 million is associated with grants which are under appeal
13 million is awaiting audit resolution
\$49 million total

However, associated with the above are \$40 million in potential deobligations:

- ▶ Associated with the \$23 million awaiting appeal resolution, should the grantees win all of their disputed costs, the total obligations would be \$30 million; and
 - ▶ Associated with the \$13 million awaiting audit resolution, based on information from the NYSDEC and should there be no appeal of these audit resolutions, only \$2.4 million will be available for deobligation. Consequently, the remaining obligated funds would be \$10 million.
- The following description of the administrative completion, audit and appeal processes, provides an understanding of the impact of deobligation issues for grants in New York State that the draft audit report fails to include:
- ▶ Administrative completion process: NYSDEC has grantees submit their administrative completion package prior to finalized costs if there are construction contractor related problems. This is consistent with the memorandum dated October 15, 1984 from the EPA Office of Water. Projects are then placed in the audit inventory while any outstanding issues are being resolved. In these cases, the grantee may have more costs to submit and, therefore, NYSDEC and EPA do not deobligate funds.
 - ▶ Audit and appeal process: Once the audit is issued, NYSDEC and EPA are often aware whether an appeal by the grantee is likely and, if so, funds are not deobligated. Grantees' comments on draft audit reports, usually contained in the final audit reports, often indicate whether the grantee will file an appeal. Uncertainty regarding the excess of the grant amount over the final payment request continues throughout the audit and appeal processes. Grantees have often added previously uncited amounts to their final claim almost up until closeout, and where these claims are found to be valid, Region II has paid them. For example, years after filing its initial appeals, Nassau County, New York is adding some \$4 million to its claim for Y-fittings.
- Most of the New Jersey projects listed in Exhibit 1, attached to the draft report, have already been scheduled and accepted by EPA Headquarters for closeout in FY 1997 or FY 1998. We also question why the Wanaque Valley Regional Sewer Authority (WVRSA) project appears on the list because there is no unliquidated balance for this grant. As background, Headquarters had negotiated a payment settlement on USEPA Bill for Collection (BFC) which allowed WVRSA to repay its BFC within 10 years from the issue date. The BFC expires in 1998. Until such time as the BFC has been satisfied, EPA cannot begin to process the closeout. It should also be noted that all of the unliquidated

obligations were deobligated, resulting in a zero unliquidated balance. As stated in Amendment No. 3 to this project (i.e., C340434-01-3; attached), "Since a negotiated settlement was reached to collect a debt owed to EPA on this project, the amount being deobligated reflects all of the unliquidated obligations which appear in the grant. Therefore, once the debt is collected by EPA, the project will then be closed out."

- For Puerto Rico, the Region previously reported projects identified in this report as having been closed out. The remaining projects listed are identified in the Grants Information Control System (GICS) as active grants (i.e., projects that are still under construction or have not reached administrative completion). To date, the Region has closed out 10 Puerto Rico construction grant projects on the OIG's list. A total of \$3,073,711 in unliquidated obligations associated with these projects was deobligated.
- The OIG Report states that the grant specialist must receive complete and timely closeout and deobligation data from Branch officials. For the program in NY, closeout and deobligation data are provided by the NYSDEC, not the Water Programs Branch.

Examples of Untimely Deobligation Section (page 14)

- City of Auburn 972-01: The OIG implies that the Region failed to deobligate funds from this grant in a timely manner after the last payment was made to the grantee in 1986. Quoting the OIG's report, "However, it wasn't until February 27, 1997 (after our audit started) that \$1,065,865 was deobligated (more than 10 years since the last payment)." Deobligation of funds from this grant was not based upon the "last payment" because the last payment was not the final payment. In addition, the fact that the grant was closed out on February 10, 1997, had been reported to the OIG prior to the issuance of the draft audit report. It should also be noted that the Region received NYSDEC's certification for the grant decrease on December 16, 1996. The Region initiated the deobligation/closeout action on January 3, 1997, and it was signed by the Regional Administrator on February 10, 1997.
- PRASA - Anasco Trunk Sewer 72-120-08: This project was closed out on July 9, 1997, which had been reported to the OIG prior to the issuance of the draft report. The information provided by the OIG on this project is confusing. Further, the OIG statement that the project has been unpaid for ten years is misleading. For example, it should be noted that the OIG held this project in its audit inventory from September 1992 to December 1995.

The report should be revised to present a accurate chronology and evaluation of this project. We recommend the following substitution: (1) the grant was awarded in March 1982 for \$2,941,870; (2) a grant decrease of \$905,503 was processed in September 1992 after the project was administratively complete (this brought the project amount down to \$2,062,457); and (3) an audit was timely requested and the project was screened out by

the OIG on December 11, 1995. When the grant was closed out on July 10, 1997, only \$299 in unliquidated balances remained to be deobligated.

Inactive Projects Section (page 15)

- The OIG seems to determine inactive status based on payment activity, which is not a good indicator of activity for a grant. For example, in some instances we have withheld payment from a grantee due to some noncompliance issues. In other cases, there are special programmatic conditions which may limit the amount of funds released dependent upon achievement of certain milestones. In addition, IFMS and GICS do not reflect the details of noncompliance issues that often affect payments to the grantees. Region II does not consider any project to be inactive until all construction work, audits and appeals are completed and therefore would not terminate a grant until such time.
- With respect to unilateral deobligations, in most cases funds are held in a grant pending audit resolution or appeal. Therefore, Region II does not believe that unilateral deobligations in advance of final agency action are appropriate.
- The OIG points to a Federal Highway Administration Directive as an example to EPA for taking action on "inactive projects." We do not believe that this analogy is appropriate because it is EPA policies and directives that are pertinent to the Region's activities.
- Mangrove Lagoon Project: The OIG characterizes the Mangrove Lagoon project grant as being inactive. Although the OIG attempts to explain the complex history of the project, the chronology does not recognize that the Region requested an investigation of the Virgin Islands Department of Public Works (VIDPW) and the consultant selected for the planning and design of the project. Further, the report does not provide information on how the length of the investigation contributed to the overall delay nor does it specify how the review assured the protection of federal grant funds (i.e., the investigation identified problems that ultimately resulted in the consultant being debarred). Nor does the report portray an accurate and complete picture of EPA-initiated enforcement actions. We believe that the Mangrove Lagoon project should not be considered as a candidate for potential deobligation since this project has been under Consent Order and the Region continues to monitor its status. Therefore, the Mangrove Lagoon project should not be considered in the comparison analysis of potential deobligations and unpaid balances shown on page 12.

In the last paragraph on page 16, the OIG states that "We believe this 13 year old project could have been managed more effectively. It had many problems since inception and should have been terminated." We disagree with the OIG's conclusion since termination of this grant would have deprived Virgin Island residents of adequate wastewater treatment services. Even if the grant were to be terminated, the recovered monies would revert back to the Virgin Islands for use in the development of other wastewater projects.

- The OIG also fails to recognize that the Virgin Islands experienced several major hurricanes during the 1980's and 1990's which resulted in construction delays. Although we realize that the delays are not all attributable to hurricanes and that VIDPW is ultimately responsible for completion of the projects, the report should be modified to distinguish when EPA is required to deobligate unused monies and when such actions may not be appropriate.

Internal Controls Section (page 18)

- The Region disagrees that there are no written procedures regarding deobligation and/or closeout of construction grants. On August 27, 1992, the agency published its Final Closeout Policy for Assistance Agreements, which includes guidance for construction grants closeouts. With respect to the statement that Region II should include construction grants as a material weakness, the Region feels that it is unnecessary since the construction grants closeout is already identified as an agency material weakness. Based on this, the Region reports progress in this area in the annual assurance letter and other FMFIA reports.

In addition, the Region follows the Handbook of Procedures for the Construction Grant Program and the Delegations Agreements for the States of New Jersey and New York. Copies of these documents were available to the OIG during the audit.

Resources, Coordination and Priorities Section (page 19)

- Although current resources dedicated to the closeout of the construction grants program are an issue, the Region has and will continue to effectively implement its strategy to complete and close out the program expeditiously. The Region has submitted to EPA Headquarters its completion/closeout strategy which has been accepted by the Office of Wastewater Management, and we are on target to meet our fiscal year commitments under this strategy.

The following are actual closeouts completed as of August 18, 1997:

	<u>New Jersey</u>	<u>New York</u>	<u>Puerto Rico/ Virgin Islands</u>
Committed	15	17	31
Completed	10	12	32

- The OIG states on page 19 that "This grants specialist also must have better cooperation and coordination with the two Water Program Branch individuals. She must receive complete and timely closeout and deobligation data from Branch officials to timely prepare

documents and date to be entered into GICS and IFMS.” We believe this statement has no place in the report and should be deleted.

- The OIG states “...the Water Compliance Branch has only 0.4 FTE assigned to all Caribbean construction grant activities. This part-time individual can not effectively handle the Puerto Rico deobligation area.” This statement should be clarified since the person working on the closeout initiative is not part-time. A more accurate characterization would be a notation that indicates that approximately 0.4 FTEs are being used to support direct construction grants activities. In addition, the report fails to acknowledge that there are activities other than closeout that are funded under the construction grants management program element.
- In this section, the OIG stresses the need for the Region to increase staff resources dedicated to construction grants program. However, the 1998 resource model shows the Region taking a net decrease in FTEs for that program element.

OIG Recommendations (pages 20-21)

“We recommend that the Regional Administrator require the Grants and Water Program Branches to:

- 2-1 Evaluate the effectiveness of its controls for reviewing unexpended obligations, make necessary changes, and promptly deobligate unneeded funds. Specifically, review grants cited and take necessary actions to deobligate unneeded funds.
- 2-2 Develop and implement specific Regional policies and procedures for reviewing and monitoring unexpended grant obligations, and determining requirements for deobligating or reprogramming unneeded or idle funds. Also, consider using alternative procedures such as unilateral deobligations. These procedures should include project management control reviews similar to the one we completed to determine whether additional funds could be deobligated from other projects not part of this review.
- 2-3 Consider designating a specific individual to coordinate reviewing open projects and unexpended balances. Special emphasis should be given to projects completed, but not closed for six months.
- 2-4 Initiate periodic review meetings between the two Water Branches and Grants personnel to increase monitoring of unexpended construction grant balances. Also, evaluate construction grant fund balances on completed or inactive projects on a semiannual basis. These meetings or evaluations should be documented.

- 2-5 Estimate minimum obligation balances necessary to expedite the release of unexpended obligations. By using these estimates, future obligation balances can then be retained and excess funds reprogrammed.”

Region II Response to Recommendations

- 2-1 The Region will conduct a review of all construction grants with unliquidated obligations to determine if any deobligation actions can be taken.
- 2-2 EPA has already issued a grants closeout policy addressing unexpended funds. As discussed above, the Region’s position is that unilateral deobligations are inappropriate given the complex nature of the program.
- 2-3 As stated above for 2-1, the Region will conduct a review of all grants with unliquidated obligations.
- 2-4 Program office and Grants and Contracts Management Branch (GCMB) staff meet periodically (i.e., quarterly) to discuss potential project closeouts. This effort includes a review of the status of the various grants in the inventory. In addition, meetings are held to review issues related to grants that are in the appeals and disputes process.
- 2-5 As stated above for 2-1, this will be covered in the review of grants with unliquidated obligations. Deobligations will be processed as appropriate.

Chapter 3 - Increased Emphasis Needed to Meet Grants Completion/Closeout Strategy

In FY 1991, EPA's strategy for completing the construction grants program was issued. It established the goals of administrative completion by the end of FY 1995 and closeout of all grants by the end of FY 1997. When Region II developed its initial strategy, the Region was aware that it would not meet the FY 1997 goal, and the strategy clearly acknowledged this fact.

The OIG suggests that increased emphasis is needed to meet the grant completion/closeout strategy. However, EPA Headquarters review of Region II's Closeout Plan concluded that most Regions would miss the FY 1997 closeout goal, and that given the number of grants remaining open in Region II, the closeout plan was reasonable.

The OIG does not comment on various programmatic and other external considerations, some of which are unique to Region II, that contribute to the long time period from administrative completion to project closeout. Among these are:

- OIG's screen out process: The increases in the inventory of grants awaiting closeout are due to the OIG's reluctance to make a determination on audit criteria. For years, the OIG had a "mega-audit" concept in mind, which involved handling several grant audits under a single report. The mega-audit approach was finally implemented in some States, such as New York and New Jersey, in 1993. The OIG later abandoned the mega-audit approach in 1995 and established new criteria in a memorandum to Region II dated December 11, 1995. In that same memorandum, the OIG screened out approximately 40 Puerto Rico Step 3 projects, which fell under the "mega-audit" concept. These same projects remained in the OIG's inventory well over the two-year time frame stated in its audit criteria. As a result, the Region recommended that the OIG prepare a written Policy on the audit criteria for the construction grants program.
- There is an inherent conflict between allowing the grantee to submit additional and/or new documents to support its claim versus the desire to expeditiously resolve the dispute.
- The use of specialty law firms by large grantees for appeals and reconsiderations. These firms often present new arguments on old issues, and raise arguments on issues which were not previously appealed.

For example, the audit resolutions for 19 Nassau County, New York grants disallowed about 4% of the total \$469 million claimed. Based on Nassau County's appeals and the resultant Regional Administrator Determinations, the difference was reduced to about 1.5%. However, when Nassau County's specialty law firm filed for reconsideration, the disputed amount rose to between 9% and 13% of the total amount claimed. Clearly, responses to these specialty law firms' arguments are resource intensive.

The report fails to acknowledge (as noted elsewhere in this response) that the Region is on target to meet its FY 1997 closeout commitments. We have also reduced the inventory of Step 1 and Step 2 projects to a minimum. This inventory now includes five projects remaining for Puerto Rico, eight projects remaining for New Jersey and twelve New York projects, all of which will be closed out once audit issues associated with related Step 3 projects are resolved.

Region 2 Must Accelerate Closeouts Section (page 24)

- The OIG states that "EPA's FY 1996 Integrity Report provided construction grant information and disclosed that 5860 projects remained to be closed at the end of FY 1990." The report should be changed or clarified to give the specific number of projects awaiting closeout in Region II.
- In addition, we believe the report should be modified to differentiate between the universe of pre-1992 grants awaiting closeout and projects awarded after 1992. For Puerto Rico, there are 41 pre-1992 projects awaiting closeout. Of these 28 have been identified by the OIG as projects that will be audited thus leaving a potential universe of only 13 pre-1992 grant awards to be closed out. Should the OIG timely complete audits or screen out additional projects, the universe of 13 "ready" could increase. Further, the report fails to provide information on how the OIG's lack of timely audit/screen out decisions hampered the Region's ability to expeditiously close out grants. Nor does it indicate that delays in OIG audit decision-making caused the Region to continuously revise its list of target grants for closeout to meet commitments.

Step 3 Grants Section (page 25)

The following should be considered:

- New Jersey: Projects are closely monitored by the Region to identify projects which are ready for closeout. Projects identified as "ready for closeout" are included in the Region's annual commitment for closeouts. In the event problems arise relating to projects that were originally slated for closeout, those projects are replaced with other projects.
- New York: New York has a fully delegated program. Therefore, the Region's commitments for New York State construction grant closeouts are based on NYSDEC's recommendations and knowledge of which projects are actually ready for closeout.
- Puerto Rico: The FY 1997 commitment of 32 projects will be exceeded by one project.
- On page 25, the OIG states "...the Region's percentage of open projects when compared to the nationwide universe dramatically increased every year from 16 to 52 percent. This percentage increase was most dramatic for FYs 1997-2000." This information is

misleading because the report does not recognize that 38 grants were awarded to Puerto Rico during the period from 1994 to 1996. In light of this, the chart presenting information on "Projected Closeouts Remaining" should be changed.

- On Page 26, the three Hudson County grants mentioned had no funds remaining to deobligate. Full grant amounts were paid out before audit.
- On page 26, middle paragraph, the OIG states that for FY 1997, 14 of 19 New Jersey grants projected for closeout remain open. We presume this should have read 14 out of 15, as per the table on page 38. The OIG further predicts that it is unlikely that 14 more would be closed out by the end of FY 1997, attributing this conclusion to "prior experience" (page 38). We disagree with these conclusions. As of July 27, nine of the 14 had been closed out with the remaining five on target for closeout by the end of FY 1997. To achieve this, grants whose closeouts were postponed were replaced with others whose closeouts were advanced.

Puerto Rico and Virgin Islands Section (page 27)

- Although we understand the need for the OIG to take a snapshot of the regional closeout inventory, we believe that a March 1, 1997 cutoff date was premature. For example, the OIG provides a table which identifies eight grants awarded over ten years ago. Of the eight grants, all but one have been administratively completed. Three of the grants identified on that table were closed out in June 1997. In addition, all of these grants, with the exception of the Mangrove Lagoon grant, were held open by the OIG awaiting screen out. It should also be noted that the seven PRASA grants listed accounted for only \$322,655 in unliquidated balances. We recommend that the OIG change the table to present an accurate picture of all the relevant facts.
- The OIG statement that "Based on prior experience we do not believe these targeted dates will be accomplished" should be removed from the report since this statement is based on the OIG's conjecture (see above comments as well). The OIG fails to note that the Region is closely monitoring the status of these projects and has received satisfactory justification for project delays by PRASA. Although this information was previously provided to the OIG, it is not incorporated into this report.

Grant Untimely Closed Out Section (page 28)

- PRASA-Caguas 72-82-01: This project was closed out on June 25, 1997. Region II was not able to close out the grant until the Bill for Collection (BFC) for \$102,289 had been paid by the grantee. A total of \$5,087,634 was deobligated from this grant on January 19, 1994.

Step 1 and 2 Grants Section (page 29)

- The amount of \$129 million cited for grants awaiting closeout is misleading because this amount does not represent unliquidated obligations nor unpaid balances appearing in any of the outstanding Step 1 and Step 2 project inventories. If this amount is cited, the Region believes it should be clearly defined as the total project amount (Federal share). As discussed above, Region II has a firm handle on the Step 1 and Step 2 projects for all States. The one issue remaining is the closeout of projects with missing files. The Region will develop specific procedures to address the missing file problem, and is aware of previous OIG decisions on this issue.
- On page 31, the OIG states "Region 2 had 25 open Puerto Rico Step 1 and 2 grants based on information given to the OIG on February 20, 1997. However, on February 25, 1997 (after our audit commenced) the Region closed six projects leaving 19 grants remaining awarded between 1974 and 1980 (all administratively completed prior to March 1991)." It appears that the OIG is implying that the Region only closed out these 6 projects after learning of the OIG's decision to review closeouts/deobligations. We take exception to this statement. These closeouts were ongoing prior to the notification of the OIG review. Rather than being overly critical of the Region's efforts, the OIG should report that Region II is addressing Step 1 and Step 2 projects concurrently with the closeout of Step 3 projects.

Duplicate Audit Requests Section (page 32)

- The Region believes that this issue is inappropriate to include in this audit, especially in light of the fact that the Region has worked closely with OIG staff to reconcile audit request inventories. This issue has been satisfactorily addressed in the past.

Screened Out Projects Remain Open Section (pages 32-33)

- Region II has closed out most of its inventory of projects that have been screened out and did not have any pending appeals or other outstanding audit-related issues. The remaining projects have some unique problems which need to be resolved prior to closeout.

Conditional Administrative Completion (page 34)

- The Region is currently developing a report that will identify projects having conditional administrative completion (N8) codes and will issue this report on a periodic basis to notify the program office of projects needing further action prior to grant closeout.

GICS and IFMS Section (pages 35-36)

- We suggest that this section be deleted. Although there are some deficiencies in GICS, the information is updated in GICS as grants are awarded.
- With respect to the differences in closeout dates found in GICS and IFMS, please note that IFMS does not contain closeout dates. For example, based on a review of the IFMS records for grant number 399-05, Hudson County, it is apparent that the date the OIG is using as the "closeout date" in IFMS is actually the date the last deobligation was posted in the system (i.e., February 28, 1997). The deobligation action was actually signed by the Regional Administrator on February 4, 1997, which is the date reflected in GICS.
- With respect to WVRSA, grant number 434-01, the final deobligation action was completed on May 13, 1994 and posted in IFMS on May 18, 1994. As discussed under Chapter 2, EPA Headquarters had negotiated a payment settlement on a BFC which allowed WVRSA to pay it within 10 years from the issue date. The BFC expires in 1998. Until such time as the BFC has been satisfied, EPA cannot begin to process the closeout for this grant. It should also be noted that all of the unliquidated obligations were deobligated, resulting in a zero unliquidated balance. As stated in Amendment No. 3 (i.e., C340434-01-3, attached), "Since a negotiated settlement was reached to collect a debt owed to EPA on this project, the amount being deobligated reflects all of the unliquidated obligations which appear in the grant. Therefore, once the debt is collected by EPA, the project will then be closed out."
- On Page 37, the OIG states that "Specifically, the grant specialist must receive complete and accurate closeout packages from the two Water Branches." Closeout packages are not forwarded from the two Water Branches. For New York State, NYSDEC prepares the closeout packages, for New Jersey, the grants specialist does the complete preparation.
- Again, as noted elsewhere in these comments, the Region has historically either met or exceeded its annual commitment for project closeouts as follows:

<u>Fiscal Year</u>	<u>Target</u>	<u>Actual</u>
1993	79	80
1994	74	79
1995	32	32
1996	38	42

The report should acknowledge this fact.

OIG Recommendation (page 39)

"We recommend that the Regional Administrator instruct the Grants and Water Branch programs offices to review the construction grant completion/closeout strategy and:

- 3-1 Determine the additional resources or actions needed to expedite the process. Consider temporarily detailing personnel with construction grant knowledge to help current personnel and assigning an individual to coordinate program offices activities.
- 3-2 Initiate regular program meetings to discuss (i) actions initiated or to be initiated, (ii) specific closeout problems, (iii) projects in OIG inventory, (iv) missing or incomplete files, (v) State activities, (vi) revised targeted dates and justifications, and (vii) OIG audit results. Regular, communications and coordination will be beneficial in accelerating closeouts.
- 3-3 Give a higher priority to more timely closing out the remaining Step 1 and 2 grants and deobligate unneeded funds."

Region II Response to Recommendations

- 3-1 Since the Region is on target to meet its FY 1997 closeout commitments, the dedication of additional resources to our grant completion/closeout strategy is not necessary.
- 3-2 The Region feels that there is already excellent coordination among those involved in construction grant management. As discussed above, the Region will develop a strategy addressing missing files.
- 3-3 We have reduced the inventory of Step 1 and Step 2 projects to a minimum. This inventory now includes five projects remaining for Puerto Rico, eight projects remaining for New Jersey and twelve New York projects, all of which will be closed out once audit issues associated with related Step 3 projects are resolved.

Chapter 4 - Audit Resolution Process was Untimely

The OIG report concludes that Region II's audit resolution process is untimely. While we acknowledge that a number of resolutions have taken longer than the targeted 180 days, our audit resolution rate compares favorably to that of other Regions, as reported semiannually to the Congress. Attachment I shows the total number of audit resolutions outstanding for more than 180-days for each EPA Region and the entire Agency for the past five years. The figures reported for Region II for each period in the semi-annual reports from 1992-1997 represent the following percentages of the Agency-wide total of outstanding audit resolutions:

<u>Fiscal</u> <u>Year</u>	<u>Spring</u>	<u>Fall</u>
1992	3%	7%
1993	5%	4%
1994	3%	6%
1995	2%	2%
1996	3%	4%
1997	4%	6% <i>projected</i>

In addition, the following factors, which contribute to the length of the audit resolution process in Region II, should be recognized in the report:

- the number, magnitude and complexity (mega audits) of the audits issued to Region II;
- the enormous dollar amounts reviewed and questioned in Region II audits;
- the complexities caused by the diverse issues raised in each audit; and
- only one State (New York) is fully delegated and provides proposed audit resolutions.

The above notwithstanding, the report should be updated to reflect that the backlog of audits has been reduced with the issuance of determination letters for Oakwood Beach and PRASA-Bayamon, and the anticipated resolution of two (possibly three) additional audits by September 30, 1997. This will leave only two pending audits, one of which (NYC-Coney Island) is awaiting NYSDEC review, and the other for which a determination will be issued in the first quarter of FY 1998.

The OIG also should note that Region II is working with NYSDEC to increase the State's Section 205(g) Management Assistance Grant from its original request of \$800,000 to \$1.1 million. The additional funds are needed to enable the NYSDEC to maintain a higher level of staffing than originally requested because of the additional work created by specialty law firms. The State's formal request, dated April 23, 1997, was submitted during the survey phase of OIG's evaluation. New Jersey has also requested an increase of \$1.68 million for its 205(g) grant. These additional funds will assure adequate funding of its delegated role of managing projects up to administrative completion through FY 2000.

OIG Recommendation (page 42)

"We recommend that the Regional Administrator instruct ORC and Water Programs Branch personnel to analyze its audit resolution process to determine the bottlenecks that are slowing the process down. In addition, a higher priority needs to be placed on timely resolution of audit reports, and to deobligate funds of \$5,468,448 associated with the 10 issued FDLs."

Region II Response

Region II has been reviewing its audit resolution process and is committed to timely resolution of audits. It is for this reason that we have reduced our backlog, as discussed above. The OIG includes the Office of Regional Counsel (ORC) in its recommendation regarding analysis of the audit resolution process. In general, ORC does not participate in the audit resolution process.

Chapter 5 - Lengthy Disputes/Appeal Process Delayed Closeouts

- The report fails to acknowledge that in August 1992 the Region created two disputes positions in the program division to facilitate more timely resolution (currently these positions are in the Construction Grants Section in the Water Programs Branch). Since that date, 51 disputes have been resolved, 17 remain to be resolved.
- There are numerous factors that contribute to the lengthy disputes/appeal process. Among these is EPA's policy to ensure that all grantees have been given every opportunity to submit additional information to support their claims. On page 46, the OIG lists the "months in process" to resolve appeals. This list does not take into account grantee requests to submit additional information. For example, at a meeting held in December 1993, Rockland County asked that all of its projects currently under review, be put on hold while the County determined the applicability to each grant of its proposed alternate system for direct and indirect costs. It was not until a May 1996 meeting (even though their study was submitted to the Region a year earlier) that the County confirmed the grants to which the direct and indirect cost issues applied. Additional information on some of the grants was also submitted at that time.
- On page 45, the OIG states "ORC must also issue bimonthly status reports indicating the appeal date, summary of issues and status and anticipated date for Regional Administrator's (RA) decision." On page 47, the report continues "Although the procedures require ORC issue bimonthly status reports indicating information and target dates, reports were not always issued on a bimonthly basis and were discontinued in October 1996." ORC and WPB had agreed that, because the status of the disputes was not progressing as expected, and because ORC had little control over the production of WPB memoranda upon which the dispute resolution schedule ultimately depended, it was an inefficient use of ORC's time to maintain this status report. However, to the extent that the recommendation on page 52 advises ORC to resume issuance of these status reports, Region II agrees that ORC will resume issuance of the bimonthly status reports containing the required information.
- On page 51, the report provides: "Adtracs also did not account for the 15 reconsideration cases returned to Region 2 for resolution. When they were returned to the Region, the attorney should have completed a form for revised information to be inputted in to the system." The Region had been informed by EPA Headquarters that Adtracs can not accommodate information on grants disputes that are before the Region for reconsideration. To the extent that the cited recommendation suggests that this information be included in Adtracs, ORC will inquire as to whether Adtracs can be revised to accommodate the additional list. In the interim, ORC will continue to include in its bimonthly status report a list of cases for which there has been a Request for Reconsideration.

No Informal Conferences or Chronological Logs Section (page 50)

It is unclear as to what impact the auditors are claiming that ORC's failure to maintain complete logs of actions and documentation of meetings and conversations has had in delaying the dispute resolution process.

OIG Recommendation (page 52)

"We recommend that the Regional Administrator instruct ORC and Water Programs Branch personnel to implement a joint plan to accelerate the dispute resolution process. This effort must certain *{sic}* a greater commitment by both offices to eliminate the case backlog. Increased Water Branch actions are clearly needed to provide complete and timely program memoranda, and dates can not be constantly revised. In addition, ORC must initiate timely informal conferences, maintain adequate files with chronological logs of actions, and adequately document all meetings and conversations."

Region II Response

Region II has made considerable progress in reducing the inventory of appeals under dispute with 51 resolved and 17 remaining to be resolved. In response to the OIG's comments, we will review our current inventory to determine the extent to which these can be resolved more expeditiously.

ABBREVIATIONS

COE	U.S. Army Corps of Engineers
DECA	Division of Enforcement and Compliance Assistance
DEPP	Division of Environmental Planning and Protection
EPA	Environmental Protection Agency
FDL	Final Determination Letter
FMD	Financial Management Division
FMFIA	Federal Managers' Financial Integrity Act
FTA	Federal Transit Administration
FTE	Full Time Employee
FY	Fiscal Year
GAB	Grants Administration Branch
GCMB	Grants and Contracts Management Branch
GICS	Grants Information Control System
IFMS	Integrated Financial Management System
NYCDEP	New York City Department of Environmental Protection
NJDEP	New Jersey Department of Environmental Protection
NYSDEC	New York State Department of Environmental Conservation
OIG	Office of Inspector General
OMB	Office of Management and Budget
ORC	Office of Regional Counsel
WCB	Water Compliance Branch - Caribbean Section
WMD	Water Management Division
WPB	Water Programs Branch - Construction Grants Section

[This page intentionally left blank]

REPORT DISTRIBUTION

Office of Inspector General

Acting Inspector General (2441)
Assistant Inspector General for Audit (2421)
Deputy Assistant Inspector General for
Acquisition and Assistance Audits (2421)
Divisional Inspector Generals

Regional Office

Regional Administrator
Assistant Regional Administrator for Policy and Management
Director, Division of Enforcement and Compliance Activities
Director, Division of Environmental Planning and Protection
Office of Regional Counsel
Audit Coordinator

EPA Headquarters Office

Comptroller (3301)
Agency Follow-up Official (3304)
Associate Administrator for Regional Operations
and State/Local Relations (1501)
Director, Grants Administration Division (3903R)
Director, Office of Wastewater Management (4201)
Headquarters Library (3404)

