

September 2010

RECOVERY ACT

Opportunities to Improve Management and Strengthen Accountability over States' and Localities' Uses of Funds (Mississippi)



GAO

Accountability * Integrity * Reliability

Appendix IX: Mississippi

Overview

The following summarizes GAO's work on the seventh of its bimonthly reviews of American Recovery and Reinvestment Act (Recovery Act) spending in Mississippi¹. The full report on all of our work, which covers 16 states and the District of Columbia, is available at <http://www.gao.gov/recovery>.

What We Did

We obtained information on four programs funded under the Recovery Act—Public Housing Capital Fund Formula Grants, Public Housing Capital Fund Competitive Grants, the Tax Credit Assistance Program (TCAP), and the Grants to States for Low-income Housing Projects in Lieu of Low-income Housing Credits Program under Section 1602 of division B of the Recovery Act (Section 1602 Program). Our work focused primarily on the status of program funding and the use of funds. As part of our review of public housing, we visited three public housing authorities, located in Meridian, Gulfport, and Picayune. Our work with TCAP and the Section 1602 Program included visits to the Mississippi Home Corporation located in Jackson and two housing projects, one in Pickens and the other in Pascagoula. For descriptions and requirements of the covered programs, see appendix XVIII of [GAO-10-1000SP](#).

Our work in Mississippi also included meeting with Tupelo city officials to determine the amount of Recovery Act funds the city had received or will receive directly from federal agencies and to learn how those funds are being used. We chose to visit Tupelo because its unemployment rate was above the state's average and it is one of the largest cities in Mississippi.

Finally, we updated information we previously reported on Mississippi's fiscal condition and on the efforts that the state has undertaken to ensure accountability of the Recovery Act funds that it has received.

What We Found

- **Public housing.** The Meridian Housing Authority (MHA) received an \$8.5 million Recovery Act Public Housing Capital Fund Competitive Grant. MHA plans to use this grant to help renovate a 113-unit public housing development. As of August 7, 2010, MHA had obligated \$520,356 and drawn down \$335,134 of the obligated funds. Also as of August 7, the Mississippi Regional Housing Authority Number VIII

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

(MRHA-8), which is located in Gulfport, Mississippi, had received a \$3,783,351 Recovery Act Public Housing Capital Fund Formula Grant and had expended a total of \$1,168,969. MRHA-8 is using the funds to remodel the office space at one housing development, re-roof 73 housing authority buildings, and conduct various renovations in 140 individual housing units. The Picayune Housing Authority (PHA) received a total of \$697,630 in Recovery Act funds from the Public Housing Capital Fund Formula Grant, and as of August 7, 2010, it had expended the full amount. PHA used the funds to renovate the bathrooms and kitchens in 22 units, as well as to replace the heating, ventilation, and air conditioning systems in another 92 units.

- **TCAP and the Section 1602 Program** The Recovery Act established two funding programs that provide capital investments in Low-income Housing Tax Credit (LIHTC) projects: (1) TCAP administered by the U.S. Department of Housing and Urban Development (HUD) and (2) the Section 1602 Program administered by the U.S. Department of Treasury (Treasury)². Before the credit market was disrupted in 2008, the LIHTC program provided substantial financing in the form of third-party investor equity for affordable rental housing units³. As the demand for tax credits declined, so did the prices investors were willing to pay for them, which created funding gaps in projects that had received tax credit allocations in 2007 and 2008. TCAP and the Section 1602 Program were designed to fill financing gaps in planned tax credit projects and jump-start stalled projects.

HUD awarded the Mississippi Home Corporation (MHC) \$21,881,803 in TCAP Recovery Act funding, and Treasury awarded MHC \$29,664,458 in Section 1602 Program funds. In turn, MHC awarded all TCAP and Section 1602 Program funds to 32 projects, with 15 receiving TCAP funds, 4 receiving Section 1602 Program funds, and 13 receiving a combination of TCAP and Section 1602 Program funds. According to HUD data, as of August 1, 2010, MHC had disbursed \$4,606,010 or 21 percent of the awarded TCAP funds. In addition, according to HUD

²State housing finance agencies allocate low-income housing tax credits to owners of qualified rental properties who reserve all or a portion of their units for occupancy for low income tenants. Once awarded tax credits, owners attempt to sell them to investors to obtain funding for their projects. Investors can then claim tax credits for 10 years if the property continues to comply with program requirements.

³Many affordable housing tax credit projects rely on LIHTCs together with other forms of subsidies such as HOME Investment Partnerships Program funds (HOME), Community Development Block Grant (CDBG) funds, and state funds.

data, as of July 31, 2010, MHC had not disbursed any Section 1602 Program funds.

MHC officials indicated that they are not concerned about disbursing seventy-five percent of TCAP funds by the February 2011 deadline. However, because of delays, MHC officials told us that project owners receiving Section 1602 Program funds may not meet the requirement of spending thirty percent of eligible project costs by the December 31, 2010 deadline. If a project owner fails to meet this deadline, then MHC must stop disbursing any additional Section 1602 Program funds to the project owner. MHC expects that it will not begin disbursing Section 1602 Program funds to projects until mid- to late-August.

- **Tupelo's use of Recovery Act funds.** Tupelo received six Recovery Act grants which totaled \$6,355,279. According to city officials, funds provided by the Recovery Act benefited the city. However, the officials told us that the city did not apply for some funds that would have helped the city meet its critical needs. Although officials identified water and sewer line improvements as a critical city need, Tupelo did not apply for Recovery Act funds for such improvements that were available through the Mississippi Clean Water and Drinking Water State Revolving Funds. According to a city official, the city chose not to apply for the funds because the city did not have 1) shovel-ready projects that met the objectives of the fund or 2) the resources to devote to quickly developing a project.
- **State fiscal condition.** Mississippi continues to experience significant fiscal challenges due to a decline in state revenues. Tax revenue collections for fiscal year 2010 were \$404 million, or 8.2 percent below expectations. The Governor stated that while preparing the fiscal year 2011 budget was a difficult process because of declining revenue, fiscal year 2012 will be even more challenging because federal stimulus funding will have ended.
- **Accountability.** The Mississippi Office of the State Auditor (OSA) and the Department of Finance and Administration (DFA) have contracted with national accounting firms to monitor and oversee Recovery Act funds. Through April 2010, BKD, the firm contracted by OSA, has tested 80 grants received by 34 grant recipients and reported a total of 101 instances where recipients did not comply with Recovery Act requirements. The greatest lack of compliance was with quarterly recipient reporting. KPMG, the firm contracted by DFA, is assessing selected state agencies for their compliance with Recovery Act provisions. As of June 30, 2010, KPMG had completed site visits at 12

state agencies and reviewed approximately 39 different grants. Similarly to BKD, KPMG found compliance problems with recipient reporting requirements.

Obligation of Mississippi's Sole Public Housing Competitive Grant Begins as the State's Formula Grants Continue to Be Expended

HUD awarded Recovery Act Public Housing Capital Fund competitive grant dollars meant to improve the physical condition of housing authority properties to only one of Mississippi's 52 public housing agencies—MHA. MHA received approximately \$8.5 million and as of August 7, 2010, had obligated \$520,356. Also as of August 7, MHA had drawn down \$335,134 of the obligated funds.

According to officials, MHA will use its Recovery Act competitive grant to help renovate a 113-unit public housing development, known as Frankberry Court. Each unit in this public housing development, which was originally constructed in 1939, will receive a number of improvements, including central heat and air conditioning units, new energy efficient windows, entry doors, roofs, and vinyl siding, as well as new baths and kitchens; energy star appliances; interior paint; and tile or carpeted floors. The existing on-site clubhouse will also be refurbished to accommodate tenant community services and a resident business center. Figure 1 shows the Frankberry Court development as it stands today, prior to renovation, as well as a newly built "affordable housing" development in Meridian that was constructed by the same developer and that serves as the model for the Frankberry Court renovation.

Figure 1: Frankberry Court Development, Prior to Renovation, and Model “Affordable Homes” in Meridian, Mississippi by the Same Developer



Exterior of Frankberry Court Development housing units, prior to renovation (left), and exterior of housing units by the same developer (right) that are serving as the model for Frankberry Court.



Exterior of Frankberry Court Community Center, prior to renovation (left), and exterior of the community center by the same developer (right) that is part of the development serving as a model for Frankberry Court.

Source: GAO.

MHA officials told us that the scope and estimated cost of the Frankberry project has remained consistent since MHA filed its Recovery Act competitive grant application. However, the timeline has slipped due to a delay in financing. Because the Recovery Act requires that housing agencies obligate competitive grant funds within one year of the funds

becoming available to them, MHA officials originally hoped to complete this task by January 1, 2010, well in advance of their September 23, 2010 deadline. Although MHA still plans to obligate its funds in advance of the mandated deadline, it does not plan to do so until September 9, 2010. The nearly \$11.9 million project will be partially financed through the sale of \$5.5 million in bonds and \$2.8 million in tax credits. The proceeds from the bonds will then provide a construction loan that MHA will eventually pay using \$4.9 million in Recovery Act funding and \$648,910 in low-income housing tax credit equity. As of August 4, 2010, MHA had a letter of agreement from a bank to both purchase the bonds and provide the construction loan and a letter from an equity fund agreeing to purchase the low-income housing tax credits. Officials at the HUD Mississippi Field Office stated that MHA might face some challenges due to today's weak economy, especially since the equity fund is to purchase tax credits in four installments based upon the progression of the project.

MHA officials expect that they will meet the requirement to expend 60 percent of their Recovery Act funds within 2 years of the date that the funds became available for obligation. The officials told us that 20 percent of their project funds will be automatically expended once HUD provides final project approval in late August and Recovery Act funds are transferred to an escrow account as collateral for the project's bond issue. The remaining project funds will then be drawn down monthly and invested as collateral for the bonds. Currently, officials believe they will meet the 60 percent expenditure deadline by April 2011, which is well in advance of their mandated September 23, 2011, deadline. Officials also added that they will continue to assess their progress in obligating and expending Recovery Act funds during weekly telephone conversations with their project staff and with HUD representatives at the Mississippi Field Office.

**Housing Authorities
Expend Recovery Act
Public Housing Capital
Fund Formula Grants for a
Variety of Projects**

Collectively, HUD provided Mississippi's 52 public housing agencies with approximately \$32.4 million in Recovery Act Public Housing Capital Fund formula grants. Similar to Public Housing Capital Fund Competitive Grants, HUD provides formula grant funds to housing authorities to improve the physical condition of their properties. As of August 7, 2010, the recipient public housing agencies had not only obligated the total \$32.4 million, but had also drawn down a cumulative total of about \$23.7 million of the obligated funds.

We visited two housing authorities that received Recovery Act Public Housing Capital Fund formula grants—MRHA-8 located in Gulfport, Mississippi and PHA in Picayune, Mississippi—both of which we previously visited and reported on in July and December 2009⁴. Based on its 2008 formula, HUD allocated \$3,783,351 in Recovery Act funds to MRHA-8 and as of August 7, 2010, the housing authority had expended a total of \$1,168,969. The projects and their value are shown in table 1. Officials told us that the remaining \$453,450 of Recovery Act funding has been obligated to help cover replacement decking for the Dan Stepney re-roofing project, architectural and engineering services, and administrative expenses. The administrative expenses include salaries for three years for an assistant and an on-site inspector, as well as the cost for three years of the authority’s telephone, fuel, training, travel, and insurance costs. HUD also provided PHA with \$697,630 in Recovery Act funds, which as of August 7, 2010, had been completely expended.

Table 1: Projects MRHA-8 Funded with Its Public Housing Capital Formula Grant

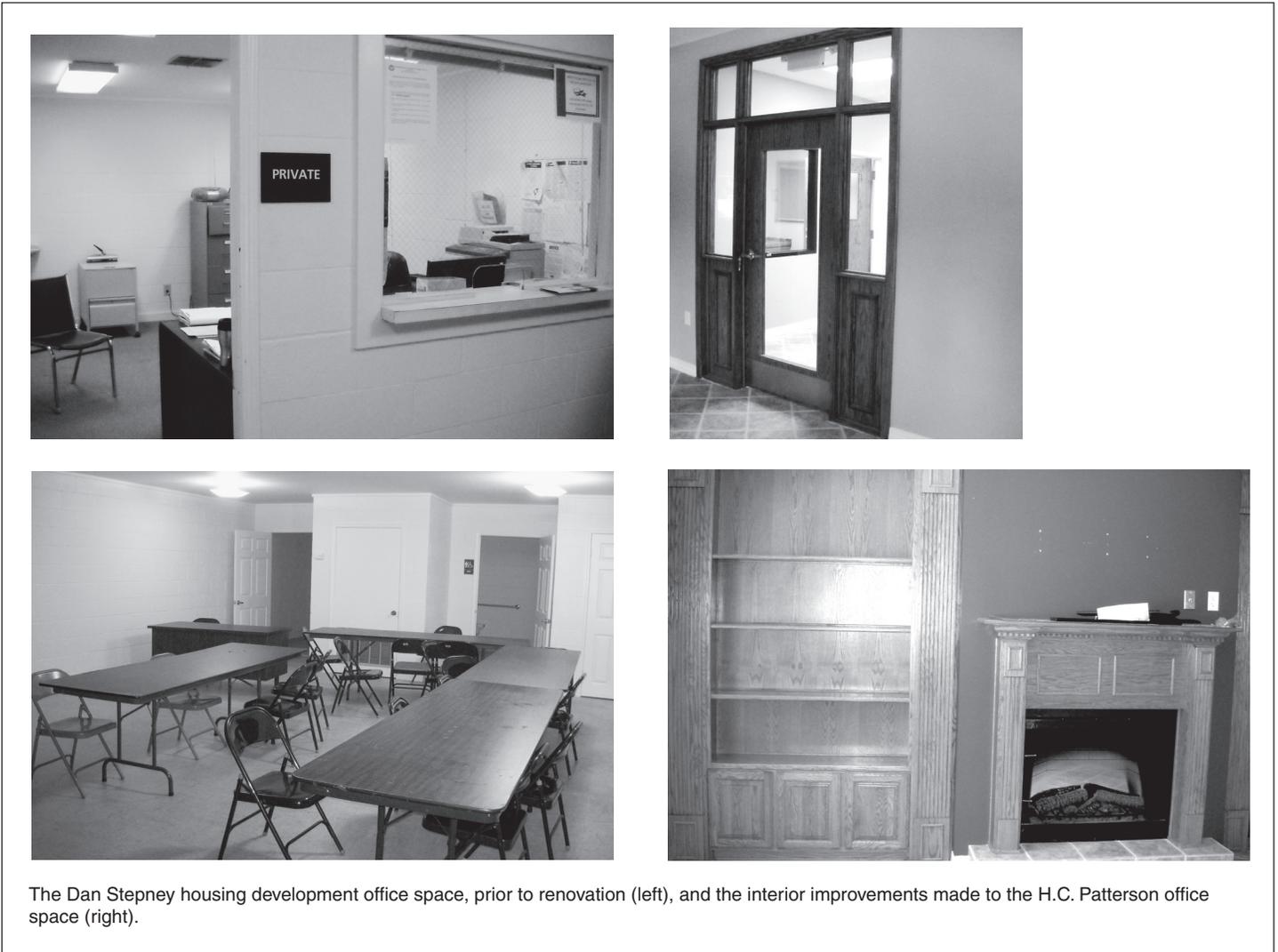
Housing development	Work funded by the Recovery Act	Contract award amount
H.C. Patterson	Office Remodel	\$228,600
Pecan Circle	Re-roof 38 buildings and install solar-powered attic fans	305,000
	Kitchen and Bath Renovation of 72 units	1,135,516
Dan Stepney	Re-roof 35 buildings and install solar-powered attic fans	287,785
	Miscellaneous Renovation of 68 units	1,373,000
Total		\$3,329,901

Source: MRHA-8.

The renovation of the office and community common area at the H.C. Patterson Housing Development in Poplarville, Mississippi is part of the MRHA-890 HUD-approved five year plan. The renovation includes the installation of a gas log fireplace, oak moldings, and oak built-in shelving, as well as ceramic tile floors. Figure 2 shows the improvements being financed with Recovery Act funds in comparison to the interior of another development’s office space that has yet to undergo renovation.

⁴GAO, *Recovery Act: States’ and Localities’ Current and Planned Uses of Funds While Facing Fiscal Stresses (Appendixes)*, GAO-09-830SP (Washington, D.C.: May 26, 2010); and *Recovery Act: Status of States’ and Localities’ Use of Funds and Efforts to Ensure Accountability (Appendixes)*, GAO-10-232SP (Washington, D.C.: December 10, 2009).

Figure 2: Columbia, Mississippi's Dan Stepney Housing Development Office, Prior to Renovation, and the Recovery Act-Financed Interior Improvements at the Poplarville H.C. Patterson Housing Development Office



The Dan Stepney housing development office space, prior to renovation (left), and the interior improvements made to the H.C. Patterson office space (right).

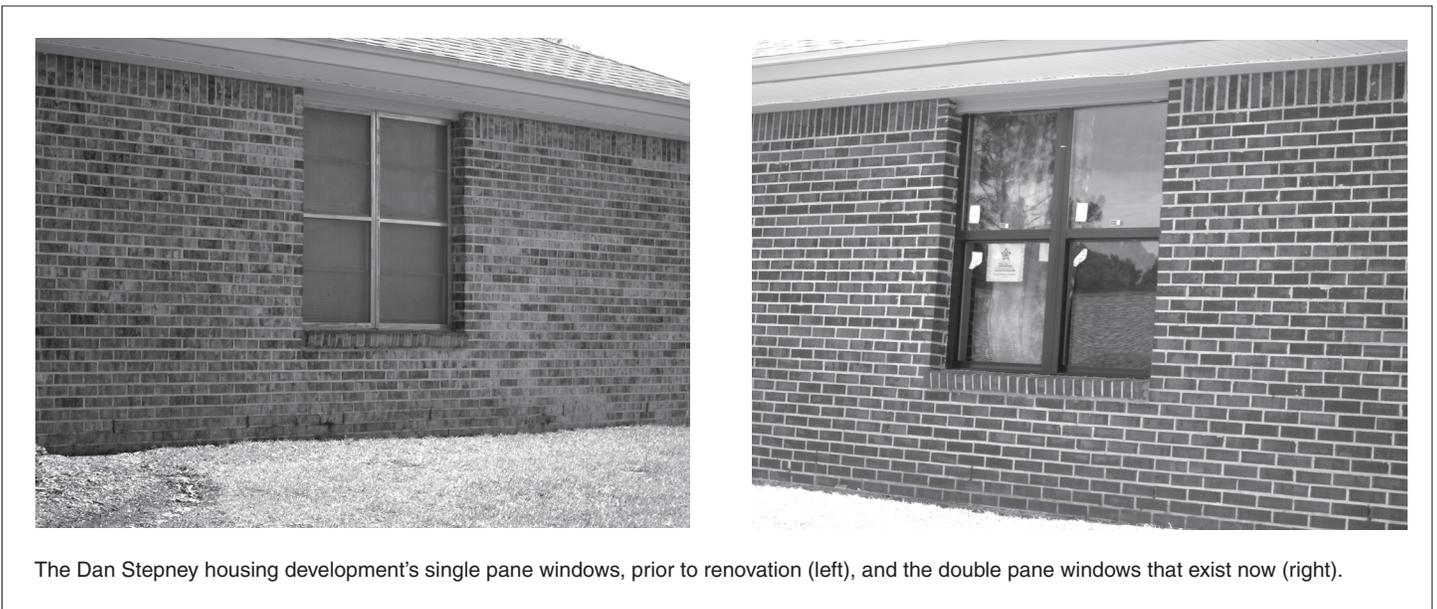
Source: GAO.

Although MRHA-8 planned to complete the H.C. Patterson renovation by April 2010, the contract administrator for this project told us that MRHA-8 now plans to close the contract without all work being completed. The contract administrator told us that the contractor not only performed substandard work but also failed to complete some work entirely. He also said that MRHA-8 officials plan to charge the contractor an amount equal to the cost of having another contractor repair the substandard work and

complete the unfinished work, as well as require the contractor to pay liquidated damages. According to the contract administrator, MRHA-8 will then decide whether to use its own staff to complete the project, hire another contractor to complete it, or implement another remedy that is allowed under procurement rules.

MRHA-8 is also making miscellaneous renovations to all 68 units of its Dan Stepney Housing Development in Columbia, Mississippi. These renovations include the replacement of single pane windows with energy efficient double pane windows; installation of solar-assisted hot water heaters; new cabinets, energy efficient refrigerators, and stoves in each unit's kitchen; and new bathtubs, water saving toilets, vanities, mirrors, lights, fans, and receptacles in each unit's bathroom. Figure 3 shows the windows at the Dan Stepney Housing Development as they existed before renovation and the windows after replacement.

Figure 3: Dan Stepney Housing Development's Window Replacement

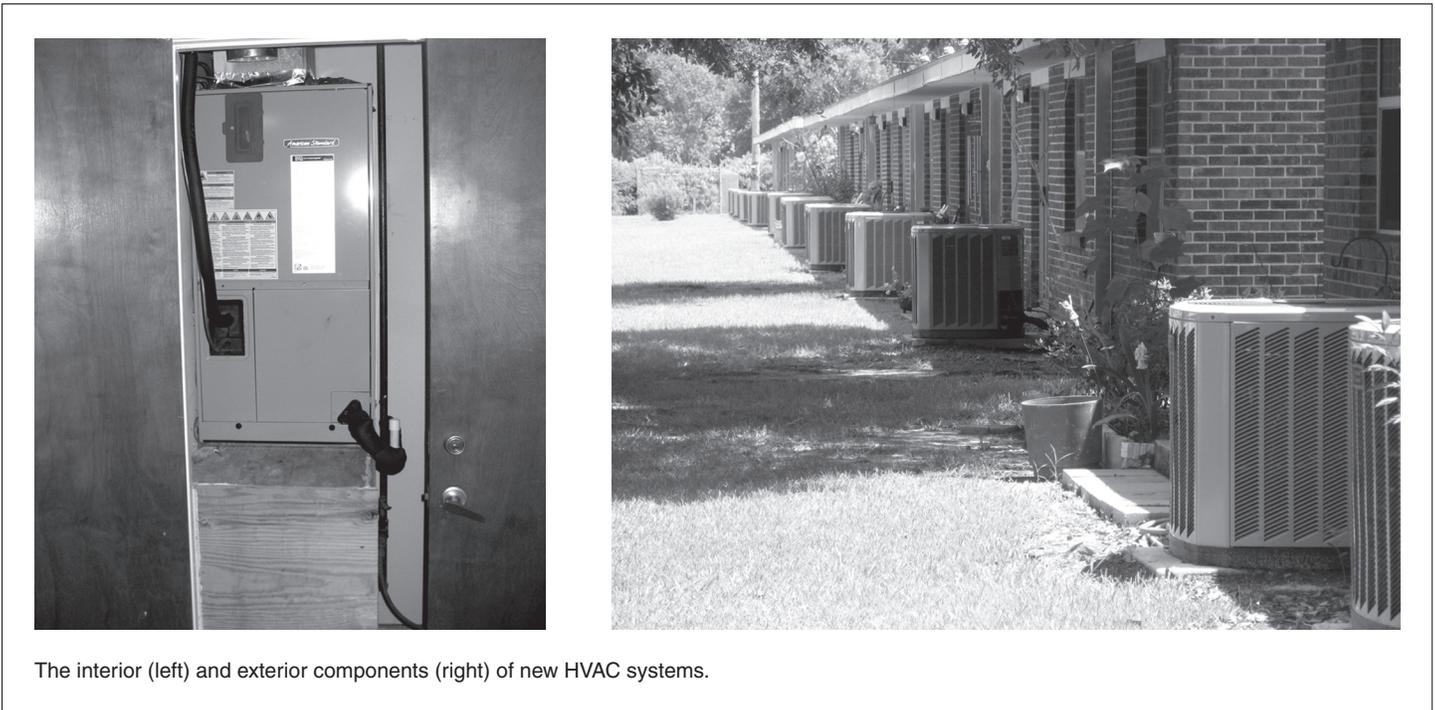


Source: GAO.

As we previously reported, PHA officials used Recovery Act funds to renovate bathrooms and kitchens in 22 units, as well as to replace the heating, ventilation, and air conditioning (HVAC) systems in another 92

units⁵. The interior and exterior components of these 92 new HVAC systems are shown in Figure 4.

Figure 4: New HVAC Systems Financed with a Public Housing Capital Fund Formula Grant and Installed at a Picayune, Mississippi Housing Development



Source: GAO.

Field Office Believes Recovery Act Funds Have Improved Monitoring Efforts

The HUD Mississippi field office Director told us that Recovery Act funds have enabled HUD headquarters to provide her office with the financial resources needed to conduct both remote and on-site reviews. In particular, the field office conducted “quick look” reviews of five Mississippi housing authorities that had obligated less than 90 percent of their Recovery Act formula funds as of February 26, 2010. The field office found deficiencies at only one of the housing authorities reviewed, the Brookhaven Housing Authority. Field office officials told us that its policy

⁵Recovery Act: Status of States’ and Localities’ Use of Funds and Efforts to Ensure Accountability (Appendixes) [GAO-10-232SP](#).

committee considered Brookhaven's use of funds for a security contract to be an improper use of funds. In addition, the officials said that Brookhaven replaced existing funding for the contract with Recovery Act funds, an action known as supplanting, which the Recovery Act does not allow. At this time, HUD plans to recapture \$153,787.64 in funding.

The field office Director also explained that her office both assists and provides guidance to housing authorities in their preparation of recipient reports required by the Recovery Act. The director told us that the field office reminds the housing authorities of upcoming deadlines, keeps track of the housing authorities that have reported, and provides support for technical problems. However, while the field office will question officials at a public housing authority if the officials observe discrepancies in the authorities' reported jobs data, the field office does not review the integrity of the data as all data quality reviews are conducted at HUD headquarters.

Housing Authorities Confirm Jobs Data in Different Ways

We spoke with officials from two housing authorities about their method of confirming the jobs data that they report. A PHA official told us that she asks PHA's on-site modification coordinator to verify the accuracy of the number of jobs that contractors report as created and retained. The coordinator compares the employees on the contractor's weekly time sheet with the information documented in the coordinator's daily on-site reports. An MRHA-8 official explained that he accepts the jobs data that his contractors certify and report to him in writing. In addition, officials from MRHA-8's contracting office verify this information by checking it against the contractor's certified payroll.

TCAP and Section 1602 Program Provide Needed Project Financing but Create Financial Burden for Mississippi Home Corporation

The Recovery Act established two funding programs that provide capital investments in LIHTC projects: (1) TCAP administered by HUD and (2) the Section 1602 Program administered by Treasury⁶. Before the credit market was disrupted in 2008, the LIHTC program provided substantial financing in the form of third-party investor equity for affordable rental housing units. As the demand for tax credits declined, so did the prices investors were willing to pay for them, which created funding gaps in projects that had received tax credit allocations in 2007 and 2008. TCAP and the Section 1602 Program were designed to fill financing gaps in planned tax credit projects and jump-start stalled projects.

Housing Finance Agencies and Project Owners Must Meet Disbursement and Expenditure Guidelines

Under the Recovery Act, housing finance agencies (HFAs) responsible for administering TCAP projects must disburse 75 percent of the funds that they receive by February 2011; project owners must expend the TCAP funds that they receive by February 2012. The Recovery Act requires that all Section 1602 Program awards be made by December 2010, or the HFA must return the unawarded funds to Treasury. Treasury's deadline for HFAs to disburse all Section 1602 Program funds is December 31, 2011. However, Treasury requires that individual project owners spend 30 percent of their eligible project costs by December 31, 2010 in order to continue receiving Section 1602 Program funds in 2011⁷.

MHC Concerned that Projects Funded by the Section 1602 Program May Have Difficulty Meeting Spending Deadline

HUD awarded the MHC \$21,881,803 in TCAP Recovery Act funds and Treasury awarded MHC \$29,664,458 in Section 1602 Program funds. In turn, MHC awarded all TCAP and Section 1602 Program funds to 32 projects, with 15 receiving TCAP funds, 4 receiving Section 1602 Program funds, and 13 receiving a combination of TCAP and Section 1602 Program funds. According to HUD data, as of August 1, 2010, MHC had disbursed \$4,606,010 or 21 percent of the awarded TCAP funds. In addition, according to HUD data, as of July 31, 2010, MHC had not disbursed any Section 1602 Program funds.

⁶State housing finance agencies allocate low-income housing tax credits to owners of qualified rental properties who reserve all or a portion of their units for occupancy for low income tenants. Once awarded tax credits, owners attempt to sell them to investors to obtain funding for their projects. Investors can then claim tax credits for 10 years if the property continues to comply with program requirements.

⁷Project owners must spend 30 percent of the project's adjustable basis for land and depreciable property by December 31, 2010.

MHC officials indicated that they are not concerned about disbursing seventy-five percent of TCAP funds by the February 2011 deadline. However, because of delays, MHC officials told us that project owners receiving Section 1602 Program funds may not meet the requirement of spending thirty percent of eligible project costs by the December 31, 2010 deadline. If a project owner fails to meet this deadline, then MHC must stop disbursing any additional 1602 Program funds to the project owner. MHC expects that it will not begin disbursing Section 1602 Program funds to projects until mid- to late-August. MHC noted several reasons for this delay. First, MHC officials told us that MHC's board delayed its request for Section 1602 Program funds to Treasury until February 2010, while the board assessed program risks related to Treasury's requirements for recapture of funds. This included an assessment of the requirement that makes MHC responsible for returning Section 1602 Program funds to Treasury if a project owner fails to complete the project or meet LIHTC requirements⁸. Further, MHC explained that delays in the approval of legal documents by investors and lenders prevented MHC from disbursing funds to the projects and delayed most Section 1602 Program development loan closings until mid-to late August.

Additional TCAP and Section 1602 Program Responsibilities Create Burden for MHC

For the TCAP and Section 1602 Program, HUD and Treasury require state Housing Finance Agencies (HFA) to exercise more management of projects than the agencies exercise under the standard LIHTC program. Normally IRS requires HFAs to review LIHTC projects at least annually to determine project owner compliance with rent and income limits and with tenant qualifications. Additionally, every three years the Agency must conduct on-site inspections of all LIHTC buildings, which includes inspecting at least 20 percent of the LIHTC units and the resident files associated with those units. Under the TCAP and Section 1602 programs, however, HFAs are obligated to perform asset management, which imposes ongoing responsibilities on the HFAs for the long-term viability of each project. For example, an HFA's asset management may include monitoring current financial and physical aspects of project operations, such as conducting analyses or approving operating budgets, developing cash flow trends, and monitoring reserve accounts, as well as performing physical inspections. Asset management activities will also examine long-

⁸GAO reported previously on the risks and responsibilities of recapture for HFAs under the TCAP and Section 1602 programs. See GAO, *States' and Localities Uses of Funds and Actions Needed to Address Implementation Challenges and Bolster Accountability*, [GAO-10-604](#) (Washington, D.C.: May. 26, 2010).

term issues related to plans for addressing a project's capital needs and changes in market conditions, as well as recommending and implementing plans to correct troubled projects. In addition, HFAs will ensure compliance with LIHTC requirements as part of its asset management activities. Further, HFAs are responsible for returning TCAP and Section 1602 Program funds to HUD and Treasury, respectively, if a project fails to comply with LIHTC requirements⁹.

MHC told us that they are taking a number of actions to meet the asset management requirements of the TCAP and the Section 1602 Program. Foremost, MHC requires program owners of all TCAP and Section 1602 Program funded projects to have investors. MHC is required to repay funds to HUD and Treasury in accordance with their respective guidelines if a project owner fails to meet LIHTC requirements during the 15-year compliance period. MHC believes that its risk of repayment is further reduced because investors often provide additional oversight and monitoring to ensure that LIHTC requirements are met.

In addition to requiring the involvement of investors, MHC is hiring additional staff, consultants and purchasing equipment, vehicles, and storage space. MHC will hire additional employees to carry out asset management tasks, and it is increasing its use of environmental consultants and lawyers to handle the additional environmental and legal reviews required by TCAP and the Section 1602 Program. MHC has also modified existing software and purchased scanners to handle the added paperwork generated by the programs. Last of all, MHC plans to purchase additional vehicles so that it can increase the number of site visits to projects and to purchase additional space to store program documents.

MHC projects that these asset management activities will cost \$500,000 in the first year and an additional \$1,000,000 over the next 5 years. However, MHC has not increased fees charged to project owners because it believes that project owners are already burdened in a depressed market, and adding fees would only serve to further hinder recovery of the LIHTC

⁹In contrast, under the conventional LIHTC program, HFAs are not liable for recapturing funds if a project owner fails to comply with LIHTC requirements. Rather, their obligation is to report any noncompliance to the IRS, and the IRS takes any further actions with respect to recapture. GAO reported previously on the risks and responsibilities of recapture for HFAs under the TCAP and Section 1602 Program. See [GAO-10-604, States' and Localities' Uses of Funds and Actions Needed to Address Implementation Challenges and Bolster Accountability](#), (Washington, D.C.: May. 26, 2010).

market. However, MHC officials told us that it was necessary to adjust the fiscal year 2010 and 2011 budgets because of increased costs. For example MHC told us that it does not plan on funding any Habitat for Humanity loans, which it has funded in the past.

Paying Prevailing Wage Rates May Create Burden for Project Owners

According to MHC officials, project owners consider the Recovery Act's requirement that laborers and mechanics working on TCAP projects be paid prevailing wages to be burdensome. Some developers told us that the prevailing wage standards can add to overall costs in certain markets. For example, the project owner of one project that we visited told us that the requirement to pay prevailing wages increased the project's overall cost by 15 to 20 percent.

Low Income Housing Tax Credit Program in Mississippi Attracting Fewer Investors and Projects Experience Financing Gaps

According to MHC officials, investors look at every project in Mississippi as rural and expect that project income will be very low or non-existent. As a result, investors scrutinize the financials on Mississippi projects. MHC officials said that in a market that is still stabilizing, a state like Mississippi is slow to rebound and investor interest is low.

Until the Recovery Act provided TCAP and Section 1602 Program funding, project owners said many projects were stalled. To restart the projects, project owners sought funds from several sources. Some projects that we reviewed included financing provided by investors, construction loans, the Section 1602 Program, TCAP, or both the Section 1602 Program and TCAP. Often all funding sources had to be pulled together simultaneously, because if one source of funding was not in place, it was difficult to acquire other sources. In particular, investors wanted the assurance that Section 1602 Program funding provided, as well as the increased equity that the funds brought to the project. For example, one project owner told us that TCAP provided the gap financing to proceed with the project. He said that without TCAP financing he would have been unable to complete the project.

Another project's owner told us that the current market conditions forced some syndicators out of business. The project owner said that within the last 3 years, the original syndicator for this project defaulted, which forced him to seek additional investors. He told us that he would not have been able to attract additional investment without the Section 1602 Program because investors want to be sure before committing funds that the funding from all sources will be sufficient to complete the project.

Recipient Reporting Requirements Apply Only to TCAP and Not Section 1602

Section 1512 of the Recovery Act describes recipient reporting requirements, including the requirement to estimate the number of jobs created and retained; but the requirements apply only to programs under division A of the Recovery Act, which includes TCAP. The Section 1602 Program is under division B of the Recovery Act, and, therefore, not subject to section 1512 requirements. Section 1512 requires recipients to file quarterly reports on the number of full-time equivalent jobs created or retained by funds spent through programs funded by division A of the Recovery Act during that quarter. Jobs are to be counted in accordance with methodology provided by the Office of Management and Budget (OMB).

In contrast, Treasury collects its own project information through quarterly performance reports submitted to Treasury by HFAs. HFAs are required to make only one report of jobs created or retained by Section 1602 Program funds. HFAs submit estimated information on the number of full-time equivalent jobs to be created or retained by the entire project with the first quarterly report for each project. The number of jobs reported to Treasury need not be reduced to reflect parts of the project not funded under the Section 1602 program.

MHC officials told us that MHC is responsible for recipient reporting for projects that receive TCAP funds. However, through June 2010, the officials said that they had not disbursed any TCAP funds and, therefore, had not reported that any jobs were created or retained with TCAP funds. The officials also told us that they anticipate that they will disburse TCAP funds during the next quarter and report jobs for the first time in the September 2010 quarterly report. MHC officials told us that they will rely on project owners to report accurate jobs information, but they plan to cross check the number of jobs reported with the payroll information that project owners must provide to ensure prevailing wages are paid to laborers.

HUD issued general guidance on how to report the jobs for TCAP projects that are partially funded with Recovery Act funds and MHC provided the guidance to the project owners. In one instance, MHC also contacted HUD for guidance on how to report jobs for projects that were completed prior to receiving TCAP funds. In addition, a project owner told us that MHC is to provide job reporting guidance when he closes on his TCAP funding.

MHC is also responsible for reporting the jobs that are created and retained when a project is financed with Section 1602 Program funds. MHC said it had not disbursed any Section 1602 Program funds as of the

end of June 2010, and it had not reported that any jobs had been created or retained. MHC officials told us that they expect to disburse Section 1602 Program funds during the next quarter, and the officials indicated that jobs reported will be based on data provided by project owners. Although Treasury guidance requires that HFAs report to Treasury on awards of Section 1602 Program funds made to project owners, the guidance does not discuss how to compute full-time equivalent positions for job reporting. MHC also said that it cannot rely on OMB guidance regarding the calculation of full-time equivalent positions because OMB guidance does not apply to Treasury's Section 1602 Program. Further, Treasury's guidance does not require HFAs to prorate the number of jobs created or retained by a project when the project is only partially funded by the Section 1602 Program.

Recovery Act Funds Benefit the City of Tupelo

We visited the City of Tupelo to assess the impact of Recovery Act funding on a local government. Tupelo is located in northeastern Mississippi and is the seventh largest city in the state in terms of population. According to a 2008 U.S. Census Bureau estimate, the city's population was 35,270, which was a slight increase over the 2000 population estimate of 34,211. According to the last complete census, about 70 percent of Tupelo's citizens are white and about 29 percent are African-American, with the remaining 1 percent made up of various other races. The 2008 census data also showed that the city's median household income was \$39,528, which is lower than the U.S. median household income of \$52,175.

According to city officials, the city's leading industry is furniture manufacturing. However, the recession prompted a number of manufacturers to relocate operations overseas in order to save costs. City officials told us that the local furniture industry is now showing signs of improvement and a number of manufacturers that had left may be returning to the area, causing officials to be optimistic that the local economy will soon improve. Additionally, on June 17, 2010, Toyota announced plans to resume construction of a vehicle manufacturing plant located near Tupelo whose construction had been postponed due to economic conditions. The facility will employ approximately 2,000 people and, according to city officials, will also create more than 3,000 indirect jobs.

City officials told us that the city first began to feel the impact of the recession in 2008. Between 2008 and 2009, as shown in table 2, the unemployment rate rose and sales tax revenues, which are a major source of the city's operating funds, dropped almost 6 percent.

Table 2: Tupelo Unemployment Rates and Tax Revenues

Fiscal year	Unemployment rate	Percentage change	Sales tax revenues	Percentage of increase/ (decrease) in revenues
2007	6.4	Not applicable	\$16,776,574	Not applicable
2008	7.4	1.0	\$17,049,934	1.63
2009	11.3	3.9	\$16,089,272	(5.63)
2010	12.3 ^a	1.0	\$16,439,272 ^b	2.18

Source: Department of Labor (unemployment data); City of Tupelo (sales tax data).

^aPreliminary.

^bProjected.

However, despite the recession and its impact on the city’s manufacturing base, city officials have kept Tupelo’s financial condition stable. The city develops its budget on a “pay-as-you-go” basis. That is, the city bases its expenditures on the revenues that it expects to collect without drawing on the city’s rainy day fund unless absolutely necessary. City officials review revenues monthly, and, if warranted, adjust revenue projections, which can precipitate adjustments to the expenditure budget. One indication of the city’s financial strength is the high bond rating of Aa3 that Moody’s Investor Service has given Tupelo’s General Obligation Bonds¹⁰.

Recovery Act Dollars Helped Tupelo Meet Some Needs

Tupelo received six Recovery Act grants, which totaled \$6,355,279. The funding agencies for the grants were the U.S. Department of Transportation (DOT), the U.S. Department of Justice (DOJ), the Environmental Protection Agency (EPA), the U.S. Department of Energy (DOE), and the U.S. Army Corps of Engineers. Table 3 presents the Recovery Act grants that the City of Tupelo received from the various federal agencies, the amount of each grant, and the specific purpose for which each grant was used.

¹⁰A bond rating represents a credit risk evaluation and an Aa3 investment grade is indicative of bonds judged to be high quality by all standards.

Table 3: City of Tupelo Recovery Act Award Summary

Recipient Entity	Funding agency	Funding program	Award amount	Use of funds
City of Tupelo	DOT	Highway Infrastructure Investment Grant	\$1,227,688.00	Construction of a new bridge
City of Tupelo	DOJ	Justice Assistance Grant	\$91,005.00	Purchase of law enforcement equipment
City of Tupelo	EPA	Clean Water State Revolving Fund	\$503,875.00	Construction of replacement sewer lines
City of Tupelo	DOE	Energy Efficiency and Conservation Block Grant	\$146,000.00	Retrofitting the lighting system at a local baseball field with a higher efficiency system
		Energy Efficiency and Conservation Block Grant	\$35,200.00	Replacement of the city's existing computer servers with high-efficiency servers
City of Tupelo	U.S. Army Corps of Engineers	Civil Program Financing-Operation and Maintenance	\$4,351,511.00	Major drainage improvements

Source: City of Tupelo.

Tupelo Did Not Apply for Some Available Recovery Act Funds

Although the Recovery Act provided funds for needed projects, city officials identified infrastructure improvements as their city's most critical need. The officials told us water and sewer lines and drainage lines need to be improved, work is needed on a number of city roads and bridges, and the city has blighted areas that it wants to improve where abandoned and structurally deteriorating buildings attract criminal activity.

Although water and sewer line improvements were identified as a critical city need, officials decided not to apply for Recovery Act funds that were available for such improvements through the Mississippi Clean Water and Drinking Water State Revolving Funds. According to the City of Tupelo's grant administrator, the city chose not to apply for the funds for two main reasons—(1) the city did not have shovel-ready projects that met the objectives of the fund and (2) it did not have the resources to quickly devote to developing a project. At the time that the Mississippi Department of Environmental Quality requested proposals for Recovery Act projects, the city's Water & Light Department was in the process of finishing up a major wastewater treatment project, carrying out day-to-day departmental work, and completing some smaller special projects. In addition, the department was devoting all available planning personnel to negotiating, engineering, and acquiring easements on the Toyota water and sewer project, which crossed city and county lines and required an extraordinary amount of personnel. With all of these projects under way, the city lacked

the resources to quickly develop another project in time to apply for the funding.

Energy Efficiency and Conservation Block Grant Improves City Park and Computer System

As part of our visit to Tupelo we looked at the execution of one grant in particular. Tupelo received a Department of Energy Efficiency and Conservation Block Grant (EECBG) that totaled \$181,200. As shown in table 3, the grant provided funding for two projects. The first provided \$146,000 for the city to retrofit field lighting at a public sports field which is located in one of the city's most heavily used parks. The new lighting system is expected to be highly efficient and will reduce energy usage by removing halide lights and replacing them with a photometric system which automatically adjusts the field lights based on existing environmental light levels. The second grant provided \$35,200 for the city to replace its existing computer server technology with high-efficiency virtual servers that reduce power consumption while increasing server capacity. City officials report that both projects are now complete and that 99.5 percent of the funds provided by the grant were obligated and expended. Because the lighting project was completed under budget, the city is returning the remaining \$959.75 to DOE.

City officials indicated that their Recovery Act reporting for the EECBG was consistent with the guidance provided by OMB. Four people from the city government provided routine oversight for each disbursement of the EECBG grant money by reviewing each transaction. Officials also stated they complied with Recovery Act provisions applicable to EECBG, such as the requirement to pay laborers and mechanics employed on Recovery Act projects the prevailing wage for the area and the requirement to purchase iron and steel for Recovery Act projects from American sources.

Concerns over Recovery Act Compliance Limit Applications for Funds

City of Tupelo officials explained that the Recovery Act funding created a dilemma for the city. Officials knew that the funds could benefit the city, but felt the long-term cost could outweigh the short-term benefit. For example, the Recovery Act requires that laborers and mechanics employed by contractors and subcontractors on projects funded by Recovery Act

funds be paid prevailing wages¹¹. City officials felt this provision could create compliance hardships that could lead to increased indirect costs, such as higher wages paid to workers after the Recovery Act expires or the need to pay increased wages for work performed on non-Recovery Act projects. Such increases could raise the costs of local employers and the municipality. These concerns made the city reluctant to apply for a number of associated Recovery Act grants. Additionally, the city avoided becoming dependent on Recovery Act funding by selecting infrastructure-related, “stand-alone” projects with minimal or no ongoing costs that would obligate long-term financial support above and beyond what the city could adequately fund. For example, the city did not apply for DOJ grants for Community Oriented Police Services, which would have allowed the city to hire additional police officers, because it did not want the financial burden of the requirement to retain those police officers for at least one additional year after the Recovery Act grant expired. Instead the city applied for Justice Assistance Grants which enabled the city to purchase needed equipment.

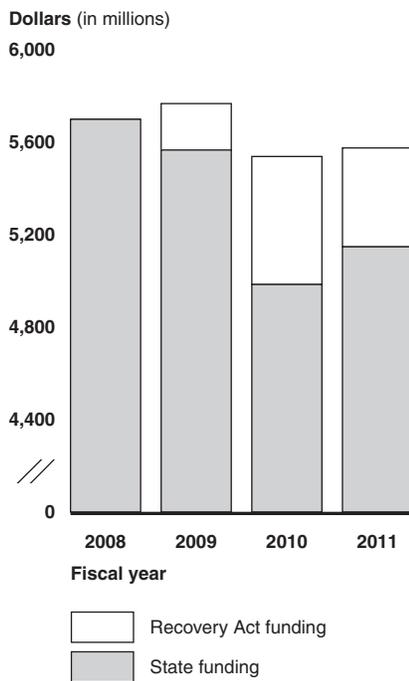
Additionally, the city’s grant administrator characterized the administrative cost associated with Recovery Act grants as high. For example, the city spent approximately \$300,000 of a \$2.5 million grant it received for a bridge project on administrative costs, including environmental studies needed because the project was near wetlands. Furthermore, the grant administrator told us that it takes 2 weeks, or about 80 hours, to complete the recipient report required by section 1512 of the Recovery Act each quarter, as well as the other reports required by the grantor agencies.

¹¹The Recovery Act, requires all laborers and mechanics employed by contractors and subcontractors on projects funded directly by or assisted in whole or in part by and through the federal government with Recovery Act funds be paid wages at rates that are not less than those paid on local projects of a similar character as determined by the Secretary of Labor. Recovery Act div. A, § 1606, 123 Stat. 303.

Recovery Act Funds Helped Mississippi Address Decline in State Revenues

As shown in figure 5, from fiscal year 2008 through fiscal year 2011 the Mississippi state budget is projected to decline from \$5,709 billion to \$5,148 billion or more than \$561 million. The primary reason for the decrease is a decline in state revenues. However, as figure 5 shows, the use of Recovery Act funds helped offset the decline in state funding.

Figure 5: State Funding, Fiscal Years 2008 to 2011



Source: Mississippi Department of Finance and Administration.

Note: Recovery Act funding includes State Fiscal Stabilization Fund monies and Increased Federal Medical Assistance Percentage Funds.

During fiscal year 2009 and fiscal year 2010 the state used more than \$201 million and \$553 million in Recovery Act funds, respectively, to help reduce the impact of declining state revenues. Likewise, the state plans to use more than \$428 million in Recovery Act funds to offset revenue shortfalls in fiscal year 2011.

In addition to Recovery Act funds, Mississippi also used its rainy day funds to reduce the impact of declining tax revenues¹². To help close out and balance the fiscal year 2009 budget, the state transferred almost \$20 million of rainy day funds to the state general fund. Similarly, the state transferred \$65.2 million of rainy day funds to the budget contingency fund to help cover a projected shortfall in the fiscal year 2010 general fund budget¹³. An additional \$80 million in rainy day funds was transferred to cover projected shortfalls in the fiscal year 2011 budget, leaving about \$80 million in rainy day funds for each of the fiscal years 2012 and 2013.

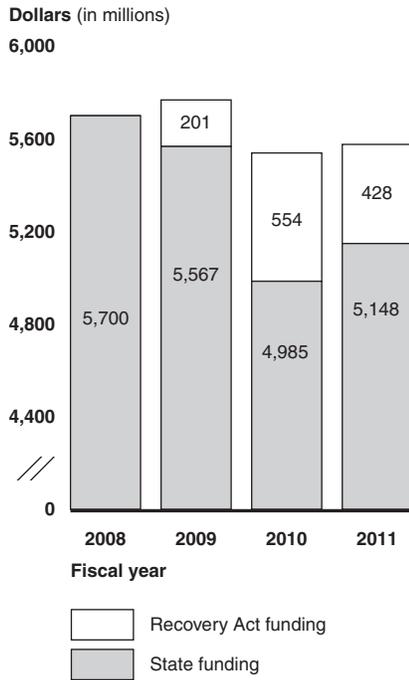
Mississippi Expects Budget Problems Will Increase without Recovery Act Funds

While Mississippi experienced serious budget problems in 2010, the Governor expects future budget years will be even more difficult as the infusion of Recovery Act funds comes to an end and state revenues lag. As shown in figure 6, Mississippi incurred a revenue shortfall of \$404 million for fiscal year 2010, which is 8.2 percent less than expected. Because state law requires a balanced budget, the Governor reduced spending for general fund and nonexempt agencies five times during fiscal year 2010 for a total of \$466 million. However, because revenue collections were not as bad as initially feared when these budget cuts were imposed, initial projections are that the state is starting fiscal year 2011 with a surplus of approximately \$50 million.

¹²The Mississippi rainy day fund, normally called the Working Cash-Stabilization Reserve Fund, is intended, among other uses, to cover any projected deficits that may occur in the general fund at the end of a fiscal year as a result of revenue shortfalls. Miss. Code § 27-103-203.

¹³The Budget Contingency Fund was created in 2001 by the legislature to identify nonrecurring funding—such as funds received from a legal judgment—that the legislature could use in the budget process. The sources of funds deposited in the budget contingency fund can differ from special fund transfers to the general fund that are identified as nonrecurring.

Figure 6: Aggregate Revenue Shortfall for Fiscal Year 2010



Source: Mississippi Department of Finance and Administration.

According to the Governor, this surplus will be crucial in preparing the fiscal year 2012 budget and spending for future years, which he expects to be as financially difficult as fiscal years 2010 and 2009. The Governor stated that while preparing the fiscal year 2011 budget was a difficult process because of declining revenue, fiscal year 2012 will be even more challenging because federal stimulus funding will end. The funds from the close of the current year can be used to help balance the budget in the difficult years to come as Mississippi copes with the budget cliff created as the infusion of Recovery Act funds ends and as the state weathers the effects of the recession. According to the National Governors Association, the most difficult budget years for a state occur two years after the national recession is declared over.

Mississippi Monitoring and Oversight Activities

To ensure accountability and oversight over federal funds received by Mississippi, the OSA conducts on an annual basis a “Single Audit” that reports on internal controls over financial reporting and compliance with pertinent laws and regulations. According to data from the Federal Audit Clearinghouse, which is responsible for receiving and distributing single

audit results, it received Mississippi's single audit reporting package for the year ending June 30, 2009, on March 30, 2010. This was the first Single Audit for Mississippi that includes Recovery Act programs, and it included only 4 months of Recovery Act expenditures. Mississippi's Single Audit report for fiscal year 2009 identified 12 significant internal control deficiencies related to compliance with Federal Program requirements, of which 2 were classified as material weaknesses.

The two material weaknesses occurred in the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) which is administered by the Mississippi Department of Health (MDH) and receives Recovery Act funding. OSA determined controls over a time study that MDH uses to allocate salaries and fringe benefits to its various programs, including the WIC program, were inadequate to ensure that the amounts entered were accurate and reliable. OSA also determined the MDH internal controls were not adequate to ensure that only obligations occurring during the funding period of the WIC grant are charged to the program.

In addition to normal oversight of federally funded programs, Mississippi has undertaken several efforts to hold state recipients accountable for the Recovery Act funds that they receive. National accounting firms, under the auspices of the OSA and DFA, are carrying out two of these efforts. OSA has contracted with the firm BKD to conduct monitoring and oversight of Recovery Act funds. According to state officials, BKD is expected to audit such entities as local governments, not-for-profit organizations, community health centers, and school districts. DFA has contracted with KPMG, to monitor the internal controls of state agencies receiving Recovery Act funds.

BKD has submitted two reports to OSA that detail the results of their monitoring efforts between January and April 2010. During this 4-month period, BKD tested 80 grants received by 34 grant recipients and reported a total of 101 instances where recipients did not comply with Recovery Act requirements. In each instance, BKD gave recipients specific recommendations for correcting existing errors in reporting and other documentation, along with recommendations for revisions to their internal control processes in order to improve future compliance.

The on-site monitoring visits found the greatest lack of compliance with recipient reporting¹⁴. Of the 101 compliance requirement findings, 30 were related to recipient reporting. BKD found that state agencies were not providing clear and consistent guidance on the recipient reporting requirements to grant subrecipients. According to BKD, agency guidance ranged from sophisticated Web-based input mechanisms to very informal guidance provided via e-mail. BKD reported that grant subrecipients expressed frustration over the reporting process, but all grant recipients appeared to be exerting their best efforts to provide accurate reporting information. In addition, BKD reported that there was some confusion on how to properly report the number of jobs created and/or retained.

BKD monitors also found a number of problems related to other Recovery Act requirements. For example, BKD reported that the majority of entities visited were not aware that they should check to determine if vendors were suspended or debarred from doing business with the federal government. BKD also reported entities entered into contracts that did not contain the appropriate Buy American language and/or provide evidence that all required materials were compliant with the Buy American provisions of the Recovery Act. Additionally, the entities did not obtain the necessary waivers when the Buy American provision was not satisfied.

DFA, with assistance from KPMG, began or completed 12 agency site visits and reviewed approximately 39 different grants between February 8, 2010, and June 30, 2010. Examples of observations that KPMG reported after site visits include the observations that documentation supporting recipient reports was not always provided to agencies for review and some agencies misunderstood recipient reporting requirements. KPMG also reported other monitoring and compliance issues, which included observing that an agency's documented policies and procedures were not inclusive of Recovery Act specific processes and that agencies did not verify that vendors were not suspended or debarred from doing business with the federal government.

¹⁴Section 1512 of the Recovery Act requires that each recipient who receives funds from a federal agency during a calendar quarter submit a report to that agency for the quarter that includes, among other information, the amount of funds received, the projects and activities for which the funds were expended or obligated, the completion status of each project or activity and estimates of the number of jobs created and the number of jobs retained by the project or activity. Recovery Act div. A § 1512, 123 Stat. 115, 287-288. We refer to the reports required by section 1512 as recipient reports.

Mississippi Initiated Several Noteworthy Efforts to Comply with Recovery Act Requirements

Mississippi has initiated several efforts to improve the state's response to the Recovery Act's transparency and accountability requirements. Both OSA and DFA have provided training sessions for prime recipients to explain how to respond to the act's requirements. In addition, OSA regularly communicates Recovery Act information to recipients through its Technical Assistance newsletter and has established a task force of governmental and non-governmental experts to assist recipients in complying with Recovery Act requirements. These experts include attorneys, engineers, project managers, educators, and accountants who are available to answer inquiries from Recovery Act recipients at no cost to the recipients or to the state.

In addition to having KPMG monitor state agencies' compliance with Recovery Act requirements, DFA has identified leading practices utilized by agencies in meeting these requirements. For example, DFA told us that one state agency contacted other states to share knowledge and identify best practices for implementing federal mandates and requirements, and another agency created a template for subrecipients that allowed them to summarize key program data for use in preparing their recipient reports.

State Comments on This Summary

We provided the Governor of Mississippi with a draft of this appendix on August 9, 2010. The General Counsel to the Governor, who serves as the stimulus coordinator, responded for the Governor on August 17, 2010. The official provided technical suggestions that were incorporated, as appropriate.

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