



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

DEC 7 2011

OFFICE OF WATER

MEMORANDUM

SUBJECT: Response to Report: EPA and States Should Strengthen Oversight of Clean Water State Revolving Fund Recovery Act Projects, Project No. OA FY10 0088

FROM: Nancy K. Stoner
Acting Assistant Administrator

A handwritten signature in black ink, appearing to read "Nancy K. Stoner", is written over the printed name and title.

TO: Melissa M. Heist
Assistant Inspector General for Audit

Thank you for the report transmitted on August 24, 2011, entitled, "EPA and States Should Strengthen Oversight of Clean Water State Revolving Fund Recovery Act Projects." We appreciate the effort involved in reviewing the inspection and oversight procedures of such a large and fast-paced program, and we welcome the opportunity to discuss the report's recommendations.

The report documents a number of findings regarding EPA and State oversight procedures as well as the frequency and effectiveness of project inspections. Additionally, the report contains nine recommendations regarding oversight of both States and projects. While I agree with the report's assertion that oversight of such a large and complex program is essential to prevent fraud, waste, and abuse, many of the conclusions reached in the report are based on faulty assumptions or limited information.

While we disagree with many of the conclusions in the report, we concur with and have implemented or are implementing most of the recommendations, which are generally reflective of good management practices. Given the special conditions unique to ARRA, we do not believe results under ARRA can be generalized to the CWSRF base program. Attachment one provides the Office of Water response to the recommendations included in the report. We remain concerned that many of the factual inconsistencies in the draft report remain unaddressed. Therefore, without reiterating each concern, we highly recommend that you review the issues highlighted in appendix 2 of my response to the draft report.

Again, thank you for the opportunity to respond to these findings and recommendations. If you have and comments or questions regarding this response, please contact me or Sheila Frace, Director, Municipal Support Division, Office of Wastewater Management, at (202) 564-1153.

Attachments

Attachment 1

Responses to Recommendations

1. Develop and implement a plan to supplement the state inspections with EPA inspections of ARRA projects that includes expanded testing to verify compliance with ARRA requirements.

The Office of Water initiated a plan to supplement state inspections. The Office of Water randomly selected approximately 30% of all projects for inspections related to ARRA specific compliance. Through mid-November, almost all inspections (approximately 500) have been completed. Reports and recommendations are being issued to all reviewed assistance recipients, and this action should be complete by September 2012.

2. Require states to follow the updated state ARRA inspection checklist and reference guide when inspecting ARRA projects.

The Office of Water does not concur with this recommendation. Beyond the question of whether EPA possesses the legal authority to impose the recommended requirement, virtually all States have already inspected projects and many used or incorporated specific elements from the inspection checklist developed by the program. Regional staff were required to accompany State staff on at least one, and preferably two, project inspections each year under ARRA. The Office of Water provided training for State programmatic staff and local staff, and provided contractor support to assist with project inspections for States with limited resources. The Office of Water independently inspected approximately 500 CWSRF ARRA projects through mid-November, 2011. Furthermore, the majority of projects have been completed and reviewed and ARRA funding to support programmatic management and oversight expired on September 30, 2011.

3. Update the semiannual ARRA review checklist to include:
 - a. Detailed questions about state oversight of project construction.
 - b. Expanding transaction testing when erroneous payments are identified.
 - c. A question as to whether the project files contain appropriate documentation that the assistance recipient complied with Davis-Bacon Act requirements.

The Office of Water concurs with recommendations 3(a) and 3(c) and they will be implemented in the next round of ARRA annual reviews. Office of Water agrees to the recommendation to expand transaction testing, but only where warranted by cases of serious, or systemic erroneous payments. Regarding recommendation 3(b), based on findings to date, we believe that our transaction tests are sufficiently rigorous when combined with our state reviews to identify if additional transaction tests should be incorporated into a future review as a follow-up item.

4. Update the state inspection checklist to include a review of Davis-Bacon documentation and a recommendation to independently verify compliance on a sample basis.

The Office of Water does not concur with this recommendation. Davis-Bacon compliance is reviewed at the project level by state programs and was also reviewed during the inspections conducted by the Office of Water during the 2011 calendar year.

5. Establish deadlines for conducting the regional semiannual ARRA reviews of state programs and documenting them in PERs.

The Office of Water concurs, as this recommendation has already been implemented. Semiannual ARRA reviews are to be done approximately every 6 months, and are typically coordinated with the established schedule of the primary annual review. The primary annual review is a pre-existing and ongoing monitoring element of the base CWSRF program. It is recommended that the primary annual review be conducted within 60 days of receipt of the State's annual report, which is to be submitted within 90 days of the end of the State's fiscal year. As a result, the schedule does not comport with the Federal Fiscal Year. Guidance has already been issued directing PERs to be issued within 60 days of a review.

6. Use the PERs as a tool to assess Agency trends to make program decisions.

The Office of Water concurs, as this is already a core part of EPA oversight. EPA used the PERs, in addition to interaction with States and Regions during reviews, summary finding memos, individual checklists for projects and transactions, and semiannual summaries to identify best practices and identify trends for needed changes and improvements in the program. EPA has used all of this information to develop program priorities, including: expanding the annual review checklists; conducting 3-day training in oversight procedures in each Regional office between March and October 2011; establishing discussion points during the monthly coordinator calls; and updating Standard Operating Procedures for Regional staff. Given the special conditions unique to ARRA, the Office of Water does not believe results under ARRA can be generalized to the CWSRF base program.

7. Use the risks that are identified in the PERs to determine the level of oversight needed for each state.

The Office of Water concurs, as this is already a core part of EPA oversight. It must be noted, however, that EPA provides findings to States during the exit conference of the State review and initiates corrective actions, if needed, well before final PERs are signed. This approach allows EPA the flexibility, for example, to increase the number of project file reviews even during the course of the ongoing review or in supplementary reviews should an issue be identified. It also allows the State to immediately begin corrective actions, as needed. Given the special conditions unique to ARRA, the Office of Water does not believe results under ARRA can be generalized to the CWSRF base program.

8. In the next quarterly ARRA stewardship plan report, discuss OW actions to address the timely completion of PERs.

The Office of Water concurs.

9. In FYs 2011 and 2012, continue to identify the progress in completing PERs and determine whether failure to complete them, and complete them in a timely manner, should be identified as an office-level weakness.

The Office of Water concurs with recommendation to continue monitoring the progress in completing PERs. The Office of Water does not concur with the recommendation to make a determination of weakness based on results from FY2011 and FY2012, given that CWSRF ARRA oversight activities will have been largely, if not fully completed by end of FY2012. Given the special conditions unique to ARRA, the Office of Water does not believe results under ARRA can be generalized to the CWSRF base program.