Why GAO Did This Study

As the federal government confronts long-term fiscal challenges, it is critical to improve the efficiency of federal grants processes, such as grant closeout procedures that allow for the return of unspent balances to the Treasury. In 2008, GAO reported that about $1 billion in undisbursed funding remained in expired grant accounts in the largest civilian payment system for grants—PMS. For this statement, GAO provides information from its April 2012 report updating its 2008 analysis. GAO also describes federal grant spending over the last three decades and discusses other grant management challenges identified in its past work and that of others.

This testimony addresses (1) the amount of undisbursed funding remaining in expired grant accounts; (2) actions OMB and agencies have taken to track undisbursed balances; (3) GAO recommendations to improve grant closeout; (4) recent and historical funding levels for federal grants; and (5) GAO’s ongoing and future work on grants management issues.

What GAO Found

Closeout is an important final point of grants accountability. It helps to ensure that grantees have met all financial and reporting requirements. It also allows federal agencies to identify and redirect unused funds to other projects and priorities as authorized or to return unspent balances to the Department of the Treasury (Treasury). At the end of fiscal year 2011, GAO identified more than $794 million in funding remaining in expired grant accounts (accounts that were more than 3 months past the grant end date and had no activity for 9 months or more) in the Payment Management System (PMS). GAO found that undisbursed balances remained in some grant accounts several years past their expiration date: $110.9 million in undisbursed funding remained unspent more than 5 years past the grant end date, including $9.5 million that remained unspent for 10 years or more. Nevertheless, the more than $794 million in undisbursed balances remaining in PMS represents an improvement in closing out expired grant accounts with undisbursed balances in PMS compared to the approximately $1 billion GAO found in 2008. This improvement is notable given that the overall amount of grant disbursements through PMS increased by about 23 percent from 2006 to 2011.

When agencies made concerted efforts to address timely grant closeout, they and their inspectors general and auditors reported that they were able to improve the timeliness of grant closeouts and decrease the amount of undisbursed funding in expired grant accounts. GAO found that raising the visibility of the problem within federal agencies can also lead to improvements in grant closeouts. However, GAO’s review of agencies’ annual performance reports for fiscal years 2009 to 2011 found that systematic, agencywide information on undisbursed balances in grant accounts eligible for closeout is still largely lacking.

The challenge presented by undisbursed balances in expired grant accounts is just one of a number of grants management challenges identified in past GAO work. Addressing these challenges is critical to increasing the efficient and effective use of federal grant funds, which represent a significant component of overall federal spending. According to the Office of Management and Budget (OMB), federal outlays for grants to state and local governments, including Medicaid, increased from $91 billion in fiscal year 1980 (about $221 billion in 2011 constant dollars) to more than $606 billion in fiscal year 2011, accounting for approximately 17 percent of total federal outlays. During this 30-year period there has been a shift in grant spending, increasing the percentage of grant funding of Medicaid while decreasing the percentage of funding of non-Medicaid-related grant programs.

GAO work on grants over the last decade has identified a range of issues related to the management of grant programs, including the streamlining of grants management processes, the measurement of grant performance, grant lessons learned from implementing the American Recovery and Reinvestment Act of 2009, and internal control weaknesses. GAO will be looking at each of these grants management issue areas in future work for this Subcommittee.
Chairman Carper, Ranking Member Brown, and Members of the Subcommittee:

I appreciate the opportunity to discuss with you today the findings from our recent report for you on the timeliness of grant closeout by federal agencies, as well as some of the new and ongoing work we are doing for this Subcommittee on other key grants management challenges.¹ Closeout is an important final point of grants accountability that helps to ensure that grantees have met all financial and reporting requirements. It also allows federal agencies to identify and redirect unused funds to other projects and priorities as authorized, or to return unspent balances to the Department of the Treasury (Treasury). (See appendix I for an illustration of how and when federal agencies may redirect unused funds.) In a 2008 report to this Subcommittee, we found that timely grant closeout was a long-standing issue at federal agencies and that roughly $1 billion in undisbursed funding remained in the largest civilian payment system for grants.² Assessing grants management practices, such as ensuring that agencies follow proper closeout procedures, is critical to increasing the efficient and effective use of federal grant funds, which represent a significant component of federal spending. In fiscal year 2011, federal grants outlays to state and local governments, including Medicaid, accounted for approximately 17 percent of total federal outlays.³ Challenges involving grants management have been a repeated theme in our work over the last decade, and at your request, I will also briefly discuss some of the work we are doing for this Subcommittee on this important area.

My testimony today is drawn from our recent report to you on the timeliness of grant closeout as well as federal grants funding data from the Office of Management and Budget (OMB). It will address (1) the amount of undisbursed funding remaining in expired grant accounts; (2) actions OMB and agencies have taken to track undisbursed balances in grants eligible for closeout; (3) GAO recommendations on how to improve


³Federal grant outlays include the federal share of Medicaid funds that are sent to the states. Medicaid is the largest federal grant program.
grant closeout from our recent report; (4) recent and historical funding levels for federal grants; and (5) our ongoing and future work on grants management challenges.

To conduct our work on grant closeout, we analyzed data from the quarterly closeout reports provided to users of the Payment Management System (PMS), the largest civilian payment system for grants, which is administered by the Department of Health and Human Services’ (HHS) Program Support Center (PSC). PMS closeout reports list all grant accounts that remain open more than 3 months past the grant end date and for which there has been no disbursement in the preceding 9 months. We analyzed data from “dormant account reports” provided to users of a second payment system, the Automated Standard Application for Payments (ASAP) system, which reports accounts for federal grants that remain inactive for 2 years or more. We also conducted a web-based search for audit reports we have issued and those issued by federal inspectors general. We interviewed agency officials, including officials from OMB, and reviewed OMB circulars and other guidance related to grants management and performance reporting. We reviewed performance reports for the 24 agencies required to issue audited financial statements under the Chief Financial Officers Act of 1990 (CFO Act) for information reported on undisbursed balances in grants eligible for closeout. More detailed information on our scope and methodology for the grants closeout work can be found in our published report. To determine the level of federal grants funding and its changes over the last three decades, we used OMB data for fiscal years 1980–2011. For a more accurate comparison of grant spending from year-to-year, we converted each fiscal year’s outlays to constant 2011 dollars.

We conducted our performance audit on grant closeout from May 2011 to April 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to

4The Automated Standard Application for Payments (ASAP) system is administered jointly by the Department of the Treasury (Treasury) and the Federal Reserve Bank of Richmond.

5GAO-12-360, pp. 35-44.

obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. In addition, we are providing information on grants funding levels for the past three decades.

We found that as of September 30, 2011, more than $794 million in undisbursed balances remained in PMS in 10,548 expired grant accounts. These are accounts that were more than 3 months past the grant end date, had no activity for 9 months or more, and therefore should be considered for grant closeout. This is an improvement from 2008, when we reported that at the end of calendar year 2006, roughly $1 billion in undisbursed funding remained in expired PMS grant accounts. These expired grant accounts do not include accounts associated with grant programs for which the duration of the grant is not limited to a specific time period, such as payments to states for the Medical Assistance Program, known as Medicaid, and Temporary Assistance for Needy Families. This improvement is notable given that the overall amount of grant disbursements through PMS increased by about 23 percent from 2006 to 2011. However, more work needs to be done to further improve the timeliness of grant closeout and reduce undisbursed balances. We have highlighted three areas in need of particular attention.

First, we found that undisbursed balances remained in grant accounts several years past their expiration date. We found that 991 expired grant accounts containing a total of $110.9 million in undisbursed funding were more than 5 years past the grant end date at the end of fiscal year 2011. Of these, 115 expired grant accounts containing roughly $9.5 million in undisbursed funding remained open more than 10 years past the grant end date. Federal regulations generally require that grantees retain financial records and other documents pertinent to a grant for a period of 3 years from the date of submission of the final report. Over time, the risk increases that grantees will not have retained the financial documents and other grant information that federal agencies need to properly reconcile financial information and make the necessary adjustments to grant award amounts and amounts of federal funds paid to recipients. This could potentially result in the payment of unnecessary and unallowable costs.

Second, we found that a small percentage of grant accounts (a little more than 1 percent) with undisbursed balances of $1 million or more accounted for more than a third of the total undisbursed funds in expired

**Undisbursed Balances in Expired Grant Accounts Have Declined but More Action Is Needed**
grant accounts. Overall, 123 accounts from eight different federal agencies had more than $1 million in undisbursed balances at the end of fiscal year 2011 for a combined total of roughly $316 million in undisbursed balances. Accounts with undisbursed balances remaining after the grant end date can indicate a potential grant management problem. Data showing that some grantees have not expended large amounts of funding, such as $1 million or more, by the specified grant end date raise concern that the grantees may not have fully met the program objectives for the intended beneficiaries within the agreed-upon time frames.

Third, we found more than 28,000 expired grant accounts in PMS with no undisbursed balances remaining that had not been closed out as of the end of fiscal year 2011. According to data provided by PSC, PMS users were charged a total of roughly $173,000 per month to maintain the more than 28,000 expired grant accounts with zero-dollar balances listed on the year-end closeout report. This would represent roughly $2 million in fees if agencies were billed for these accounts for the entire year. While the fees are small relative to the size of the original grant awards, they can accumulate over time. If the grant has otherwise been administratively and financially closed out, then agencies are paying fees to maintain grant accounts that are no longer needed. However, the presence of expired grant accounts with no undisbursed funds remaining raises concerns that administrative and financial closeout—the final point of accountability for these grants, which includes such important tasks as the submission of financial and performance reports—may not have been completed.

In addition to data from PMS, we also reviewed data from the ASAP system and found that as of September 30, 2011, $126.2 million in undisbursed balances remained in 1,094 dormant grant accounts. Agencies can use the information in these reports to help identify accounts in need of attention and unspent funds available for deobligation. For example, agencies may want to focus attention on accounts where there has been no activity for a prolonged period. We found roughly $11 million in 179 accounts that had been inactive for 5 years or more.
We have found that when agencies made concerted efforts to address timely grant closeout, they, their inspectors general, and auditors reported that they were able to improve the timeliness of grant closeouts and decrease the amount of undisbursed funding in expired grant accounts. Agencies’ approaches generally focused on elevating timely grant closeouts to a higher agency management priority and on improving overall closeout processing. For example, in response to past audit reports, HHS officials reported increasing monitoring of grant closeout. Since fiscal year 2006, the HHS independent auditor had routinely reported on concerns with management controls over grant closeout, including a backlog of HHS grant accounts in PMS that were already beyond what the auditor considered a reasonable time frame for closeout. In fiscal year 2011, the independent auditor noted significant improvements in the closeout of grants in PMS. While we found that roughly three-fourths of all undisbursed balances in expired PMS grant accounts were from grants issued by HHS, we also found that the total undisbursed balances in these accounts represented the lowest percentage (2.7 percent) for any federal department included on the September 30, 2011, closeout report. In comments on our draft report, HHS reported that it had identified $116 million in undisbursed balances in PMS available for deobligation through a special initiative begun in 2011 and is updating existing department policies and procedures to improve the grant closeout process going forward.

In 2008, we recommended that OMB instruct all executive departments and independent agencies to annually track the amount of undisbursed balances in expired grant accounts and report on the status and

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7Independent auditors are independent accounting experts who conduct impartial audits of the financial statements of public and private organizations to ensure there are no misstatements, and assess whether organizations’ systems to detect and prevent fraud (internal controls) are effective. Independent auditors also provide consulting non-audit services in areas such as information technology.

8We excluded grant accounts from our analysis that did not have a defined end date, including large Medicaid formula grants for the Medical Assistance Program. The purpose of the PMS closeout report is to alert awarding agencies of accounts in PMS that remain open after their posted end date. If a grant does not have a defined end date then HHS staff consider the PMS closeout report merely as a reminder to the awarding agency of the open account. We did not exclude grant accounts for similar programs that were identified in the Catalog of Federal Domestic Assistance as Recovery-Act-related, because, to achieve the purposes of the Act, Congress explicitly directed federal departments and agencies to expend the funds made available in this Act as quickly as possible consistent with prudent management.
resolution of the undisbursed funding in their annual performance reports. At the time, OMB supported the intent of our recommendations, but its comments did not indicate a commitment to implement our recommendations. Starting in 2010, OMB has issued guidance to track and report on undisbursed balances in expired grant accounts to only certain federal departments and entities covered by the Commerce, Justice, Science, and Related Agencies Appropriations Act, as required by law. However, in its instructions, OMB equated “expired grant accounts” with expired appropriation accounts. Based on this definition, OMB’s guidance included grant accounts that were still available for disbursement and was not limited only to those grant accounts eligible for closeout. In our review of CFO Act agencies’ annual performance reports for fiscal years 2009 to 2011, we found that systematic, agencywide information on undisbursed balances in grant accounts eligible for closeout was largely lacking.

In our 2012 grant closeout report, we reiterate our recommendation that OMB instruct all executive departments and independent agencies to report on the status and resolution of the undisbursed funding in grants that have reached the grant end date in their annual performance reports, the actions taken to resolve the undisbursed funding, and the outcomes associated with these actions. In addition, we recommend that the Director of OMB take the following three actions:

- Revise the definition of “undisbursed balances in expired grant accounts” in future guidance issued to agencies to focus on undisbursed balances obligated to grant agreements that have reached the grant end date and are eligible for closeout.
- Instruct agencies with undisbursed balances still obligated to grants several years past their grant end date to develop and implement strategies to quickly and efficiently take action to close out these grants and return unspent funds to the Treasury when appropriate.
- Instruct agencies with expired grant accounts in federal payment systems with no undisbursed balances remaining to develop and implement procedures to annually identify and close out these accounts to ensure that all closeout requirements have been met and to minimize any potential fees for accounts with no balances.

OMB staff said that they generally agreed with the recommendations and will consider them as they review and streamline grant policy guidance.
OMB did not provide specific actions or time frames with which it would address the issues that we have raised. We will continue to monitor OMB’s action on our recommendations.

The challenge presented by undisbursed balances in expired grant accounts is just one of a number of grants management challenges we have identified in our past work. Grants continue to be an important tool used by the federal government to achieve national objectives. As the federal government confronts long-term and growing fiscal challenges, its ability to maintain the flow of intergovernmental revenue, such as through grant programs, could be constrained. To make the best use of federal grant funds, it is critical to address grants management challenges that could impact the efficiency and effectiveness of federal grants processes. Accordingly, the Subcommittee has requested that we examine a number of areas involving these issues in future work. However, before I discuss these I would like to put them in a broader context by briefly describing the level of recent federal grant spending and how it has changed over the last three decades.

While Grants Have Consistently Been a Significant Component of Federal Spending, the Focus of Grants Outlays Has Shifted In the Last 30 Years

Grants have been, and continue to be, an important tool used by the federal government to provide program funding to state and local governments. According to OMB, federal outlays for grants to state and local governments increased from $91 billion in fiscal year 1980 (about $221 billion in 2011 constant dollars) to over $606 billion in fiscal year 2011. Although many federal departments and agencies award grants, HHS, which administers the Medicaid program, is by far the largest grant-making agency, with grants outlays of almost $348 billion in fiscal year 2011, or about 57 percent of the total federal grants outlays that year. Even when Medicaid’s outlays of $275 billion are excluded, HHS remains the largest federal grant-making department. Figure 1 shows the total federal outlays for grants to state and local governments over the period from fiscal years 1980 to 2011, in constant dollars, and the increasing amount of this total that went to Medicaid over time.

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9We used OMB data on grants outlays to state and local governments for this testimony. Constant dollar amounts reflect adjustments for inflation (e.g., the purchasing power of the $91 billion spent in 1980 represents about $221 billion in fiscal year 2011 dollars).

10All further references to total or overall federal grants outlays refer to outlays to state and local governments.
It is important to note that although federal outlays for grants have increased during the past three decades, as shown in Figure 2, grants outlays as a percentage of total federal outlays in fiscal year 2011 was at a roughly comparable level to what it was more than 30 years earlier (15.5 percent vs. 16.8 percent). At the same time, Medicaid outlays increased from over 2 percent of total federal outlays in 1980 to almost 8 percent in 2011. The considerable increase in Medicaid outlays was offset by an approximately equivalent decrease in the share of outlays for all other grants.
Given the federal government’s use of grants to achieve national objectives and respond to emerging trends, this Subcommittee has recently requested that we conduct a number of grant-related reviews in support of its oversight efforts. Today, I would like to briefly highlight four areas where our previous work and that of the inspectors general and others have identified challenges, and where we are beginning the work you requested related to the management of grant programs. Specifically, they are the streamlining of grants management processes; the measurement of grant performance; grant lessons learned from implementing the American Recovery and Reinvestment Act of 2009 (Recovery Act); and internal control weaknesses in grants management processes.

For more than a decade, the federal government has undertaken several initiatives aimed at streamlining governmentwide grants management.
Over the years, Congress has expressed concern over the inconsistencies and weaknesses we and the inspectors general have found in grants management and oversight. In response to your request we plan to examine the progress OMB and federal grant governance bodies have made toward streamlining grants management. We also expect to assess what further actions should be taken to simplify processes, reduce unnecessary burdens, and improve the governance of streamlining initiatives. We plan to report our results next year.

We also expect to evaluate the extent to which there are governmentwide requirements for measuring and reporting grant performance and the extent to which federal agencies measure grant performance to report progress toward their goals, as well as offer assistance to grantees on collecting data and reporting grant performance. As with our streamlining work, the specifics of this grant performance reporting work are currently under development, and we anticipate a 2013 report. In our past work we have reported that effective performance accountability provisions are of fundamental importance in assuring the proper and effective use of federal funds to achieve program goals.

Under the Recovery Act, grants have played an important role in distributing federal funds in light of the most serious economic crisis since the Great Depression. As of June 2012, Treasury had paid out more than $250 billion in Recovery Act funds to state and local governments, much of it through grants. Given the significant investment made in the Recovery Act, and the considerable challenges facing our nation moving forward, this Subcommittee recognized the importance of collecting, analyzing, and sharing grant lessons and insights gained as a result of this process. Building on our previous reviews, we will examine lessons from the implementation of the Recovery Act—including specific examples of practices and approaches that worked as well as challenges encountered by federal, state, and local agencies. Among the potential issues to consider are the efforts to facilitate coordination and collaboration among federal, state, local, and nongovernmental partners and actions taken to enhance the organizational and administrative capacity of federal partners. Once again, we anticipate reporting to the Subcommittee next year.

Finally, in numerous reviews over the years, we have identified weaknesses in federal agencies’ processes for managing and overseeing grant programs. Among the issues we are planning to address in future work is how federal agencies can improve internal control over grants monitoring. We will also examine what improvements, if any, are needed
in federal agencies’ internal controls to help ensure the primary grantees are providing adequate oversight of subgrantees.

Concluding Observations

The improvements made in the timeliness of grant closeouts since our 2008 report demonstrate that congressional oversight can lead agencies to focus attention on a specific grant challenge, and result in real progress. However, our recent update of our earlier analysis of undisbursed balances also shows that more still needs to be done to close out grants; agencies would use their resources most effectively by focusing initially on older accounts with larger undisbursed balances. As our review of past grant work suggests, there are numerous other issues where congressional attention could also likely pay dividends. This is all the more relevant because federal grant programs remain important tools to achieve national objectives and continue to be a significant component of federal spending. We look forward to continuing to support this Subcommittee’s efforts to examine the design and implementation of federal grants and participating in its active oversight agenda.

Chairman Carper, Ranking Member Brown, and Members of the Subcommittee, this completes my prepared statement. I would be pleased to respond to any questions that you or other members of the Subcommittee may have.

Contacts and Acknowledgments

If you or your staff have any questions about this testimony, please contact me at (202) 512-6806 or czerwinski@gao.gov, or Beryl H. Davis, Director, at (202) 512-2623 or davisbh@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. GAO staff who made key contributions to this testimony are Phyllis L. Anderson, Assistant Director; Peter Del Toro, Assistant Director; Thomas M. James, Assistant Director; Kimberly A. McGatlin, Assistant Director; Laura M. Bednar, Maria C. Belaval, Anthony M. Bova, Amy R. Bowser, Virginia A. Chanley, Melissa L. King, Thomas J. McCabe, Diane N. Morris, and Omari A. Norman. Additional contributions were made by Andrew Y. Ching, Travis P. Hill, Jason S. Kirwan, Jennifer K. Leone, Cynthia M. Saunders, Albert C. Sim, and Michael Springer.
While there can be substantial variation among grant programs, figure 1 illustrates how closing out grants could allow an agency to redirect resources toward other projects and activities or return unspent funds to Treasury.

Figure 1: Deobligating Undisbursed Balances in Expired Grant Accounts

- **Award expiration date**: The grant reaches the end date determined by authorizing legislation or terms of the grant agreement established by the agency.
- **Grant closed out**: Awarding agency ensures the grantee has completed all work and administrative requirements; grantee liquidates all obligations properly incurred before the grant end date and submits all final financial, performance, and other reports.
- **Grant not closed out**: Undisbursed balances remain in grant accounts after the grant end date.
- **Agency's funds are still available for new obligations.**
- **Agency's funds are no longer available for new obligations.**
- **Funds are deobligated and used for new grants or other authorized purposes.**
- **Unspent funds are temporarily retained for making adjustments to existing obligations.**
- **Unspent funds are returned to the Treasury.**

Source: GAO analysis of OMB circulars and federal regulations.
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