

**TESTIMONY OF MELISSA HEIST ASSISTANT
INSPECTOR GENERAL FOR AUDIT U.S.
ENVIRONMENTAL PROTECTION AGENCY
BEFORE THE
COMMITTEE ON ENVIRONMENT AND PUBLIC WORKS
UNITED STATES SENATE
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Good morning, Mr. Chairman and members of the committee. I am Melissa Heist, Assistant Inspector General for Audit for the United States Environmental Protection Agency. I am pleased to be here today representing Nikki Tinsley, the Inspector General. Thank you for the invitation to inform you about the work we have done reviewing EPA's administration of assistance agreements, also known as grants.

Assistance agreements are a primary means EPA uses to carry out its mission of protecting human health and the environment. More than half of EPA's fiscal 2003 budget was awarded to organizations outside the Agency through assistance agreements. EPA primarily awards assistance agreements to State, local, and tribal governments; universities; and nonprofit organizations. Because the amount is large, approximately \$4.4 billion dollars, and it is the primary mechanism EPA uses to fulfill its mission, it is imperative that the Agency use good management practices in awarding and overseeing these agreements to ensure that they effectively contribute to attaining environmental goals.

EPA's management of assistance agreements has been an area of emphasis for the Inspector General's office for many years. In fact, we have been issuing audit reports and raising concerns about EPA's management of assistance agreements for over ten years. In addition to our audit work, we have also conducted a number of investigations related to the improper and illegal activities of some EPA grantees.

Our grants management work has focused on crosscutting national issues and has included grants made to States, local and tribal governments, and nonprofit organizations. We have looked at major program areas in EPA headquarters and regions. We designed our work to identify systemic problems preventing the Agency from achieving the maximum results from the billions of dollars awarded in assistance agreements every year. In my testimony I will include examples from our work that illustrate the types of problems we have found in EPA's grants management activities. The entire reports for these examples can be found on the OIG web page at www.epa.gov/oig.

On Monday, March 1, 2004, we issued an audit report on an EPA grantee that we initiated at the Agency's request. We found an ineligible lobbying organization was performing work under cooperative agreements and the procurement process was circumvented. We questioned \$4.7 million because the work was performed by an ineligible lobbying organization. EPA awarded the cooperative agreements to an associated organization that did not have any employees, space or overhead expenses. In addition, the ineligible organization's financial

management practices did not comply with Federal regulations. For example, the ineligible organization did not adequately identify and separate lobbying expenses in its accounting records. As a result, lobbying costs may have been charged to the Federal projects. The ineligible organization also claimed that it had not always followed Federal regulations because EPA directed the recipient to use a particular contractor.

Pre-Award Activities

In May 2001, the OIG reported that EPA did not have a policy requiring program officials to competitively award discretionary assistance funds. EPA had done little to promote competition, and often did not provide adequate justification for not using competition to award grants. Assistance agreements were awarded without competition based on the project officer's opinion that the recipient was uniquely qualified. There was no documented evidence that no other organizations existed that could perform the desired work. We also found that EPA was not performing a widespread solicitation for assistance agreements. Without widespread solicitation, EPA limited the potential applicants and created the appearance of preferential treatment. Without competition, EPA cannot be sure that it is funding the best projects based on merit and cost-effectiveness to achieve environmental objectives, and accomplishing its mission with a reasonable return on the taxpayer's investment.

Before EPA awards an assistance agreement, the EPA project officer must conduct a programmatic and technical review of the application package in order to select those applications that will most effectively contribute to EPA program objectives and priorities. A main focus of the project officer's review is the work plan, which should describe what will be done, when it will be accomplished, and the estimated costs. The pre-award review is critical to ensure that the results of the assistance agreement will contribute to protecting human health and the environment.

In 1998, the OIG issued a report stating that project officers were not always negotiating work plans with well-defined commitments or adequately determining and documenting that costs for the assistance agreement were reasonable. In March 2002, the OIG reported that EPA was awarding assistance agreements without identifying expected outcomes, quantifying outputs, linking outputs to funding, or identifying milestone dates for completing work products.

In a report issued in March 2003, we reported that project officers did not perform all the necessary steps when conducting pre-award reviews. For this audit, we selected a statistical sample of 116 assistance agreements awarded by the Office of Air and Radiation, the Office of Water, and related regional offices. We found:

- § EPA awarded \$700,000 without knowledge of the work the recipient was going to perform. The work plan did not have clear objectives, milestones, deliverables, or outcomes.

The recipient stated in the work plan: "Because of the exploratory nature of these activities and the need to bring together various market players, exact deliverables and schedule will be determined based on what participants tell us they want from our project."

- \$ In 79 percent of the sampled assistance agreements over \$100,000, project officers did not document cost reviews of proposed budgets. For example, a recipient was awarded \$1.3 million to operate its air pollution control program without determining the reasonableness of the proposed costs to the expected benefits of the projects.
- \$ In 42 percent of the sampled assistance agreements, EPA did not negotiate environmental outcomes. For example, EPA awarded a recipient \$200,000 to regulate costs charged by power companies. The work plan contained no environmental outcomes, and stated that specific projects would be identified at a later date. In fact, the work plan itself only provided possible activities, and stated specific projects would be established later. The project officer wrote on the application, "why this, why now?" yet still approved the work plan.

Without complete pre-award reviews of proposed projects, there was insufficient assurance that the funded projects would accomplish program objectives or desired environmental results. There was also insufficient assurance that proposed costs were reasonable, and that recipients were technically capable of performing the work. EPA may also have lost the opportunity to fund other projects that would have better achieved its mission.

Post-Award Grants Management

OIG reports continue to find that improvements are needed in EPA oversight of assistance agreements after they are awarded. In 1995, we found that EPA staff were not (1) making site visits, (2) timely processing financial status reports, (3) obtaining or reviewing required audit reports, and (4) ensuring that final reports were completed. In 2002, we followed up on EPA's progress in improving oversight and found that weaknesses continued to exist. While EPA had developed policies and training to improve the oversight of assistance agreements, it did not ensure that the policies were followed consistently.

OIG reports continue to identify examples of EPA staff not adequately overseeing awards to states for environmental programs and nonprofit organizations for specific projects.

- \$ A February 2003 report found that EPA Region 6's oversight of Louisiana was insufficient and could not assure the public that Louisiana was protecting the environment. We initiated this review because EPA had received petitions from citizen groups to withdraw Louisiana's National Pollutant Discharge Elimination System, a water program; the Resource Conservation and Recovery Act, a hazardous waste program; and the Title V air permit program. Region 6 leadership (1) did not develop and clearly communicate a vision and

measurable goals for its oversight of the State or emphasize the importance of consistently conducting oversight, (2) did not hold Louisiana accountable for meeting goals and commitments, and (3) did not ensure that data of poor quality was corrected so that it could be relied upon to make sound decisions. As a result, EPA was unable to assure the public that Louisiana was operating programs in a way that effectively protected human health and the environment. In its response, EPA's Region 6 said it would implement its new oversight protocol for use beginning in FY 2005.

- \$ A March 2002 report found that EPA had no assurance that as much as \$187 million spent on procurements by assistance recipients was used to obtain the best products, at the best prices, from the most qualified firms. Recipients were not competing contract awards or performing cost or price analysis as required by the regulations. For example, a nonprofit recipient awarded two sole source contracts to its for-profit subsidiary. The recipient also awarded sole source contracts to three for-profit companies created by its for-profit subsidiary. The recipient entered into 23 contracts, 20 of which were awarded sole source. As a result, we questioned \$1.3 million of costs claimed.

Insufficient EPA Review and Oversight Contributed to Recipient-s Problems

Recent audits of grant recipients show how EPA's lack of review and oversight can contribute to problems for the grantee.

- \$ We questioned \$1.7 million in costs claimed because a recipient did not have an adequate time distribution system and an indirect cost rate, as required by EPA regulations. The EPA project officer focused his oversight on the technical performance of the recipient, with little emphasis on business and administrative aspects of the recipient-s performance. The grants specialist did not respond to repeated requests from the recipient for assistance in developing the indirect cost rate. Further, the project officer did not conduct an onsite review of the recipient until almost six years after the first award.
- \$ We questioned \$1.6 million in costs claimed by another recipient for, among other things, improper procurement. The recipient did not competitively procure equipment and services, and did not perform cost or price analysis for the purchases. Furthermore, procuring goods and services for State agencies is not an authorized use of the funds provided under Section 103 of the Clean Air Act. EPA staff contributed to the problem when it wrote the sole source justification and scope of work for the contract. The justification for the sole source procurement was the EPA staff-s familiarity with the contractor and the work that needed to be performed. EPA policy specifically prohibits employees from directing a recipient to award a contract to a specific individual or firm or participate in the negotiation of an award of a contract under an assistance agreement.

Improved Accountability Needed

The deficiencies in EPA's pre-award reviews and post-award oversight were not due to the lack of policies, but rather existing policies and guidance were not always followed. EPA policies and guidance identify the reviews EPA staff are to perform prior to and after assistance agreements are awarded. However, EPA staff did not always follow the policies and were not held accountable when they did not do so.

- § The project officer function is often a collateral duty for EPA staff. In some instances, the performance agreements and position descriptions did not identify project officer responsibilities. Even when the performance agreement identified the individual as a project officer, the agreement did not reference specific project officer duties such as determining the programmatic and technical merit of a project or conducting cost reviews.
- § Senior Resource Officials did not emphasize the importance of post award monitoring. Senior Resource Officials are charged with strengthening Agency-wide fiscal resources management. They are typically Deputy Assistant Administrators or Assistant Regional Administrators. These officials stated that the level of post award monitoring was affected by the limited availability of resources for staffing, travel, and training.

EPA's Actions to Address Weaknesses

EPA has taken some corrective actions to address our recommendations to better manage assistance agreements.

- During 2002, the Administrator issued two orders to implement new changes – the Policy on Competition in Assistance Agreements and the Policy on Compliance, Review, and Monitoring. Through enhanced monitoring required by the new policy, EPA has increased the number of requests to the OIG for audit.
- During 2003, EPA issued its Grants Management Plan, a five-year strategy designed to ensure that grant programs meet the highest management and fiduciary standards.
- EPA initiated a review of performance standards for all employees involved with grants management and required new standards to be in place by January 2004.
- EPA has drafted a Long-term Grants Management Training Plan designed to improve the skills of those responsible for grants management activities.

The challenge for EPA now will be to ensure that staff implement, and are held accountable for, following the new policies and for implementing the new grants management and training plans.

Many of the deficiencies we found were due to EPA staff not following existing policies and not being held accountable.

In issuing its Grants Management Plan, EPA stated its vision was to ensure that its grants programs meet the highest management and fiduciary standards and further the Agency's mission of protecting human health and the environment. The OIG will monitor the Agency's progress in implementing the Plan, and we will evaluate whether the actions are effective in improving the accountability of recipients.

We are proud of the efforts the OIG staff have made in bringing these issues to light, and I thank you, Mr. Chairman and members of the Committee, for the opportunity to participate in a discussion of such an important topic. We are committed to working with you and EPA to ensure that the money awarded every year through assistance agreements is producing the intended environmental and public health benefits.

This concludes my prepared remarks, and I will be happy to respond to questions.