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RECOVERY ACT

Funds Continue to Provide Fiscal Relief to States and Localities, While Accountability and Reporting Challenges Need to Be Fully Addressed (Arizona)



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Appendix I: Arizona

Overview

The following summarizes GAO's work on the third of its bimonthly reviews of American Recovery and Reinvestment Act (Recovery Act)¹ spending in Arizona. The full report on all of our work, which covers 16 states and the District of Columbia, is available at www.gao.gov/recovery/.

We reviewed two programs in Arizona funded under the Recovery Act—Highway Infrastructure Investment and the Weatherization Assistance Program. We selected these for different reasons. Contracts for highway projects using Highway Infrastructure Investment funds have been under way in Arizona for several months, and provided an opportunity to review financial controls, including the oversight of contracts. The Weatherization Assistance Program funding provided a significant addition to the annual appropriations for the program assisting more low-income households to achieve energy efficiency while providing long-term financial relief. Furthermore, it provided an opportunity to determine the state and local procedures in place to ensure monitoring, tracking, and measurement of weatherization program success. We reviewed contracting procedures and examined four specific contracts under Recovery Act Highway Infrastructure Investment funds. In addition to these two programs, we also updated funding information on three Recovery Act education programs with significant funds being disbursed—the U.S. Department of Education (Education) State Fiscal Stabilization Fund (SFSF) and Recovery Act funds under Title I, Part A, of the Elementary and Secondary Education Act of 1965 (ESEA), as amended, and the Individuals with Disabilities Education Act (IDEA), Part B. Consistent with the purposes of the Recovery Act, funds from the programs we reviewed are being directed to help Arizona and local governments stabilize their budgets and to stimulate infrastructure development and expand existing programs—thereby providing needed services and potential jobs. The following provides highlights of our review of these funds:

Highway Infrastructure Investment

- The U.S. Department of Transportation's (DOT) Federal Highway Administration (FHWA) apportioned \$522 million in Recovery Act funds to Arizona. As of September 1, 2009, the federal government has obligated \$293 million to Arizona and \$18 million has been reimbursed by the federal government.

¹Pub. L. No. 111-5, 123 Stat. 115 (Feb. 17, 2009).

- As of September 3, 2009, Arizona has awarded 47 contracts totaling \$135.1 million for statewide highway projects. Arizona has provided for at least one construction contract for Recovery Act highway project in each of its 15 counties with all counties receiving at least \$100,000 in statewide Recovery Act Federal Highway funds and 13 of the 15 counties each receiving at least \$1.8 million.
- Arizona has awarded only three construction contracts for local highway projects because of a lack of local shovel-ready projects. The lack of projects was due to some localities' not understanding the allocations that they would receive as well as their unfamiliarity with federal highway requirements.

Weatherization Assistance Program

- The U.S. Department of Energy has allocated to Arizona about \$57 million in funding for the Recovery Act Weatherization Assistance Program for a 3-year period. As of September 1, 2009, approximately \$49 million has been allocated to local service providers to conduct weatherization training and make energy efficiency improvements with approximately \$28.5 million eligible for reimbursement.
- Arizona expects to expend the full Recovery Act funding allocation before the 3-year period and plans to weatherize approximately 6,400 units statewide, which according to state officials, could result in as much as \$1.8 million in overall energy savings annually.
- As of September 11, 2009, Arizona had expended \$771,485 of Recovery Act weatherization funds, or about 1.4 percent of the total allocation. While most local service providers were ready to begin weatherization work, they waited until they were provided final Davis-Bacon Act local wage requirements.

Updated Funding Information on Education Programs

- Education has awarded Arizona approximately \$557 million of the state's approximately \$1 billion of SFSF available funds. Of that, Arizona had planned to provide approximately \$250 million to elementary and secondary local education agencies and approximately \$183 million to public institutions of higher education. As of September 8, 2009, Arizona had not disbursed any SFSF funds to local education agencies or community colleges, but has disbursed approximately \$154 million to the state's three universities.
- Additionally, Education has awarded Arizona about \$195 million in Recovery Act ESEA Title I funds. Arizona has allocated about \$185 million, or 95 percent of these funds, to local education agencies

(LEA). Based on information available as of September 8, 2009, Arizona has disbursed about \$3 million to local education agencies. These funds are to be used to help educate disadvantaged youth.

- Education has also awarded Arizona about \$184 million in Recovery Act funds under IDEA, Part B. As of September 8, 2009, local education agencies have been allocated all \$184 million and have received \$2.2 million of the funds. The IDEA funds are to be used to support special education and related services for children and youth with disabilities.

Arizona Using Recovery Act Funds to Provide Short-Term Relief; Anticipates Fiscal Challenges to Continue after Recovery Act Funds Expire

In the face of declining revenues and economic activity, Arizona is using Recovery Act funding to help balance the state budget and minimize the large program reductions to the fiscal years 2009 and 2010 budgets. According to state budget officials, Arizona's general fund full year collections for fiscal year 2009 were \$7.69 billion, a decrease of 18.4 percent compared to fiscal year 2008, after various accounting adjustments, such as fund transfers. To address this revenue gap, the state reduced its overall general fund appropriations by approximately \$1.4 billion in fiscal year 2009, or 14 percent compared to fiscal year 2008, and applied \$750 million in Recovery Act funding to reduce expenditures, according to the Joint Legislative Budget Committee.² However, despite these cuts and the Recovery Act federal assistance, Arizona had an estimated remaining budget shortfall of \$479 million. While the state has a balanced budget requirement, according to the budget committee staff, the Arizona constitution permits the state to address any year-end shortfall in the next fiscal year. As a result, Arizona's fiscal year 2009 estimated shortfall of \$479 million was carried over and addressed in the fiscal year 2010 budget.

For fiscal year 2010, which began in Arizona on July 1, 2009, Recovery Act funding will continue to temporarily stabilize the state budget. As of September 4, 2009, Governor Brewer has signed, vetoed or line item vetoed all fiscal year 2010 budget bills transmitted to her by the Arizona legislature. Arizona's anticipated shortfall for fiscal year 2010 of \$3.16 billion was largely resolved by the Governor's actions on the budget bills, according to the Joint Legislative Budget Committee. The budget includes

²In our April 2009 report we noted that Arizona depleted its budget stabilization fund, or rainy-day fund.

Recovery Act funding of approximately \$1.13 billion.³ However, according to the Governor, the bills did not amount to a comprehensive state revenue strategy for fiscal year 2010 and future fiscal years. In particular, the Governor exercised line item veto authority on the Department of Education and Department of Economic Security reductions, while acknowledging this level was higher than the state's current available revenues can sustain. In her transmittal letter, the Governor cited her intent to restore education funding and preserve spending levels to meet Recovery Act requirements. The Governor vetoed legislation which affected funding and the assessment of fees for a number of smaller state agencies and commissions and also allowed the 3-year-old temporary suspension of the State Equalization Assistance Property Tax, which supports K-12 education, to expire, according to the Governor's budget office.⁴ As officials explained, because this tax is levied at the local level—increasing the proportional contribution of local monies to education funding—the return of this tax effectively means a decrease in the state's formula contribution to education funding. According to the Governor's budget officials, the legislature had made several additional cuts to state support for education funding which would have pushed Arizona below the education expenditure level that it must maintain to meet requirements for SFSF funds.⁵ However, the Governor exercised line item veto authority on certain Department of Education reductions in order to maintain education expenditures at the required levels. The Joint Legislative Budget Committee now estimates a remaining shortfall of approximately \$350 million. The Governor is now planning to call the legislature back into session to address the outstanding budgetary challenges. In addition to the budget shortfall, reduced revenues have resulted in the state treasurer having to make short-term borrowings from other state and local

³Recovery Act funds used to stabilize the state's operating budget include approximately \$816 million in state funds made available as a result of the increased Federal Medical Assistance Percentage for Medicaid (discussed in detail in [GAO-09-1016](#)) and \$311 million in SFSF funding. These figures do not include \$250 million in SFSF funds for elementary and secondary education that were anticipated in fiscal year 2009, but which will now be made available in fiscal year 2010.

⁴Arizona Senate Bill 1025: The General Revenue Act. In her transmittal letter, the Governor stated her willingness to support a permanent repeal, but as part of a comprehensive proposal that addresses the state's revenue shortfall.

⁵Among other provisions, the Recovery Act requires states to assure that states' support for education will not fall below the levels provided in fiscal year 2006. Also, the return of this tax could affect the LEAs' budgets and LEAs may have to modify their applications for SFSF monies.

government funds to cover cash deficits in order to continue state operations. In addition, the state is preparing to establish an external line of credit of \$500 million, according to the Governor's office.

The Governor has proposed that she and the legislature continue to work to address the state's revenue shortfall. As part of a five-part long-term solution to Arizona's fiscal condition, the Governor has asked the legislature to consider a temporary sales tax increase, particularly in light of the fact that the Recovery Act funding will expire. The staff of the Joint Legislative Budget Committee has estimated that a voter-approved temporary sales tax increase of 1 cent for the first 24 months and a half-cent for the following 12 months would generate revenue totaling approximately \$2.5 billion for fiscal years 2010 through 2013. In addition, the Governor called for a state tax reform to promote investment in Arizona, revenue stability and job growth and sustainability. According to state officials, members of the legislature have proposed individual and corporate income tax reductions—estimated to reduce revenue by \$400 million in fiscal years 2012 and 2013—and to permanently repeal the State Equalization Assistance Property Tax—estimated to cost \$250 million in fiscal year 2010 and up to \$281 million in fiscal year 2013.

Arizona is currently looking for additional ways to address its projected fiscal challenges and is developing budgetary plans to avoid a sudden drop in revenues as the Recovery Act funding period ends, according to Governor's staff members. The \$750 million spent in fiscal year 2009 and \$1.13 billion obligated for fiscal year 2010 to address budget shortfalls leave Arizona with only a projected \$417 million in Recovery Act funding remaining for fiscal year 2011. Current estimates project a deficit between \$0.89 billion and \$2.2 billion in the state's general fund for fiscal year 2011, depending on various budget solutions being considered. The Governor's staff continues to develop plans to work with state agencies on internal organizational changes that can help reduce expenditures. In addition, on August 17, 2009, the Arizona Senate President established the Arizona Budget Commission, which will assess how appropriations are allocated by state agencies; streamline the agencies' organization, operation and costs; and create a best-practices management model for state government.

Arizona May Have Insufficient Funds to Cover Administration Costs of Recovery Act Oversight without Expedient Review of State Proposals

Given Arizona's budgetary challenges, officials in the Governor's Office of Economic Recovery (OER) and the Arizona State Comptroller expressed their concern about having adequate funding to cover the additional administrative costs associated with compliance of the Recovery Act provisions. States have been given the option to recoup costs for central administrative services, such as providing oversight and meeting reporting requirements of the Recovery Act, as outlined in Office of Management and Budget (OMB) memorandum M-09-18.⁶ The OMB memo presented two alternative methods—using estimated costs or billing for services. Both alternatives are longstanding methods that have been allowed under the guidance in OMB Circular A-87. However, as understood by the state's Comptroller, the cost recovery processes that OMB currently allows will not cover all the additional administrative costs under the Recovery Act, and he expressed two major concerns over the OMB Circular A-87 cost allocation methodologies. First, according to the Comptroller, the state will not be able to fully recapture the cost of depreciable equipment that is dedicated specifically for Recovery Act purposes. For example, equipment such as a computer server that is purchased by the state to comply with Recovery Act reporting or monitoring would be depreciated over the life of the asset and not over the period of Recovery Act programs. The life of the asset would be longer than the period of Recovery Act programs, resulting in the state receiving an allowance for depreciation for a shorter period. Therefore, the state comptroller maintains that Arizona would not receive full cost recovery. Second, the traditional cost allocation methodologies require that the state charge administrative costs according to a formula based on the actual amount of money spent.

To address Arizona's concerns about insufficient funds to cover the administrative costs, the Arizona State Comptroller, along with other state comptrollers, collaborated with their national association, the National Association of State Auditors, Comptrollers, and Treasurers (NASACT), to address these issues, and on August 7, 2009, requested on behalf of the states, a waiver of certain requirements of OMB Circular A-87. The request

⁶OMB Memorandum, M-09-18, *Payments to State Grantees for Administrative Costs of Recovery Act Activities* (May 11, 2009), provides that states may charge Recovery Act grants up to 0.5 percent of total Recovery Act funds received by the state under cost recovery processes under current guidance of OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*. Under the provisions of OMB Circular A-87, states can recoup administrative costs through the Statewide Cost Allocation Plan (SWCAP), which is submitted to the Department of Health and Human Services annually for review and approval. There are two alternatives, use of estimated costs for centralized services, or billed services.

asked for a change (1) to increase the allowance for depreciation of assets that are dedicated to Recovery Act purposes; and (2) to allow states to apply a prorated allocation of central service agency costs based on the ratio of state agency Recovery Act funds received as compared to total Recovery Act funds received by the state.

Additionally, Arizona submitted a proposal to the Department of Health and Human Services's (HHS) Division of Cost Allocation to simplify the calculation and accounting for central administrative costs related to Recovery Act programs.⁷ Arizona proposed that it be allowed to base the allocation of central service agency costs based on budgeted dollars that would not be adjusted to the actual amount of money spent.

According to the state Comptroller, OMB reviewed the waiver request and advised that the request to increase the depreciation allowance was a policy issue and would not be treated as a waiver. Regarding the second waiver request, OMB advised that the Division of Cost Allocation would approve cost allocation methodologies on a state-by-state basis.

As of September 15, 2009, Arizona is awaiting a decision from OMB on the policy issue for depreciation allowance and from HHS for approval of the cost allocation methodology. The state, pending a decision from HHS on the cost allocation methodology, plans to go forward using the second option—billing for services—allowed by OMB Memorandum M-09-18. However, the state comptroller is concerned that by the time OMB and HHS make a decision, recipients of Recovery Act funds in Arizona will have already spent significant portions of these funds leaving the state with a much smaller pool of remaining funds from which the state could collect the administrative costs. Therefore, the ability of the state to collect for all administrative costs could be jeopardized.

⁷The Division of Cost Allocation within HHS administers state cost allocation plans, which provide a process whereby state central service costs can be identified and assigned to benefited activities.

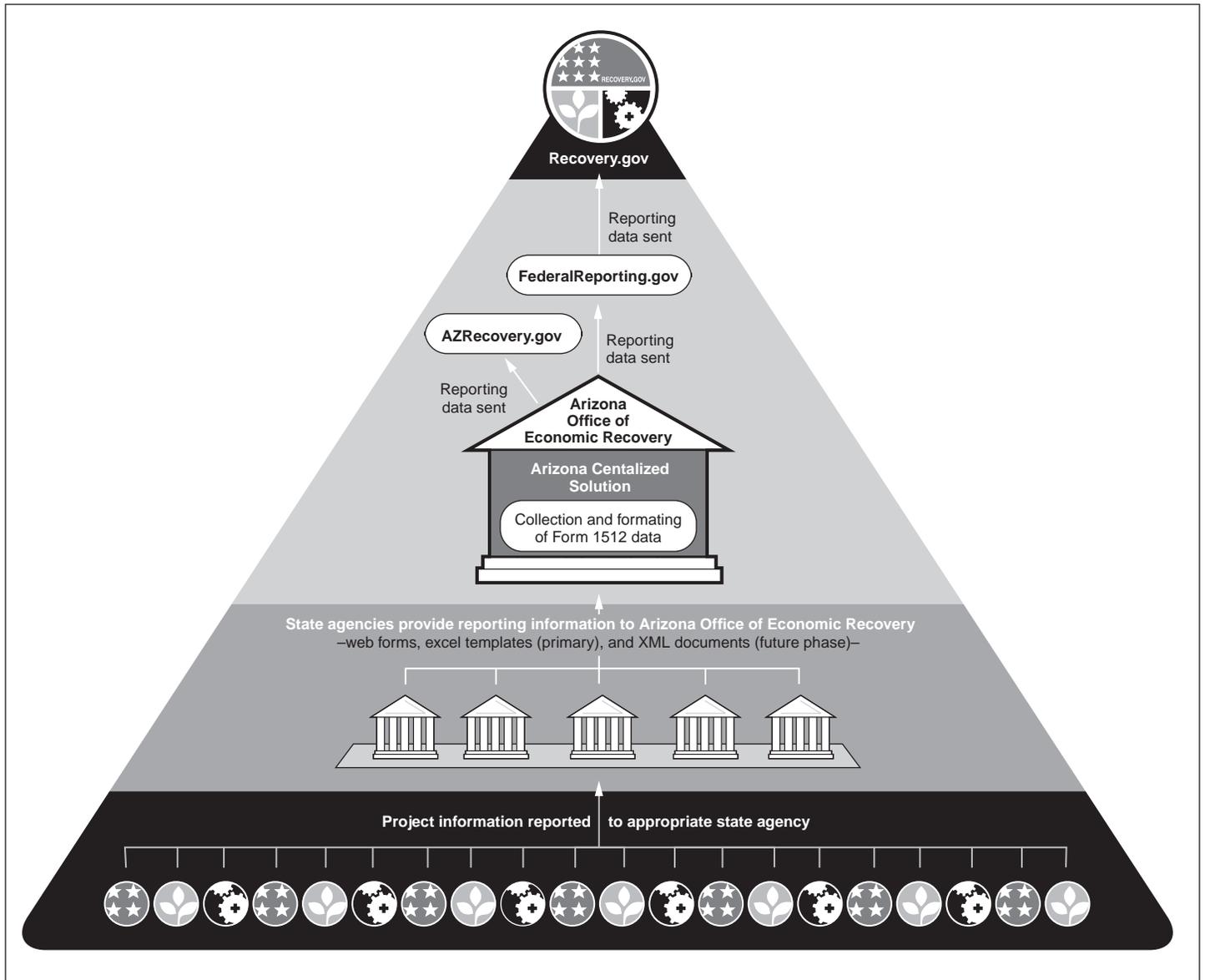
Arizona's Strategy to Meet October Reporting Deadline Is Based on Implementing a System Intended to Centrally Collect and Report Data on State Agencies' Use of Recovery Act Funds

Recipients of Recovery Act funds are required to submit quarterly reports under section 1512 of the act to the federal agencies providing those Recovery Act funds. These reports are to include, among other requirements, (1) the total amount of Recovery Act funds received by each recipient from the federal agency, (2) a list of all projects and activities for which Recovery Act funds were expended or obligated, (3) an evaluation of the completion status of each project or activity, and (4) an estimate of the number jobs created and number of jobs retained by each project or activity. Recipients are to submit the first report by October 10, 2009, for the quarter ending September 30, 2009. The Recovery Act requires that the reporting be done by entities, other than individuals, that receive money directly from the federal government. These entities are to submit their data using www.federalreporting.gov which will then be made available to the public at www.recovery.gov.

Arizona officials from the Governor's office explained that the Governor envisions her office as the responsible party for Recovery Act funds received by the state of Arizona. Therefore, OER plans to centrally collect data and to submit these quarterly 1512 reports for the state agencies. Some of the benefits envisioned by the Governor for single reporting are the ability to expedite the reporting process, provide a common system for reporting, and use built-in audit capabilities. Arizona will employ a centralized reporting solution that, according to OER officials, will comply with OMB reporting guidance. The centralized solution is based on a software application known as Stimulus 360 that is customized to meet the Recovery Act reporting requirements. State agencies that receive Recovery Act funds will send the required reporting data to the OER team. The Governor's OER team will compile this data into a single entry and report the information through www.federalreporting.gov, the reporting portal, to www.recovery.gov.

Using this centralized approach, the Governor's team will extract financial data already available from the state's accounting system on Recovery Act funds that state agencies are using, add in any other data from the agencies, and upload these combined data into the centralized reporting solution. (See figure 1.) According to OER officials, their team will provide reporting and auditor resources to review data quality and perform data validation and data cleanup. The state comptroller noted that the inherent risk of double reporting certain data elements, such as the number of jobs created, by both the state agency and other subrecipients, such as a vendor performing the work, would be reduced with centralized reporting.

Figure 1: Arizona's Centralized Reporting System for October Reporting



Source: GAO.

As an additional check on data accuracy, each state agency will be responsible for validating its data prior to submitting it to the state. For example, as discussed later in this appendix, data for transportation projects are housed in the Arizona Department of Transportation's

(ADOT) existing reporting system, LCPTracker, and will undergo numerous levels of review by ADOT prior to reporting these data to OER for inclusion in the centralized reporting system.

To coordinate with and obtain cooperation from the state agencies on using the centralized solution, the Governor's team started meeting in July 2009 with the directors of state agencies. The Governor's team explained its preference for the centralized reporting method over each state agency reporting separately. The team also gathered information on reporting requirements and subsequently began planning for a test run of the centralized reporting method. According to OER officials, as of September 8, 2009, all state agencies plan to use the Governor's centralized reporting methodology.

Early Identification of Key Long-Term Recovery Act Impacts on the State Could Help the State, Its Agencies, and Localities Ensure They Will Have the Necessary Data and Tools to Ensure Accountability

Recognizing that the state and agencies have focused their limited resources in the short term on putting the Recovery Act funds to work in Arizona and meeting the October reporting deadline, staff in OER are beginning to think about what unique economic impact of Recovery Act funds the state would want to track and measure over the long term, separately from the federal government data requirements. By doing so, the state will be positioned to identify any lessons learned from its implementation of the Recovery Act program and to provide accountability to the public on the act's effects. OER staff acknowledged, however, that they have limited resources to do longer term planning, but are moving forward as resources become available. Determining at the start of the Recovery Act program which long term effects to track would help the state to ensure it is collecting data from the outset that it will need, as well as has the systems and skilled staff in place to complete analysis.

For agencies, localities, and other Recovery Act funding recipients outside of OER, considering ways to use collected data and measure long-term effects of Recovery Act funding is valuable, assuming resources for planning and analysis are available. Officials within the Arizona Department of Education stated that they hope to use data to identify correlations between uses of program funds and improvements in student performance. Consequently, they can continue successful efforts if alternative funding is available. Likewise, officials managing the ESEA Title I education program acknowledged the benefits of determining research questions on final Recovery Act impacts so that they can prepare as needed. In addition, officials within the state Department of Commerce managing the Recovery Act weatherization funds are positioning the

department to estimate the amount of energy saved as a result of work completed with these funds. These are positive steps consistent with the state's long-term planning objectives. The state could also help to ensure that other agencies and localities, as appropriate, are taking such steps to make the best use of funds.

SFSF Funds Help Address Education Cuts in Some Programs, but K-12 Funds Delayed

The Recovery Act created the State Fiscal Stabilization Fund (SFSF) in part to help state and local governments stabilize their budgets by minimizing budgetary cuts in education and other essential government services, such as public safety. Stabilization funds for education distributed under the Recovery Act must be used to alleviate shortfalls in state support for education to school districts and public institutions of higher education (IHE). The initial award of SFSF funding required each state to submit an application to Education that provided several assurances. These included assurances that the state will meet maintenance-of-effort requirements (or it will be able to comply with waiver provisions) and that it will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. In addition, states were required to make assurances concerning accountability, transparency, reporting, and compliance with certain federal laws and regulations. States must allocate 81.8 percent of their SFSF funds to support education (these funds are referred to as education stabilization funds), and must use the remaining 18.2 percent for public safety and other government services, which may include education (these funds are referred to as government services funds). After maintaining state support for education at fiscal year 2006 levels, states must use education stabilization funds to restore state funding to the greater of fiscal years 2008 or 2009 levels for state support to school districts or public IHEs. When distributing these funds to school districts, states must use their primary education funding formula, but they can determine how to allocate funds to public IHEs. In general, school districts maintain broad discretion in how they can use education stabilization funds, but states have some ability to direct IHEs in how to use these funds.

In July 2009, we reported that the Governor had applied to the U.S. Department of Education for SFSF funds that would allow the state to offset budget cuts and that Education approved this application. According to the Governor's office, Arizona plans to use the government services funds for programs to support children's services, community health centers, and officer salaries in the state's Department of

Corrections. As of August 28, 2009, Education had awarded to Arizona approximately \$557 million of its nearly \$1 billion in available SFSF funds. The state had planned to provide \$433 million to school districts and charter schools (otherwise referred to as local education agencies) and public IHEs for fiscal year 2009 expenditures, with approximately \$250 million available to local education agencies (LEA) and approximately \$183 million to public IHEs. However, based on guidance from Education, the state now plans to provide some of these funds in fiscal year 2010 instead, as discussed in the following section.

Arizona Plans to Make First Round of SFSF Funds Available to LEAs in Fiscal Year 2010 Rather than 2009 as Planned after Additional Guidance from U.S. Department of Education

The OER is creating an application process and deadlines for the LEAs and plans to distribute the first round of \$250 million SFSF funds to LEAs in fiscal year 2010. In our July 2009 report, we reported that because Arizona was facing a nearly \$3 billion budget deficit, the Governor and legislature had backfilled \$250 million in general fund appropriation reduction for K-12 programs with SFSF funds. However, based on communications with Education after the issuance of our report, Arizona was not able to effect this budgetary change.⁸ Education and OER have agreed to procedures that will allow SFSF funds to be utilized in Arizona consistent with the intent of the Recovery Act. OER revised its original approach and plans to make the SFSF funds available in September 2009, upon receipt of applications from LEAs.

According to the Governor's office and Joint Legislative Budget Committee staff, the postponement in draw down of the funds has complicated the state's budget balancing efforts. In addition, the state had to borrow money in order to cover the first monthly state aid payment to LEAs in fiscal year 2010 because the SFSF funds were not available, according to the Office of the Arizona State Treasurer.⁹ Office of the

⁸Education advised the state that this action would be inconsistent with some of the Recovery Act requirements, as at the time of the state's initial drawdown request, LEAs had not been asked to submit applications for the SFSF funds. In addition the funds would have gone to the state's general fund and only indirectly to LEAs, although Education noted that, per the act, the funds must go directly to LEAs.

⁹As part of the fiscal year 2009 budget plans adopted by the Arizona governor and state legislature in June 2008, Arizona shifted \$602.6 million for K-12 education, effectively delaying 2 months of fiscal year 2009 school payments to fiscal year 2010. According to the Office of the Treasurer, this was accomplished by rolling over half of the May 2009 and all of the June 2009 payments to July 1, 2009. In addition, in May 2009, a further adjustment was made for fiscal year 2009, according to the Office of the Treasurer staff, such that the remainder of the May 2009 payment was deferred until October 2009.

Treasurer staff noted this has increased the total amount the state has borrowed to maintain cash flow for state operations, and has played a role in the state's bond rating being placed on negative watch by one rating agency. Furthermore, according to a Governor's office budget official, the state anticipated challenges to making a scheduled state aid payment to school districts for September 2009 due to the state's cash flow situation. Therefore, the state intends to provide up to \$300 million in SFSF funds to schools in lieu of a September 15 state aid payment, according to a Governor's office budget official.

SFSF Funds Help Institutions of Higher Education Avoid Steep Tuition Surcharges, and Cuts in Personnel and Student Services

Of the \$182.8 million in SFSF funds originally planned for public IHEs in fiscal year 2009, the Governor allocated about \$154 million to the three universities in the state and the remaining approximately \$29 million to the 11 eligible community college districts. In fiscal year 2009, the level of state support for public IHEs was approximately \$1.06 billion.¹⁰ As of August 3, 2009, the three public universities each had submitted applications for SFSF and received the full amount of allocated SFSF funds. The three universities requested the SFSF monies as a reimbursement for fiscal year 2009 employee benefits, personnel services—such as salaries for faculty and instructors—and supplies. As of September 8, 2009, the community colleges are in the process of completing inter-government agreements with the state with respect to their SFSF disbursements.

According to the Arizona Board of Regents and the three university presidents in their SFSF applications, the SFSF funds helped the universities absorb budget reductions the state had implemented in order to address budget deficits. More specifically, the universities had their state support reduced by \$29 million in fiscal year 2008 and \$163 million in fiscal year 2009, amounting to approximately 17 percent of the overall state appropriations in fiscal year 2009 for the universities. Faced with these reductions, the universities took various actions such as operating reductions, academic restructuring, and layoffs and furloughs for faculty,

¹⁰Public Higher Education in Arizona is comprised of two systems; the state universities and the community colleges. The universities' governing body is the Arizona Board of Regents (ABOR), which provides policy guidance to Arizona State University, Northern Arizona University, and the University of Arizona in such areas as academic affairs, financial and human resource programs, tuition and financial aid, and strategic planning. The community colleges operate independently as districts, each governed by an elected board.

staff, and administrators. In addition, the universities anticipated an average tuition surcharge for the 2009-2010 academic year of \$2,051 before receiving Recovery Act funding, according to Regents' staff calculations. Table 1 shows the state appropriation reductions and the anticipated tuition surcharges for each university for fiscal year 2009.

Table 1: State Fiscal Stabilization Funding for Arizona's Public Universities

	Student body	General fund appropriation reduction, fiscal year 2009 (dollars in millions)	SFSF funding, fiscal year 2009 (dollars in millions)	Anticipated tuition surcharge before Recovery Act offset (2009-2010)	Actual tuition surcharge (2009-2010)
Arizona State University	67,082	\$66.1	\$69.82	\$1,609	\$510
University of Arizona	38,057	\$69.0	\$60.82	\$2,568	\$766
Northern Arizona University	22,307	\$19.2	\$23.49	\$1,975	\$422

Source: Arizona Board of Regents.

According to the three university presidents, the SFSF monies were necessary to avoid additional personnel reductions and furloughs and the resulting reduction of programs and student services. Furthermore, the availability of SFSF monies allowed the universities to significantly reduce the tuition surcharges for the 2009-2010 academic year to an average of \$566, based on Regents' staff calculation. From this perspective, the state universities and Board of Regents executive staff deemed the Recovery Act a success. Nevertheless, the tuition calculations show surcharges escalating for the 2012-2013 academic year, by approximately \$2,693 on average, once Recovery Act funding expires. Absent additional state or federal funding, the universities will need to develop budget plans to explicitly address their anticipated funding challenges.

Funds Starting to Flow to LEAs As Arizona Has Approved Many Applications for ESEA Title I Funding

The Recovery Act provides \$10 billion to help LEAs educate disadvantaged youth by making additional funds available beyond those regularly allocated through Title I, Part A of ESEA. The Recovery Act requires these additional funds to be distributed through states to LEAs using existing federal funding formulas, which target funds based on such factors as high concentrations of students from families living in poverty. In using the funds, LEAs are required to comply with current statutory and regulatory requirements and must obligate 85 percent of the funds by September 30, 2010.¹¹ Education is advising LEAs to use the funds in ways that will build the agencies' long-term capacity to serve disadvantaged youth, such as through providing professional development to teachers. Education made the first half of states' Recovery Act Title I, Part A funding available on April 1, 2009, and announced on September 4, 2009, that it had made the second half available.

The state educational agency (SEA) in Arizona has allocated \$185 million of the \$195 million in ESEA Title I Recovery Act funds to LEAs. The SEA official said that the remaining \$10 million has been set aside for administration and reallocation to LEAs. In the ESEA Title I Recovery Act funding process, each LEA submits an application that contains a detailed plan on how and when the funds will be used, and SEA officials review the application to ensure that LEAs' spending plans comply with applicable laws and regulations. When the SEA approves an LEA's application it also obligates ESEA Title I funds to the LEA. As seen in table 2 below, as of September 8, 2009, the SEA had approved 84 applications for about \$46.3 million. SEA officials expect to approve all applications and obligate \$185 million of ESEA Title I funds by September 30, 2009.

¹¹LEAs must obligate at least 85 percent of their Recovery Act ESEA Title I, Part A funds by September 30, 2010, unless granted a waiver, and must obligate all of their funds by September 30, 2011. This will be referred to as a carryover limitation.

Table 2: Number and Dollar Value of LEA Applications for Recovery Act ESEA Title I by Status, September 8, 2009

	Number of applications	Dollar value (in millions)	Amount of ESEA Title I Recovery Act funds disbursed to LEAs (in millions)
Applications approved by SEA	84	\$46.3	\$3.0
Applications submitted but not approved	133	38.9	
Applications to be submitted	209	99.4	
Total LEAs eligible for ESEA Title I Recovery Act funds	426	\$184.7	

Source: SEA grants management system for Recovery Act funds for state fiscal years 2009 and 2010.

Note: Totals may not add due to rounding.

LEAs with approved applications submit monthly cash management reports to SEA and the SEA provides funds to them with Recovery Act funds for their expected Recovery Act ESEA Title I program expenditures. As of September 8, 2009, LEAs had received \$3.0 million in ESEA Title I Recovery Act funds. SEA officials stated that the grants approved are in accordance with ESEA Title I and related statutory and regulatory requirements to improve students’ academic achievement, and include projects such as hiring specialists to provide strategic and intensive reading intervention to students who are not meeting Arizona’s reading standards.

SEA Applied for Authority to Approve LEAs' Requests to Waive Certain Requirements in the Use of ESEA Title I Recovery Act Funds

On August 26, 2009, the SEA applied to Education for the authority to grant LEAs' requests to waive various requirements for ESEA Title I Recovery Act funding.¹² As we reported in our July 2009 Recovery Act report, some LEAs will likely seek waivers from requirements to provide funds for public school choice-related transportation and supplemental educational services, such as tutoring, because they go unused, and this waiver will provide more funding for other ESEA Title I projects in those districts.¹³ As seen in table 3, as of September 8, 2009, a number of the 84 LEAs with approved applications are requesting waivers for various required activities.

Table 3: Number of LEAs Requesting Waivers

	Number of LEAs requesting waivers
Waiver to exclude the Recovery Act funds when calculating the 20 percent requirement for transportation and supplemental educational services	23
Waiver to exclude the Recovery Act funds when calculating the per pupil amount (PPA) of funds available for supplemental educational services	20
Waiver to exclude the Recovery Act funds when calculating the 10 percent set aside required for professional development when an LEA is identified for improvement	16
Waiver that allows a school to factor out some or all of its LEA's Recovery Act funds when calculating the required 10 percent set aside for professional development when a school is identified for improvement	18
Waiver to authorize LEAs to offer supplemental educational services in addition to public school choice to eligible students in schools in the first year of school improvement	Note ^a
Waiver to authorize LEAs and schools identified for improvement to apply to become supplemental educational services providers	Note ^a
Waiver to authorize the SEA to waive the carryover limitation for LEAs more than once every three years	Note ^a

Source: SEA grants management system for Recovery Act funds for state fiscal year 2010.

^aSEA has not asked LEAs if they need the waiver.

¹²Under ESEA Title I, states are required to establish performance goals and hold their ESEA Title I schools accountable for students' performance by determining whether or not schools have made adequate yearly progress (AYP). Schools that have not made AYP goals for 3 or more consecutive years must offer students an opportunity to transfer to a higher-performing school (public school choice) or supplemental educational services (SES). Districts are required to provide an amount not less than 20 percent of their ESEA Title I, Part A allocation to cover public school choice-related transportation costs and SES. Unless a waiver is granted, this requirement would apply to ESEA Title I Recovery Act funds also.

¹³GAO, *Recovery Act: States' and Localities' Current and Planned Uses of Funds While Facing Fiscal Stresses*, [GAO-09-830SP](#) (Washington, D.C.: July 8, 2009).

According to SEA officials, if the SEA’s application to waive Title I requirements for LEAs is granted by Education, the SEA will be able to decide which LEAs’ requests for waivers should be approved and thereby provide flexibility in the use of Title I funds. As of September 8, 2009, Education had not granted the SEA authority to grant LEAs waivers but Education expects to consider Arizona’s request soon.

Arizona LEAs Have Submitted Applications for IDEA Part B Funding and Some Have Been Approved, Allowing Funds to Flow to the LEAs

The Recovery Act provided supplemental funding for programs authorized by Parts B of IDEA, the major federal statute that supports the provisions of special education and related services for children, and youth with disabilities. Part B funds programs that ensure preschool and school-aged children with disabilities access to a free and appropriate public education and is divided into two separate grants—Part B grants to states (for school-aged children) and Part B preschool grants (section 619). Education made the first half of states’ Recovery Act IDEA funding available to state agencies on April 1, 2009, and announced on September 4, 2009, that it had made the second half available.

The SEA has allocated all of the \$184 million of the Recovery Act IDEA Part B funds to LEAs. Specifically, it allocated \$178 million to LEAs for school-age children and \$5.7 million to LEAs with preschool programs for preschool grants. To receive Recovery Act funds, each LEA must submit an application that outlines how it will use the funds. Subsequently, the SEA officials review the application to ensure that spending plans comply with applicable laws and regulations. When the SEA approves an application, this action also obligates the funds to the LEA. As seen in table 4, many LEAs have submitted applications and some have been approved.

Table 4: Number and Dollar Value of LEA Applications for Recovery Act IDEA by Status, September 8, 2009

	Grants for school-age children		Grants for preschool programs	
	Number of applications	Dollar value (in millions)	Number of applications	Dollar value (in millions)
Applications approved	121	\$14.9	45	\$1.0
Applications submitted but not approved	149	\$36.0	27	\$0.8
Applications to be submitted	284	\$127.5	114	\$3.9
Total LEAs eligible for Recovery Act IDEA grants	554	\$178.4	186	\$5.7

Source: SEA grants management system for Recovery Act funds for state fiscal years 2009 and 2010.

Specifically, as of September 8, 2009, the SEA had approved 22 percent of the 554 applications for about \$14.9 million of Part B grants to states and 24 percent of the 186 applications for about \$1 million of Part B preschool grants. LEAs with approved applications submit monthly cash management reports to SEA and the SEA provides funds to them with Recovery Act funds for their expected Recovery Act IDEA program expenditures, and as of September 8, 2009, the LEAs had received \$2.2 million of Recovery Act funds. SEA officials stated that the IDEA grants approved are in accordance with statutory and regulatory requirements and include projects such as professional development and assistive technology that may help the student participate in classroom activities (such as special computer software or a device to assist students in holding a pencil).

SEA Expects to Meet Recovery Act Reporting Requirements Primarily through Use of Existing Grants Management System for ESEA Title I and IDEA

The Arizona Governor's office is requesting that its state agencies use a centralized reporting methodology and report through the Governor's office. According to SEA officials, they plan to use this reporting methodology for Recovery Act funds for both ESEA Title I and IDEA funds. The SEA plans to obtain much of the reporting information for the LEAs from the existing grants management system that LEAs use for non-Recovery Act grants as LEAs use these same systems for non-Recovery Act funds as they do for Recovery Act fund. LEAs currently use this system to apply for grants and it already contains much of the information required for Recovery Act reporting, such as LEA name, LEA officials' names, award number, and amount disbursed. Any required additional information will be collected in a web application that is being developed by the Arizona Department of Education Information Technology unit. According to state education officials, they do not expect to have difficulties meeting Recovery Act reporting requirements.

Arizona Education Audit Unit Has Processes to Monitor the SEA's and LEAs' Internal Controls and the Corrective Actions They Take to Address Problems Identified through Single Audits

Arizona's SEA has an audit unit (the Arizona Education Audit Unit) that performs two functions that help to safeguard Recovery Act funds. The audit unit monitors how the SEA and LEAs are correcting problems or issues identified during the Single Audits and it also reviews the internal controls the LEAs have in place in their financial systems.¹⁴ The audit unit has developed a system to monitor whether LEAs who receive yearly federal funding of \$500,000 or more obtain Single Audits, and to monitor corrective actions taken by the SEA and LEAs for problems identified in their Single Audit reports. For fiscal year 2008, 164 or 29 percent of the 572 LEAs that were allocated Recovery Act funds had a single audit conducted. Audit officials noted that with the additional federal funds that LEAs will be receiving due to the Recovery Act, additional LEAs will likely exceed the \$500,000 threshold in federal funds for fiscal year 2010 and thus will be required to have Single Audits. The audit unit also conducts fiscal monitoring of a sample of LEAs' internal controls and in fiscal year 2009, the audit unit also reviewed the internal controls of 21 LEAs' financial accounting systems.

The Arizona Education Audit Unit is currently monitoring the SEA's and LEAs' responses to Single Audit findings that could affect the safeguarding of Recovery Act funds. According to the audit officials, they plan to continue their oversight during calendar year 2009 using fiscal year 2008 Single Audit reports and will also continue their fiscal monitoring reviews. The audit unit is monitoring six findings for the SEA that were particular to the ESEA Title I and IDEA programs in the fiscal year 2008 Single Audit Reports. Specifically, they included the following findings:

- The SEA did not verify that LEAs complied with ESEA Title I requirements by consulting with private schools within their boundaries to provide services to eligible private school children, their teachers, and their families or to report that there are no eligible private schools within the LEA boundaries;

¹⁴The Single Audit Act of 1984, as amended (31 U.S.C ch. 75), established the concept of the single audit to replace multiple grant audits with one audit of a recipient as a whole. As such, a Single Audit is an organization wide audit that focuses on the recipient's internal controls and its compliance with laws and regulations governing federal awards. It requires that each state, local government, or nonprofit organization that expends \$500,000 or more a year in federal awards must have a Single Audit conducted for that year subject to applicable requirements, which are generally set out in OMB Circular No. A-133, *Audits of States, Local Governments and Non-Profit Organizations* (June 27, 2003). If an entity expends federal awards under only one federal program, the entity may elect to have an audit of that program.

- Some LEA annual financial reports were incomplete or contained accounting errors and inconsistent information that prevented the SEA from determining whether LEAs met the IDEA program requirement—that state and local funding cannot be lower than it was in the previous 2 years;
- The SEA needed to provide additional documentation to support that it verified the number of students with disabilities to validate the accuracy of the Report of Children with Disabilities Receiving Special Education, Part B (an IDEA program);
- Some LEAs lacked adequate procedures to ensure compliance with Education’s requirements to submit monthly cash management reports;
- The Title I and IDEA grants management system did not have adequate controls because it did not require users to periodically change passwords, did not always maintain a history of user access, and permitted some internal users with access rights that were incompatible with their job responsibilities or that enabled them to change data without supervisory approval; and
- The SEA did not comply with the subrecipient monitoring requirements of ESEA Title I and IDEA, because it did not obtain Single Audit reports within 9 months of the subrecipient’s fiscal year-end, did not retain documents to support that the SEA tried to ensure audit requirements were met, and did not issue management decisions within 6 months after receipt of subrecipient Single Audit reports.

According to the audit officials, the SEA has been taking corrective action on these findings that will strengthen the safeguards for Recovery Act funds.

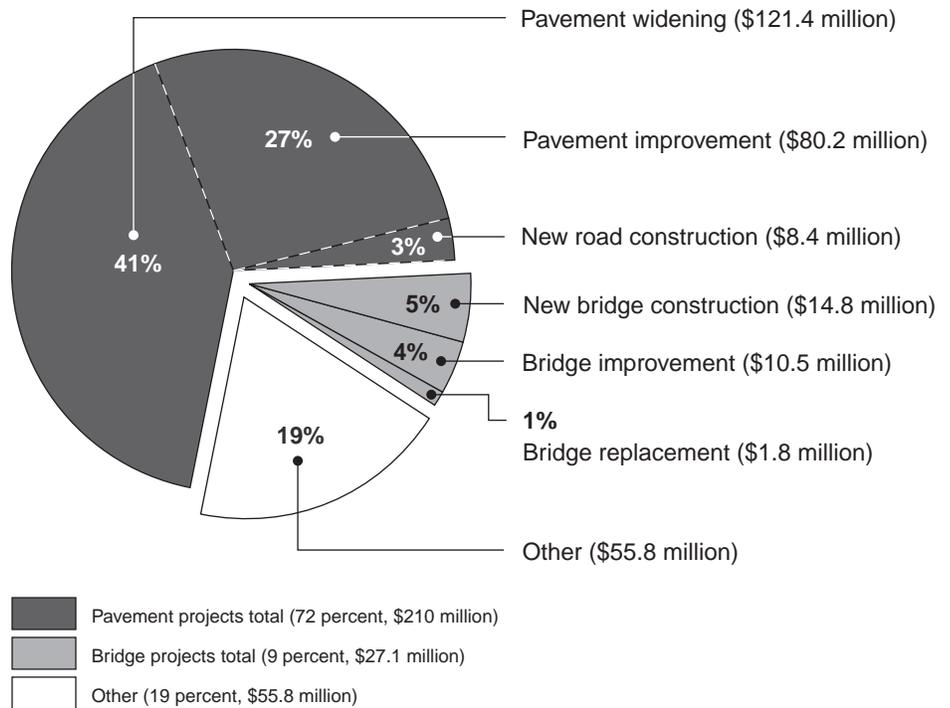
Arizona Continues to Move Forward with Statewide Highway Projects, but the Slow Pace of Local Projects and Impending Deadlines Are Cause for Concern

As we previously reported, \$522 million was apportioned to Arizona in March 2009 for highway infrastructure and other eligible projects. As of September 1, 2009, \$293 million had been obligated. As of September 1, 2009, \$18 million had been reimbursed by FHWA.¹⁵

Almost 72 percent of Recovery Act highway obligations for Arizona have been for pavement projects. Specifically, \$210 million of the \$293 million obligated as of September 1, 2009, is being used for pavement projects, including \$202 million for pavement preservation and roadway widening. State officials told us they selected this type of project specifically because they knew the projects could be completed within 3 years. Figure 2 shows obligations by the types of road and bridge improvements being made.

¹⁵States request reimbursement from FHWA as the state makes payments to contractors working on approved projects.

Figure 2: Highway Obligations for Arizona by Project Improvement Type as of September 1, 2009



Source: GAO analysis of FHWA data.

Note: Totals may not add due to rounding. "Other" includes safety projects, such as improving safety at railroad grade crossings, and transportation enhancement projects, such as pedestrian and bicycle facilities, engineering, and right-of-way purchases.

Arizona has Awarded Contracts on its Statewide Highway Projects and Started Construction on Many

As of September 1, 2009, FHWA has obligated 71 percent of the Recovery Act funds apportioned to Arizona for statewide highway projects.¹⁶ Of these Recovery Act funds, most, about \$350 million, were to be spent on statewide projects, or those highway projects selected by Arizona Department of Transportation (ADOT) from Arizona's 5-year transportation plan. The remainder of the highway funds is to be suballocated to localities across the state. These statewide projects were

¹⁶For the Highway Infrastructure Investment Program, the U.S. Department of Transportation has interpreted the term "obligation of funds" to mean the federal government's contractual commitment to pay for the federal share of the project. This commitment occurs at the time the federal government signs a project agreement.

selected based on a number of factors, including the level of priority of the project, the ability of the state to award contracts and begin construction in a timely manner, and the location of these projects in economically distressed areas of the state. The Recovery Act mandates that 50 percent of apportioned Recovery Act funds be obligated within 120 days of apportionment (before June 30, 2009). The 50 percent rule applied only to funds apportioned to the state and not to the 30 percent of funds required by the Recovery Act to be suballocated, primarily based on population, for metropolitan, regional, and local use. In addition, states are required to ensure that all apportioned funds—including suballocated funds—are obligated within 1 year. The Secretary of Transportation is to withdraw and redistribute to other states any amount that is not obligated within these time frames. As we previously reported, Arizona has met the 50 percent obligation requirement. By September 1, 2009, approximately 71 percent of Recovery Act funds had been obligated for statewide highway projects.

Arizona provided for at least one construction contract for a Recovery Act highway project in each of its 15 counties (see table 5), with all counties getting at least \$100,000 in statewide Recovery Act Federal Highway funds and 13 of the 15 counties each receiving at least \$1.8 million.

Table 5: Number and Amount of Construction Contracts for Statewide Highway Projects in Arizona by County

County	Number of construction contracts	Dollar value of construction contracts
Apache	3	\$2,997,320
Cochise	5	7,967,748
Coconino	5	13,174,891
Gila	5	11,537,077
Graham	1	133,331
Greenlee	1	567,178
La Paz	2	7,969,226
Maricopa	5	39,903,012
Mojave	3	6,426,321
Navajo	4	8,882,830
Pima	5	7,336,759
Pinal	1	13,133,079
Santa Cruz	1	1,873,811
Yavapai	1	1,899,987
Yuma	2	9,360,932
Statewide ^a	3	1,957,769
Total	47	\$135,121,271

Source: GAO analysis of ADOT data.

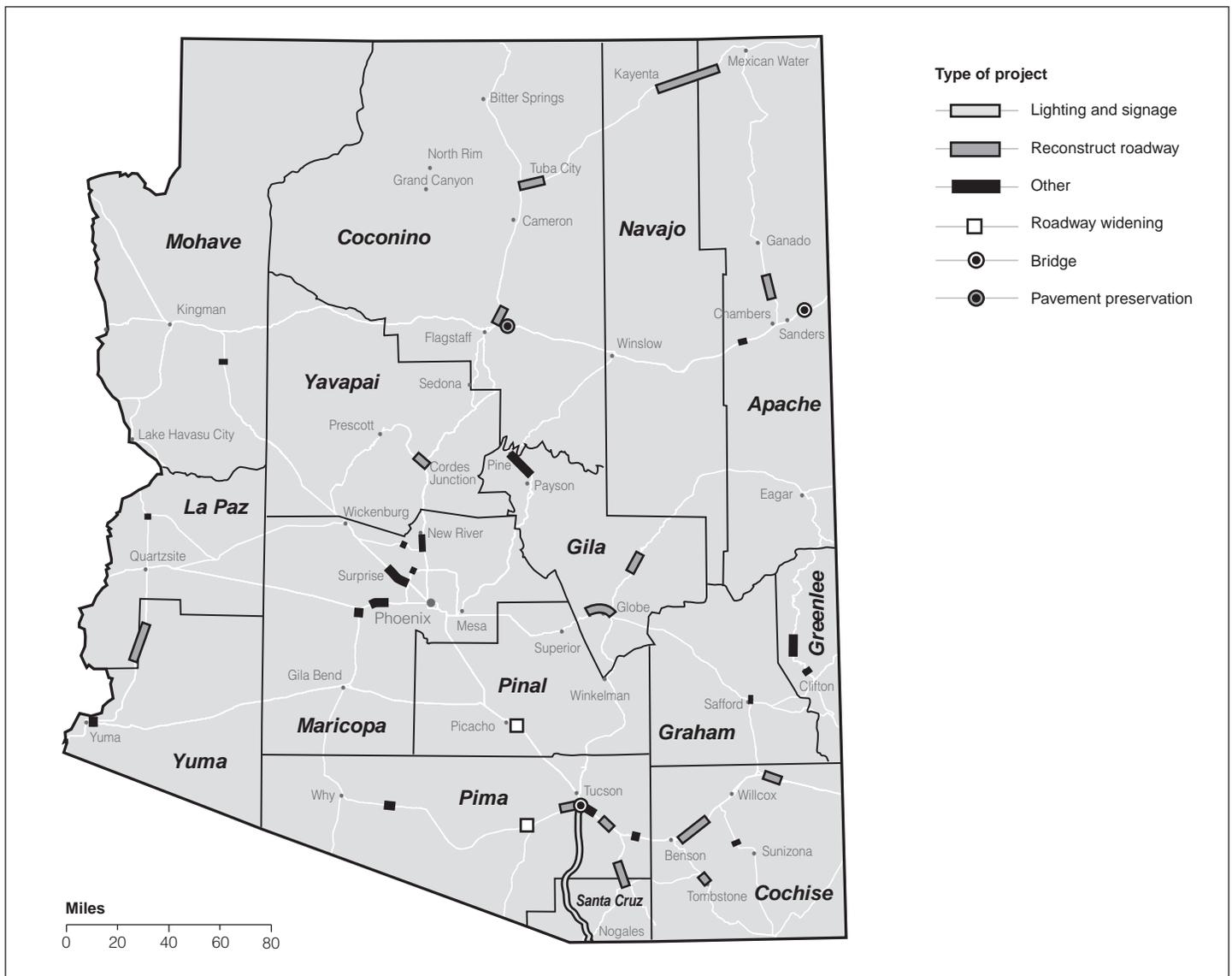
^aStatewide projects are multiple projects in various parts of Arizona with a similar scope.

Arizona’s original plan was to undertake 41 statewide highway projects under the Recovery Act, but due to significant underbidding by contractors, Arizona has, as of August 30, 2009, been able to add 2 additional statewide highway projects, both roadway widening projects, in Maricopa County, Arizona’s most populous. In addition, Arizona is hoping to add even more Recovery Act projects with the existing cost savings, which, as of August 30, 2009, were about \$60 million. ADOT officials believe that this underbidding is caused by the current low levels of economic activity in the construction industry due to the state’s economic downturn, as well as lower prices for commodities like asphalt and oil.

Arizona officials told us that, for the most part, Arizona’s statewide projects could be started quickly and completed within 3 years. All of the statewide highway projects undertaken by Arizona were already on the State Transportation Improvement Plan (STIP). ADOT officials told us

that most of the projects that the state undertook with Recovery Act funds were relatively simple and able to be completed within 3 years, such as pavement preservation, roadway widening, and lighting and signage (see figure 3).

Figure 3: Map Depicting Arizona’s Initial Statewide Recovery Act Highway Projects



Source: Arizona Department of Transportation (data and map).

Arizona Has Awarded Only Three Construction Contracts for Local Highway Projects Due to a Lack of Shovel-Ready Projects, Among Other Reasons, Which Could Pose Challenges in Meeting Recovery Act Time Lines

In contrast to the rapid awarding of contracts that the statewide Recovery Act highway projects have seen, three construction contracts for suballocated local projects have been awarded as of September 1, 2009. ADOT and FHWA both indicated that local projects have lagged behind statewide projects because of a lack of local shovel-ready projects. The lack of projects was due to some localities' not having an understanding of the allocations that they would receive as well as the unfamiliarity of some local agencies with federal highway requirements. Under the Recovery Act in Arizona, about \$157 million was suballocated to localities for federal highway construction. These funds were allocated to regional bodies known as Metropolitan Planning Organizations¹⁷ (MPO) members of which decide the highway projects they will undertake. Table 6 shows the distribution of funds across these regional bodies as well as the number of contracts awarded and total dollars obligated for these locality-led projects.

Table 6: Localities' Total Recovery Act Allocations, Number of Construction Contracts Awarded, and Total Funds Obligated for Construction as of September 1, 2009

Region	Total allocation	Number of construction contracts awarded	Total funds obligated for construction
Maricopa Region	\$104,578,340	0	0
Pima Region	34,876,167	1	\$276,000
Northern Arizona Counsel of Governments	4,112,608	0	0
Central Yavapai Metropolitan Planning Organization	1,283,485	0	0
Western Arizona Council of Governments	2,464,687	0	0
Central Arizona Association of Governments	3,258,973	0	0
South Eastern Arizona Governments Organization	2,795,080	0	0
Yuma Metropolitan Planning Organization	2,257,052	2	\$2,075,000
Flagstaff Metropolitan Planning Organization	961,128	0	0
Total	\$156,587,520	3	\$2,351,000

Source: GAO analysis of ADOT and FHWA data.

¹⁷Metropolitan planning organizations, federally mandated regional organizations, representing local governments and working in coordination with state departments of transportation, are responsible for comprehensive transportation planning and programming in urbanized areas. MPOs facilitate decision making on regional transportation issues including major capital investment projects and priorities.

When the Recovery Act was enacted, localities submitted a number of what they considered to be shovel-ready projects to ADOT for its approval and subsequent FHWA obligation of funds. An ADOT official told us that the department did not approve any projects and sent them back to the localities because either the scope of the project was too large; the project would exceed the localities' Recovery Act allocation; or the project was not designed to meet federal requirements. To explain, prior to the Recovery Act, Arizona had a program called the Highway Users Revenue Fund (HURF) exchange program. Through this program, local agencies sent their Federal Aid highway funds to ADOT in exchange for state funds. This allowed ADOT to design and administer highway projects to federal standards, including federal environmental standards, with which they have considerable experience, and allowed localities to use their own experience with the state standards to design and build highway projects to state standards. However, the HURF exchange program was suspended due to lack of funds in September 2008, so the Recovery Act represented the first time in years that many localities would have to design highway projects to federal specifications. To address the problems above, ADOT and FHWA held a number of training sessions to educate localities on their responsibilities under the Recovery Act. According to state and local officials we interviewed, nevertheless, some localities were still confused about the federal requirements they had to meet, particularly the environmental clearance requirements.

Because of the suspension of the HURF exchange program, which meant that localities would have to design federal highway projects on their own, and recognizing that the Recovery Act would represent a large amount of work for the localities to redesign and prepare highway projects to meet federal standards, ADOT has required that many localities work with management consultants to help design and submit for obligation their highway projects undertaken through the act. According to agency officials, these consultants are costing localities from 5 percent to 15 percent of their allocations under the act. ADOT said that the management consultants provide localities the means and expertise to design highway projects to federal standards, and concluded that were it not for the consultants, these local agencies would not be able to meet the March 2010 obligation deadline.¹⁸

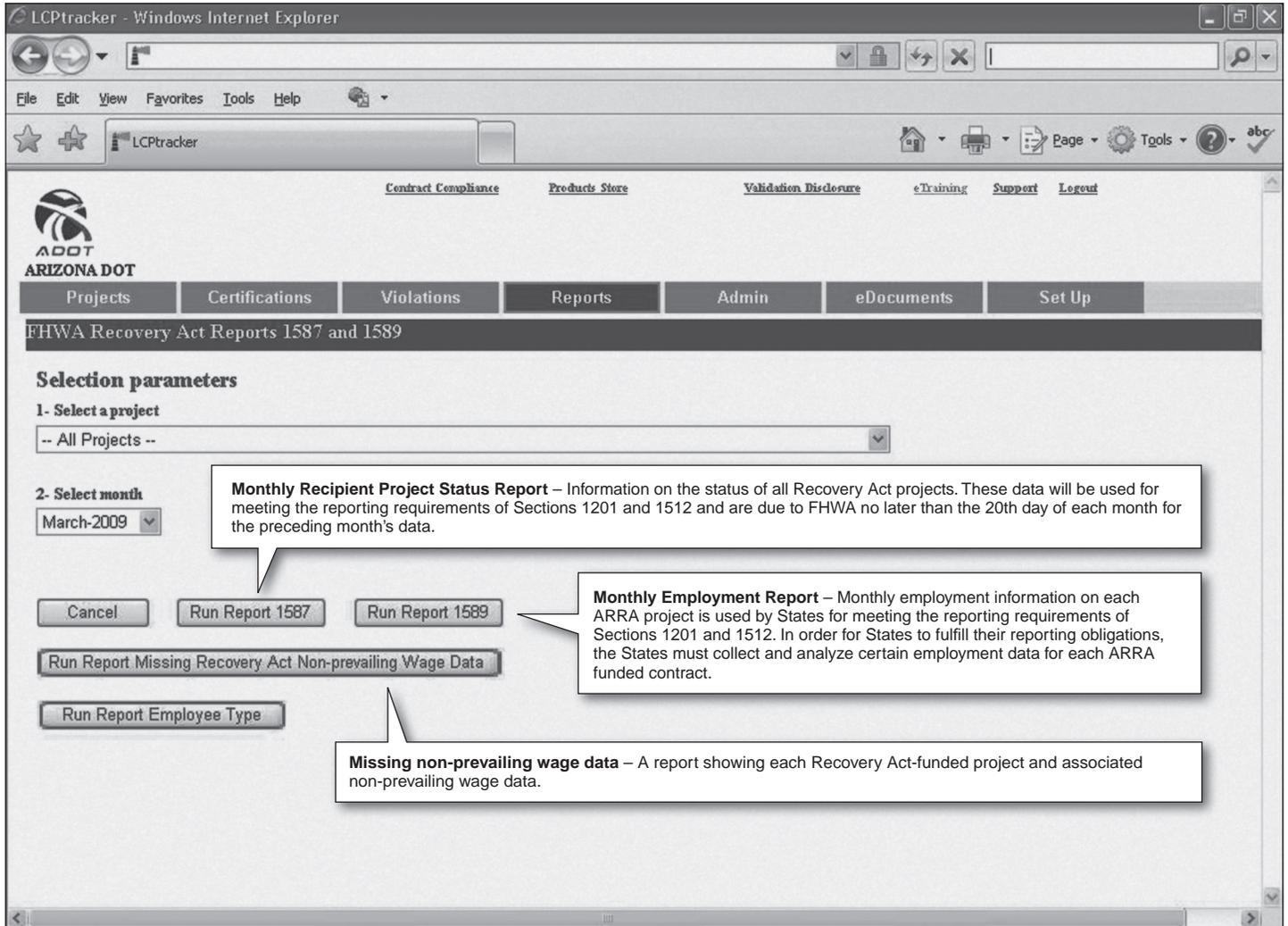
¹⁸The Recovery Act mandates that all apportioned funds, including suballocated funds, need to be obligated by, March 2010, 1 year from apportionment.

Despite having the benefit of the management consultants to help them design their Recovery Act highway projects, ADOT and two of the local officials we spoke with are still concerned that meeting the March 2010 obligation deadline could be a challenge. To address this concern, ADOT has instituted an internal deadline of December 2, 2009, by which they expect to receive submissions from all localities regarding the highway projects that they propose to undertake under the Recovery Act. Without this internal, statewide deadline, ADOT was concerned that there could be a glut of submissions to the agency and to FHWA requesting obligations just prior to the March 2010 deadline. According to an ADOT official, by moving the date forward to December, they can process all of the suballocated projects and send them on to FHWA for obligation and still meet the Recovery Act time frames. In addition, ADOT is considering actions that could be taken in the event localities are unable to submit shovel-ready projects by the March 2010 deadline. According to management consultants who are working with the localities, meeting the December time frame will be a major challenge, but they will submit as many of their highway proposals to ADOT as quickly as they can.

Arizona's Department of Transportation Does Not Anticipate Problems in Meeting Recovery Act Reporting Requirements and Intends to Participate in Centralized Statewide Reporting

To meet Recovery Act reporting requirements, the state has mandated in all of its contracts relating to Recovery Act highway work that all contractors shall report monthly to ADOT on the number of jobs created and preserved. The state has implemented the use of a database, LCPtracker, that allows contractors to simply enter financial and employment information into this database and submit that information electronically to ADOT. The agency is then able to transfer that information to the FHWA, as mandated by the Recovery Act. According to an agency official, ADOT is able to sort all contractor information, determine any penalties that need to be applied for incomplete or incorrect reporting, and run reports on the numbers of jobs created and preserved, as well as the wages paid for this Recovery Act work. Figure 4 shows an interface of the database with various reports that are able to be generated using contractor-supplied reporting information.

Figure 4: ADOT Database Used to Receive Recovery Act Information from Contractors and Report to FHWA and Descriptions of Database Report Mechanisms



Source: GAO analysis of Arizona Department of Transportation information.

To gain perspective on this issue, we visited three statewide highway projects in various areas in Arizona. Among other topics, we asked contractors working on these projects about their experiences in reporting wage and employment information to ADOT and whether they had experienced any problems in working with ADOT's reporting system, LCPtracker. For all three projects, the contractors hired laborers from the areas where the projects were located, and reported having no problems

in identifying and reporting the numbers of jobs created and preserved by their work on the Recovery Act projects. ADOT officials and contractors told us this is due, in large part, to training that ADOT conducted in the use of LCPtracker, which was used in a limited manner prior to Recovery Act projects, but made mandatory for all contractors working on Recovery Act projects.

Both the state and the contractors conduct numerous levels of review in order to verify the number of jobs reported as well as the wages paid to workers on Recovery Act highway projects. For example, one contractor we spoke with said she conducts periodic interviews with laborers on a highway project to determine that what the contractor reported to ADOT in monthly employment reports through LCPtracker was in fact the work that the laborer was doing on that particular day, as well as that those laborers were paid accurately according to Davis-Bacon Act prevailing wage requirements. In addition, ADOT officials told us they are conducting periodic site visits to determine that the number of laborers working on a particular day match the number that the contractor submits to ADOT in those monthly reports. In addition, according to ADOT officials, they visit the site of Recovery Act highway projects and examine the records kept by the contractors to verify that the number and type of jobs being reported to ADOT accurately reflect the number and type of jobs on the individual projects. When contractors do not report this information properly, a number of financial penalties are triggered that ADOT can impose on the contractors. As of September 4, 2009, no contractors have been found to misreport this required information, so no financial penalties have been levied on contractors.

FHWA's Arizona Division has also developed an inspection plan specific to Recovery Act highway projects. These inspections, conducted by FHWA staff, cover multiple levels of the project, including traffic control, changes to the contracts, material testing, and other construction activities. Inspections will be based on FHWA's assessment of the risk of each project, with new and reconstruction projects having the highest risk due to higher project costs, among other factors. FHWA considers pavement preservation projects with a cost of over \$5 million as medium risk, and miscellaneous projects with a cost under \$5 million as low risk. FHWA plans for approximately half of all Recovery Act highway projects in Arizona to have an initial inspection, which will be completed before 30 percent of the highway project is complete. FHWA plans intermediate inspections for a sample of the Recovery Act highway projects based on findings from initial inspections; the size, complexity, and scope of a project; and other factors. These inspections, when FHWA deems them

necessary, will occur when the project is 30 percent to 95 percent complete. Some projects will receive a final inspection to determine that the project was completed in a manner that conformed to the plans, specifications, and authorized changes. If FHWA finds that a project is not in compliance, it will then take corrective actions.

ADOT intends to send information on the number of jobs created and preserved as well as other financial and performance metrics required by OMB both to FHWA, as required by the Recovery Act, as well as to the Governor's office, to be part of Arizona's planned centralized reporting system. The data integrity manager at ADOT does not think that the Recovery Act poses any new challenges to ADOT in terms of either reporting to FHWA, which ADOT has done for years prior to the Recovery Act, or to the state for centralized reporting, which the agency has also done in the past. The issue of centralized reporting, however, is one that the Arizona State Comptroller's Office said might present a problem because ADOT uses different accounting codes than are used in the state's system, and reconciling those codes might become a challenge. But an ADOT official said that the issue of different accounting codes has existed for some time, and he does not foresee this becoming a major issue.

Contracts We Reviewed Indicate That ADOT Contracts for Recovery Act Work Were Awarded Competitively

We selected a total of four contracts, worth a total of \$40.7 million, to discuss with ADOT contracting officials to determine how the contracts were being awarded. ADOT awarded these contracts to conduct work in support of Recovery Act highway projects. We selected two contracts for work to be conducted in urban areas, and two contracts for work to be conducted in rural areas. According to an agency official, each of the contracts we reviewed was awarded competitively. For each of the contracts, the agency official stated that a project development process, an FHWA/ADOT operating partnership, ADOT standard specifications, and Recovery Act specifications were followed when the contracts were awarded. Further, the official said specific Recovery Act objectives were included in the solicitations that resulted in the contracts awarded pursuant to the act. Among other things, according to the ADOT standard specifications, prior to submitting a bid, ADOT will have to prequalify a bidder (unless waived by ADOT). The official indicated that all bidders for the contracts we reviewed were prequalified. Additionally, ADOT provided information to potential bidders on its Web site that explicitly stated that by submitting a bid for a Recovery Act funded project, the bidder agrees to be bound by conditions and reporting requirements in the contract, which identifies penalties for noncompliance. According to an ADOT official, the

work on the contracts we reviewed was awarded using unit fixed price contracts.

Determining Weatherization Wage Rates Has Delayed Contracts; Arizona Has Procedures in Place to Monitor and Report Program Results, but Is Still Uncertain about Counting Jobs Created

The Recovery Act appropriated \$5 billion over a 3-year period for the Weatherization Assistance Program, which the U.S. Department of Energy (DOE) administers through each of the states, the District of Columbia, and seven territories and Indian tribes. The program enables low-income families to reduce their utility bills by making long-term energy efficiency improvements to their homes by, for example, installing insulation, sealing leaks, and modernizing heating equipment, air circulation fans, or air conditioning equipment. Over the past 32 years, the Weatherization Assistance Program has assisted more than 6.2 million low-income families. By reducing the energy bills of low-income families, the program allows these households to spend their money on other needs, according to DOE. The Recovery Act appropriation represents a significant increase for a program that has received about \$225 million per year in recent years.

As of September 14, 2009, DOE had approved all but two of the weatherization plans of the states, the District of Columbia, and territories, and Indian tribes—including all 16 states and the District of Columbia in our review. DOE has provided to the states \$2.3 billion of the \$5 billion in weatherization funding under the Recovery Act. Use of the Recovery Act weatherization funds is subject to Section 1606 of the act, which requires all laborers and mechanics employed by contractors and subcontractors on Recovery Act projects to be paid at least the prevailing wage, including fringe benefits, as determined under the Davis-Bacon Act.¹⁹ Because the Davis-Bacon Act had not previously applied to weatherization, the Department of Labor (Labor) has not established prevailing wage rates for weatherization work. In July 2009, DOE and Labor issued a joint memorandum to Weatherization Assistance Program grantees authorizing them to begin weatherizing homes using Recovery Act funds, provided they pay construction workers at least Labor's wage rates for residential construction, or an appropriate alternative category, and compensate workers for any differences if Labor establishes a higher prevailing wage rate for weatherization activities. Labor then surveyed five types of

¹⁹The Weatherization Assistance Program funded through annual appropriations is not subject to the Davis-Bacon Act.

“interested parties” about labor rates for weatherization work.²⁰ The department completed establishing prevailing wage rates in all of the 50 states and the District of Columbia by September 3, 2009.

Arizona Department of
Commerce Had
Weatherization Contracts
Ready to Go as Soon as
Davis-Bacon Wage
Requirements Were
Established

DOE has allocated approximately \$57 million to Arizona for the Recovery Act Weatherization Assistance Program over a 3-year period (2009-2012), with about \$10 million of the total allocation to support initial ramp up activities, such as training center expansion, curricula development, staff training, and equipment purchases. On June 5, 2009, DOE approved Arizona’s Recovery Act Weatherization Assistance Program plan and the Arizona Department of Commerce (ADOC) allocated about \$49 million of the approximate \$57 million to local service providers to conduct ramp up and weatherization activities. Approximately \$28.5 million, or about half of the total allocation, is currently eligible for reimbursement. ADOC is the prime recipient as defined by OMB, while the subrecipients are the local service providers and the contractors that conduct the weatherization work. ADOC obligates funding to local service providers to weatherize low-income households by making long-term energy efficiency improvements, such as installing insulation or modernizing heating and cooling systems.²¹ After a local service provider determines that a home is eligible²² to receive weatherization work, the local service provider may employ in-house construction crews, hire contractors, or use a combination of both approaches to make the improvements. As the state does not have a centralized procurement system for purchasing weatherization materials, local service providers are delegated the responsibility of procuring their weatherization materials. ADOC officials expect to expend the full allocation before the 3-year period and plan to weatherize 6,409 units statewide, which, according to ADOC officials, could result in as much as \$1.8 million in overall energy savings annually. This is an almost threefold increase beyond the total number of units weatherized in the previous 3 years using regular program and other

²⁰The five types of interested parties are state weatherization agencies, local community action agencies, unions, contractors, and congressional offices.

²¹Building rehabilitation projects that are in a state of disrepair where failure is imminent and the condition cannot be resolved cost-effectively are beyond the scope of the Weatherization Assistance Program.

²²A household is eligible for Recovery Act weatherization services if they are at or below 200 percent of the federal poverty level. Priority service is given to the elderly, people with disabilities, families with children, or high residential energy users, and households with a high energy burden.

sources of funding.²³ Table 7 shows Arizona’s local service providers, their obligated funding amounts, the number of units they expect to weatherize from 2009 through 2012, and the cities and counties they serve.

Table 7: Arizona Local Service Provider Funding Obligations, Projected Number of Weatherized Units (2009-2012), and the Cities and Counties Served

Arizona local service provider	Funding obligation	Projected number of units	County/city served
Maricopa County Human Services Department, Community Service Division	\$11,911,987	1,604	Maricopa County coverage except cities of Phoenix and Mesa
Northern Arizona Council of Governments (NACOG)	7,500,359	997	Apache, Navajo, Coconino, and Yavapai Counties
City of Phoenix Neighborhood Services Department	7,222,865	960	City of Phoenix
Western Arizona Council of Governments (WACOG)	5,911,442	778	Yuma, La Paz, and Mohave Counties
Tucson Urban League, Inc.	4,749,363	618	Cities of Tucson and South Tucson
Southeastern Arizona Community Action Program (SEACAP)	4,654,446	603	Graham, Greenlee, Cochise and Santa Cruz Counties
Community Action Human Resource Agency (CAHRA)	2,269,618	275	Pinal County
Gila County Community Action Program	1,744,457	204	Gila County
Pima County, Community Development and Neighborhood Conservation Department	1,705,544	199	Pima County coverage except cities of Tucson and South Tucson
Mesa Community Action Network (Mesa CAN)	1,500,512	171	City of Mesa
Total	\$49,170,593	6,409	

Source: GAO analysis of ADOC data.

As of September 11, 2009, Arizona had expended \$771,485 of Recovery Act weatherization funds, or about 1.4 percent of the total allocation. According to ADOC, while most local service providers were ready to begin weatherization work, they had to wait until they were provided final Davis-Bacon local wage requirements before they could proceed because most providers did not have an existing in-house Davis-Bacon compliance officer providing them guidance on wage rates, and they preferred to avoid having to reconcile if wages in the awarded contracts differed from the required rates. Local service providers submitted their city’s or county’s

²³Local service providers partner with and receive other sources of funding from local, state, and federal utility and energy programs to maximize the return on investment for energy conservation-related activities, such as the Weatherization Assistance Program.

weatherization wage surveys directly to Labor and received final wage determinations on August 30, 2009. State and local service providers we met with have incorporated the Davis-Bacon Act requirements in their contracts stipulating that all laborers and mechanics employed by contractors and subcontractors for Recovery Act-funded weatherization work be paid the prevailing wage for their skill set in their locality. For example, the average hourly wage rate for heating and cooling installation workers in Arizona was about \$16.00, however, using the Davis-Bacon prevailing wage determination, the hourly wage for those same workers will be \$24.38 in Maricopa County and \$15.63 in Pima County. The final wage rates differ amongst the weatherization specialties and vary throughout the state of Arizona as determined by Labor. According to ADOC officials, the effect of the increased wages will not change the number of homes expected to be weatherized.

The City of Phoenix decided not to wait on the Davis-Bacon wage determination and began weatherizing eligible homes because Phoenix officials conducted their own wage determination analysis, consulted with their long-established Davis-Bacon compliance officer on relevant DOE and Recovery Act guidance, and were prepared to reconcile any wage differences. ADOC officials stated that they did not have concerns about the City of Phoenix moving forward prior to a final prevailing wage determination as they believe Phoenix officials were capable of meeting requirements and reconciling any wage differences. According to Phoenix officials, in mid-August, a three-bedroom single-family home was the first Recovery Act-funded weatherization project completed in Phoenix. The home had shade screens installed, an evaporative cooler removed, and a gas stove replaced that was found to be emitting potentially dangerous levels of carbon monoxide. This weatherization work resulted in a safer and more energy efficient home, which is expected to decrease the family's energy bill by 30 to 40 percent. Phoenix officials added that the project employed 6 full-time and 12 part-time workers over a 2-week period.

Recovery Act Funding and Program Requirements Result in Increased State and Local Support and Training to Effectively Manage Weatherization Activities

States and localities have had to increase the number of support activities needed to manage the increased funding and program requirements under the Recovery Act. According to ADOC officials, their organization ramped up from 5 to a total of 12 full-time staff to support Recovery Act requirements. Three of the seven program administration staff were hired to ensure Davis-Bacon compliance, weatherization database management, and general administration. Four of the five energy monitors were hired to assist with the additional weatherization monitoring and inspections. ADOC has also provided funding to hire two additional weatherization training center consultants and one contractor to conduct public outreach activities. Also, the number of energy auditors qualified to support weatherization monitoring and inspections is expected to increase from 137 to about 250 before the end of the 3-year Recovery Act period. In an effort to support more weatherization activities and effectively administer the program, Northern Arizona Council of Governments officials have proposed to establish two satellite field offices in rural communities to increase their capacity to conduct and monitor weatherization activities and provide local outreach while minimizing travel time and the associated costs.

Furthermore, ADOC has partnered with a local training center that is recognized as one of twelve National Weatherization Training Centers in the nation to develop additional courses and expand existing facilities necessary to train the number of weatherization contractors and auditors required to meet the Recovery Act weatherization program goals for Arizona.²⁴ ADOC has obligated \$300,000 of the approximate total of \$10 million, or 3 percent, in Recovery Act training and technical assistance funding to the training center. By late September 2009, the center plans to spend (1) \$40,000 of this amount to expand the training classroom space to accommodate the increased contractors requiring basic and advanced weatherization training, (2) \$10,000 to develop training curricula, and (3) \$250,000 to expand the training center's capabilities to include a larger laboratory for conducting hands-on diagnostic and heat performance testing and demonstrations.

²⁴The Southwest Building Science Training Center, in Phoenix, is one of twelve National Weatherization Training Centers, providing beginner and advanced classroom-style and hands-on weatherization training to contractors in California, Nevada, and Arizona.

Specifically, the increase in the number of contractors needed requires that they be trained and certified to conduct weatherization work.²⁵ Training center officials told us that a large number of contractors have expressed interest in becoming weatherization contractors. According to training officials, they have screened potential weatherization contractor viability by explaining the training and materials costs and type of activities involved in becoming a weatherization contractor as well as the training process, and provided hands-on experience to ensure they are highly motivated to remain in and succeed as a weatherization contractor. The weatherization training entails receiving hands-on training and testing in energy principles, heat performance, health and safety, diagnostics, and applied repair. Furthermore, if contractors are interested in becoming a certified energy auditor, they must complete one required course in building performance auditing. According to the training center officials, before the Recovery Act, they were training about four to six contractors per month, but now are training 20 to 40 weatherization professionals per month, a tenfold increase since June 2009. Since early January 2009, 52 people have completed weatherization training and more than 70 energy auditors have been certified at both the state and local levels. ADOC has also obligated \$150,000 in Recovery Act training and technical assistance funding to establish a free statewide weatherization contractor mentorship program designed to ensure the field readiness of every new weatherization contractor in Arizona. Specifically, experienced weatherization contractors approved and managed by the training center will mentor new weatherization contractors on the program and technical requirements, work techniques, and other aspects of successfully completing weatherization jobs.

State and Local Agencies Have Procedures for Monitoring Work Achieved and Uses of Recovery Act Weatherization Funds

Arizona has two key state and local procedures in place to ensure monitoring, tracking, and measurement of weatherization program success. These procedures involve multi-tiered monitoring and inspections and the statewide participation in an ADOC-developed weatherization Web-based reporting database. First, three levels of monitoring and inspections occur during the weatherization process: (1) by the contractor who made the improvements, (2) by the local service provider who employed the contractor or in-house crew, and (3) by the state who

²⁵In Arizona, Building Performance Institute (BPI) certification is recommended, but not required to be a weatherization technician, monitor, or inspector. BPI certified professionals diagnose, evaluate, and optimize the critical performance factors of a building that can impact health, safety, comfort, energy efficiency, and durability.

oversees the program and subrecipients. Contractors, local service providers, and ADOC officials conduct 100 percent mandatory file reviews on proposed weatherization projects to monitor whether contractors are making cost-effective improvements and that no opportunities are missed to further weatherize the eligible homes. Contractors and service providers also conduct 100 percent of the mandatory physical inspections for all completed weatherization jobs to ensure that the weatherization work meets safety and program requirements as well as results in energy savings. Also, according to ADOC, it regularly conducts physical inspections on about 20 percent of the weatherized homes, thereby exceeding the DOE requirement of conducting physical inspections on 5 percent of homes.

Second, the state and local service providers utilize a state-developed, Web-based reporting database to centralize audit data, facilitate the inspection process, and reduce the risk of fraud by weatherization contractors. Data collected during weatherization audits are entered into the Web-based reporting database and are only accessible by the contractor entering the data, its respective local service provider, and ADOC until they are submitted for state review at which point, data manipulation cannot be made. According to state officials, these internal control features, linking field-based work with a Web-based database and limiting accessibility to audit data, ensure proper monitoring and data integrity, and are essential in tracking the quantity and quality of weatherization work throughout the state.

According to ADOC officials, they conduct risk assessments of their local service providers and if any are determined to be at risk as a result of low weatherization production activities compared to funding received or noncompliance with health, safety, and program requirements, or if inspection files are incomplete, these weatherization contractors will receive additional oversight until they are in compliance and have reduced or eliminated their program risks. According to ADOC officials, one local service provider is currently undergoing increased monitoring to correct management and in-house crew deficiencies that resulted in inaccurate data collection and reporting and poor quality weatherization workmanship. The increased monitoring will continue for at least 2 months after the local service provider demonstrates better program administration and contract work compliance. The Arizona Office of the Auditor General has not audited the Weatherization Assistance Program as a major program in the Single Audit for the last 5 years and, therefore, cannot determine whether there are any internal control weaknesses in the state program. However, according to ADOC officials, the normal

monitoring of their state weatherization program and independent program reviews of their local weatherization service providers have not identified internal control weaknesses for 9 of their 10 local service providers. Although state and training center officials consider the program's principal risk to be the fast-growing number of weatherization contractors requiring increased oversight, they believe these risks are mitigated by the following:

1. Rigorous contractor vetting process conducted by the national training center. This process identifies viable and long-term weatherization professionals.
2. Requirement to have contractor weatherization training and auditor certification to conduct and monitor state-funded weatherization activities.
3. Limiting of new contractors to one weatherization job at a time until they prove reliable, when they can then eventually be given up to five jobs.
4. State and local inspection framework and procedures conducted at multiple levels and performed at various phases of weatherization work.
5. Requirement to use the state's weatherization Web-based reporting system capturing mandatory monitoring and reporting information.
6. Proven abilities of state and local program management who have successfully accomplished weatherization activities, some for more than 25 years.

City of Phoenix officials described two additional mechanisms they use to minimize weatherization contractor-related risks and to ensure their program success. First, they subsidize half of the required training costs for individuals who have demonstrated that they can be long-term, viable weatherization contractors. Second, the Phoenix program officials require that all new weatherization contractors participate in a city-managed weatherization mentoring program designed to assess their ability to conduct the weatherization field work and meet reporting requirements.

In addition to taking steps to monitor the use of funds, state officials are using performance measures to determine the effectiveness of Recovery Act weatherization funds that will meet and extend beyond the DOE required performance measurements. For example, ADOC officials have partnered with local utility companies to access 5 years of utility data to compare the pre and post energy consumption of weatherized homes to analyze whether improvements are achieving energy effectiveness over time. The tracking of post-weatherization energy savings will provide on-

going feedback to weatherization staff, highlighting measures or processes that provide high returns. According to ADOC, local operational changes can be based on this information, thereby improving cost-effectiveness.

ADOC Expects to Meet Federal Reporting Requirements and to Use the State's Centralized Reporting Process

ADOC is responsible for reporting on performance measures required under the Recovery Act to DOE, including the program expenditures, the number of homes weatherized, the number of jobs created and preserved, and the energy savings achieved. Currently, local service providers report to ADOC on regular Weatherization Assistance Program activity quarterly, but are now expected to report on Recovery Act-related activities monthly. In order to meet such requirements, ADOC plans to report performance measurement data collected in the ADOC Web-based reporting database described above to both DOE and to the Governor's centralized statewide reporting system quarterly. While ADOC officials expect all subrecipients to adjust as necessary to comply with Recovery Act Section 1512 reporting requirements,²⁶ ADOC does not anticipate any issues with local service providers' ability to comply in a timely manner, because of their established Web-based reporting structure and monitoring procedures. ADOC plans to report actual figures on program expenditures, weatherization units completed, and the number of jobs created and preserved for the first report due in October 2009.

Despite Guidance, Local Officials Remain Uncertain about How to Accurately Count Jobs Created and Need Further Clarification from ADOC

According to state and local officials, some local service providers remain uncertain about how to accurately count jobs created and need further clarification from ADOC. ADOC is developing an alternative methodology to assist local service providers in properly counting and tracking the number of jobs created as required by the Recovery Act reporting requirements. Currently, weatherization reports track the number of housing units completed, not hours worked. ADOC officials anticipate that local service providers would have difficulty gathering this information because contractors have tracked and reported housing units completed, use of funds, and the results of work completed, rather than the number of hours worked or number of jobs created. Furthermore, local service

²⁶Office of Management and Budget (OMB) Memorandum M-09-21 *Implementing Guidance for the Reports on Use of Funds Pursuant to the American Reinvestment Act of 2009* (June 22, 2009) provides guidance for carrying out the federal reporting requirements included in Section 1512 of the Recovery Act. However, this guidance does not impact other program-specific requirements in the Recovery Act and, as a result, agencies may issue additional and similar reporting requirements.

providers expressed concern that smaller contractors may not have the tracking mechanisms and administrative controls in place to manage the different reporting requirements and administrative tasks required of them to be in compliance.

In an effort to have consistent and cost-effective reporting from subrecipients, ADOC officials are developing an alternative way to determine the number of weatherization jobs created in order to comply with Recovery Act requirements without increasing reporting burdens on the contractors conducting the work. Their alternative methodology for determining the number of jobs created will use a statewide average number of hours it takes to complete different weatherization job tasks (such as duct insulation, window replacements, and weather stripping of doors), then apply those averages to the contracted work completed to generate the total number of Recovery Act-related hours worked which can be translated into the number of full-time equivalent jobs created. ADOC officials are currently sending out surveys to local service providers to obtain average number of hours worked for different weatherization tasks. ADOC officials plan to discuss this alternative for measuring the number of jobs created with DOE officials before the end of September. ADOC officials believe that this alternative will be an easier and more cost-effective way to count the number of weatherization hours worked and number of weatherization jobs created in their state, however, it is too early to assess whether this alternative methodology can successfully assist state and local officials in meeting Recovery Act reporting requirements.

State Comments on This Summary

We provided the Governor of Arizona with a draft of this appendix on September 8, 2009. The Director of the Office of Economic Recovery responded for the Governor on September 16, 2009. Also, on September 10, 2009, we received technical comments from the State of Arizona's Office of the Auditor General. The state agreed with our draft and provided some clarifying information which we incorporated.

GAO Contacts

Eileen Larence, (202) 512-6510 or larencee@gao.gov

Charles Jeszeck, (202) 512-7036 or jeszeckc@gao.gov

**Staff
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