A Special Performance Audit

Pa Office of the Budget: Poor Administration of the Redevelopment Assistance Capital Program

June 2012

Jack Wagner, Auditor General

Pennsylvania Department of the Auditor General
Bureau of Special Performance Audits

June 27, 2012

The Honorable Tom Corbett
Governor
Commonwealth of Pennsylvania
Harrisburg, Pennsylvania 17120

Dear Governor Corbett:

Enclosed is the report of our special performance audit of the Office of the Budget as it administered the state's Redevelopment Assistance Capital Program, which we refer to as RACP. The audit covers the primary period of July 1, 2005, through June 30, 2011, with updates through May 2012 where applicable.

We conducted this special performance audit in accordance with generally accepted government auditing standards as issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to 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 does indeed provide a reasonable basis for our findings and conclusions based on our audit objectives.

During our six-year primary audit period, the Pennsylvania General Assembly passed capital budget acts that represent 3,981 RACP projects totaling $20.9 billion. The budget acts are often referred to as "wish lists," meaning they are *potential* projects but not guaranteed. The *actual* grants awarded to successful RACP applicants during the first five years of that period totaled around $1.5 billion, representing just over 500 projects.

Our report presents 11 findings and 17 recommendations. In summary, the Office of the Budget's administration of RACP was fraught with shortcomings. In particular was a lack of openness and transparency—problems made all the more serious by the agency's lack of initiative in addressing them.

In its written response included in this report, the Office of the Budget concurs with a number of our findings and recommendations. In fact, shortly after participating in the audit exit conference and just days before responding to us in writing, the agency announced what it called “sweeping reforms” to RACP. The plan for reform was a good surprise, one withheld from our auditors during their many months of audit work as the RACP deficiencies became clear, and even as Office of the Budget officials argued they could not initiate the needed reforms.

Although the announced changes do acknowledge our call for corrective actions, it is important to note they must be verified via future audits or investigations.

It is also important to note that we are not alone in calling for change. The public, too, most often through the media, has questioned this taxpayer-funded program and its lack of openness. In addition, Representative Mike Turzai, as prime sponsor of House Bill 2175, has called for RACP reforms. Improved direction, transparency, and oversight will go far to make the program successful in fostering job-creating projects and helping local economies, all while requiring the Commonwealth to be more accountable to its taxpayers.

Sincerely,

JACK WAGNER
Auditor General

Enclosure

cc: The Honorable Charles B. Zogby, Secretary
Pennsylvania Office of the Budget

The Honorable Mike Turzai, Majority Leader
Pennsylvania House of Representatives

Peter J. Tartline, Executive Deputy Secretary
Pennsylvania Office of the Budget

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Results in Brief

The Redevelopment Assistance Capital Program (RACP) was originally established in 1984 and then reestablished in 1999 through the current Capital Facilities Debt Enabling Act.

The Pennsylvania Office of the Budget administers RACP and is the entity whose performance we evaluated in this special performance audit. That agency awarded RACP funds for what were billed as economic development projects; applicants were county, city, and local governmental entities, as well as economic development agencies and authorities throughout the state.

Ultimately, we found that the Office of the Budget lacked initiative in administering RACP. More specifically, we found that the Office of the Budget demanded little accountability from applicants, failed to measure economic impact or even to make it a measurable part of the process, and did little to address a lack of transparency or to provide meaningful information to the public whose tax dollars fund RACP projects.

Significant information withheld by Office of the Budget officials: Total program redesign was in the works!

Of particular interest is that Office of the Budget officials argued vehemently—as recently as our exit conference on May 29, 2012—that they had no power to address many of our findings, saying that any initiatives or corrective actions would have to originate from the Governor and/or the General Assembly.

Significant new information *not* provided to us during our field work or during any of our meetings was the Office of the Budget's apparent work in progress to totally revamp RACP. In fact, via press release dated June 5, 2012, the Secretary of the Budget announced what he called "sweeping reforms" of the program just two days before his office provided a formal written response to the audit. *See Appendix E for a reprint of the press release.*

The announced program redesign appears to address various findings that we report and recommendations that we made. Some of the changes also align with reforms proposed in legislation that has passed the Pennsylvania House.

The fact that the Office of the Budget concealed its planned initiatives from us and even argued against our position that our recommended initiatives were within the agency's responsibility is important to discuss here for several reasons:

- **Good changes, good government.** First, and most important: if the actual changes turn out to be all that the Office of the Budget has touted in its response and press release, the changes are good ones that, again, will attempt to correct many of the issues we raised. Equally important, the changes show that our independent government auditing process works to bring about important performance initiatives, even if the audited entity appears on the surface to resist them.

- **Not yet verified.** In its June 7, 2012, response to us *(see Appendix D beginning on page 74)*, the Office of the Budget presents its program changes. In Appendix E *(page 79)*, we also include the agency's news release dated two days prior to that response. We note, however, that we have not audited any of the announced changes to verify their veracity or effectiveness. Accordingly, we will follow up at the appropriate time to ensure that the changes reflect an improved performance mindset that Office of the Budget officials neither demonstrated nor agreed to during our audit work.

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- **Lack of collaboration raises red flags.** It raises red flags that the Office of the Budget argued with our recommendations when we presented them and, concurrently, failed to disclose it was about to announce implementation of many of them. Audits should be viewed as constructive, and early on we told agency officials we would report any plans for improvements just as we would report negative findings.

  Neglecting to inform us of planned corrections makes us ask why. Whatever the reasons for nondisclosure, our findings remain the same for the period reviewed, which was primarily July 1, 2005, through June 30, 2011, with additional information (except for the planned corrections) provided by Office of the Budget officials through the date of our exit conference on May 29, 2012.

With the preceding background in mind, we present the following summary of our findings and recommendations below. Our audit was conducted in accordance with generally accepted government auditing standards as issued by the Comptroller General of the United States.

Summary of our audit findings and recommendations

From July 1, 2005, through June 30, 2010, the Office of the Budget entered grant agreements totaling more than $1.5 billion under the Redevelopment Assistance Capital Program. The grants assisted in the funding of 506 projects, projects that according to the RACP mission were supposed to create jobs and impact local economies.

Our audit work and testing revealed that, despite the supposed emphasis on job creation and economic impact, RACP administrators—i.e., officials from the Pennsylvania Office of the Budget—did not require applicants to commit that their taxpayer-funded projects would actually create jobs or help the economy.

We also found that, in many cases, the ultimate beneficiaries of the grant funding were not the actual public nonprofit entities who were eligible for the grants; instead, the recipients could be private for-profit entities or "sub-grantees" who contracted with the eligible nonprofits for specific projects.

RACP is a valuable tool. It can be especially significant in today's economy where the members of the workforce—Pennsylvanians and their families—face less-than-favorable conditions. Accordingly, it should have been an absolute priority for the Office of the Budget to administer RACP to maximize and account for each and every grant award with keen oversight and monitoring. But the Office of the Budget did not do so, according to our findings.

Altogether, we have developed 11 findings to report on the existing RACP administration, and we provide 17 recommendations as corrective actions.

Findings One and Two show that the RACP project selection process was not transparent. For example, selections of funding-eligible projects were made by the General Assembly and Governor *before* grant applications were even completed. Project descriptions—as listed in the Governor's capital budget acts (also known as "capital project itemization acts")—were vague, and the Office of the Budget took no initiative in trying to clarify the descriptions. There were also no expiration dates for itemized projects; in other words, they could remain eligible for funding indefinitely.

> To address the preceding issues, we developed recommendations 1, 2, and 3. Those recommendations tell the Office of the Budget to work with the General

Assembly to amend the Capital Facilities Debt Enabling Act to ensure the RACP grant selection process is transparent, and to ensure that the capital project itemization list includes a *specific* description of projects as well as funding expiration dates.

Finding Three shows how the Office of the Budget failed to enforce existing six-month deadlines by which (1) potential grantees must submit their applications and (2) grantees must comply with certain funding conditions spelled out in RACP grant agreements.

To address those issues, we present recommendations 4 and 5, saying that the Office of the Budget should enforce the six-month deadlines in both instances—submitting applications and complying with the stated special conditions.

Findings Four and Five discuss how the Office of the Budget failed to collect economic impact data and monitor the economic impact of RACP projects.

Our recommendations 6, 7, and 8 tell the Office of the Budget to ensure that grant applications contain the required economic impact data, and also to ensure that economic impacts are monitored as projects are finalized and over time after they are completed.

Finding Six explains that RACP administrators place no eligibility restrictions on sub-grantees that end up receiving RACP funds**.**

Our recommendations 9 and 10 tell the Office of the Budget to work with the General Assembly to amend the Capital Facilities Debt Enabling Act to place eligibility requirements on any such sub-grantees.

Finding Seven shows that the Office of the Budget did provide the public with names of RACP grantees or sub-grantees.

> Our recommendation 11 tells the Office of the Budget to provide more public disclosure, including the listing of grantee and sub-grantee names (for every project) on the agency's website.

Findings Eight and Nine explain that the Office of the Budget did not conduct required close-out audits on RACP projects in a timely manner. Nor did the Office of the Budget monitor completed projects for continued compliance with RACP grant agreement requirements.

> Our recommendations 12, 13, 14, and 15 tell the Office of the Budget to take immediate steps to finish all outstanding close-out audits, complete all future audits in a more timely manner, and implement procedures to monitor RACP-funded projects on a routine basis *after* the close-out audits have been conducted. The Office should also add fund recovery provisions to grant agreements for cases in which grantees fail to comply with their requirements.

Finding Ten explains how the Office of the Budget failed to provide quarterly RACP reports to the General Assembly as required under the Capital Facilities Debt Enabling Act.

> Our recommendations 16 and 17 tell the Office of the Budget to ensure that it complies with the law in reporting quarterly to the General Assembly. As part of its reporting, the Office of the Budget should also include the names of grantees and sub-grantees on the reports.

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Finding Eleven is a positive finding. Specifically, we found that the Office of the Budget did adequately monitor RACP projects during their construction phases, and that the agency also properly accounted for project expenses prior to approving a payment (i.e., reimbursement) requests.

Response: Office of the Budget

See Appendix D of this report for the Office of the Budget's full response to our report findings and recommendations.

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Introduction and Background

Creation and administration of the Redevelopment Assistance Capital Program

The Redevelopment Assistance Capital Program (RACP) was established in 1984 and reestablished in 1999 through the current Capital Facilities Debt Enabling Act.[1] RACP is a Commonwealth grant program that awards grant funds for the acquisition and construction of regional economic, cultural, civic, and historical improvement projects.

The Office of the Budget, specifically the Bureau of Revenue, Capital and Debt, is responsible for the administration, oversight, and monitoring of RACP[2]. The Office of the Budget's duties related to RACP include the following:

- Sending copies of grant authorization letters to eligible applicants after receiving approval from the Governor's Office.
- Reviewing the applications submitted by eligible applicants.
- Executing grant agreements between the Commonwealth and grantees.
- Monitoring project development and construction.
- Reviewing and processing grantee payment requests.
- Issuing reimbursement payments to grantees for eligible costs.
- Conducting close-out audits of completed projects.

As of December 31, 2011, this bureau had a staff of 25 employees, of which 22 were dedicated to RACP.

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[1] Act 1 of 1999, as amended, 72 P.S. § 3919.101 *et seq.* (formerly 72 P.S. § 1601-B *et seq.*, Act 83 of 1984, entitled "Capital Loan Fund Act").
[2] Act 39 of 1993 gave the Office of the Budget administrative and oversight responsibilities for the Redevelopment Assistance Capital Program.

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History of RACP Funding

RACP is funded from the proceeds received from the issuance of general obligation bonds. Under the Capital Facilities Debt Enabling Act, when RACP bonds are issued, the 'issuing officials' include these signers: the Governor and either the Auditor General **or** the State Treasurer.[3] Required bond payments as well as related interest are paid by the taxpayers through the General Fund. In this way, taxpayer dollars are the ultimate source of funding for RACP.

RACP was initially funded in 1987 with $400 *million* in bond proceeds. As of 2010, RACP's borrowing authority had escalated to $4.05 *billion*, with the most significant increases occurring from 2004 through 2010, when the debt limit increased by $2.5 billion. The history of RACP funding is shown on the table below.

History of RACP Funding			
Year	**Legislation increasing funding**	**Amount of funding increase**	**Cumulative limit on general obligation borrowing authority**
1987	Act 63 of 1987	$400 million	$400 million
1993	Act 39 of 1993	$300 million	$700 million
1997	Act 46 of 1997	$150 million	$850 million
1999	Act 1 of 1999	$350 million	$ 1.2 billion
2002	Act 130 of 2002	$250 million	$1.45 billion
2003	Act 49 of 2003	$ 60 million	$1.51 billion
2004	Act 67 of 2004	$640 million	$2.15 billion
2005	Act 87 of 2005	$500 million	$2.65 billion
2008	Act 48 of 2008	$800 million	$3.45 billion[4]
2010	Act 48 of 2010	$600 million	$4.05 billion

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[3] *See* 72 P.S. § 3919.315.
[4] Act 48 of 2010 provided that "…no more than $200,000,000 in debt shall be issued in any of the first four fiscal years beginning with the fiscal year commencing July 1, 2008[.]"

Types of projects eligible for RACP funding

The Capital Facilities Debt Enabling Act (also referred to in this report as the Enabling Act) defines the types of projects that are eligible for RACP funding.[5] Specifically, RACP projects are defined by the Enabling Act as the design and construction of facilities as follows:

- Economic development projects which generate substantial increases in employment, tax revenues, or other measures of economic activity, including projects with cultural, historical, or civic significance.
- Facilities which have regional or multijurisdictional impact.
- Hospital facilities and capital improvements for hospital facilities.
- Sports facilities, which are further defined as a stadium, arena, or other place owned or leased by a professional sports organization at which a professional athletic event is conducted in the presence of individuals who pay admission to view the event. The term includes a facility to be constructed as well as an existing facility.[6]
- Projects eligible for tax-exempt bond funding under existing federal law and regulations.
- Fire trucks and firefighting equipment to the extent that the request for assistance does not exceed $50,000.

This same act also lists *ineligible* projects, which are highways, bridges, waste disposal facilities, sewage facilities, and water facilities. However, there is an exception by which bridges, roads, and water or sewer infrastructure do qualify for RACP funds when included as part of a business or industrial park facility.

[5] *See* 72 P.S. § 3919.302.
[6] *See* 72 P.S. § 9319.501.

RACP project eligibility requirements

The Capital Facilities Debt Enabling Act[7] lists other requirements that projects must meet in order to be eligible for RACP funds as follows:

- Have non-state matching funds of 50 percent:
  - ✓ With identifiable and firm commitments from all sources that can be documented at the time of the application.
  - ✓ At least half of which is secured funding.
  - ✓ Sources of matching funds can be local government, federal government, or private funding.
  - ✓ Only non-cash items that can be used for the matching share are land or fixed assets that have a substantial useful life and are directly related to the project.
  - ✓ State funds from other programs cannot be used as matching funds.
- Total project cost of at least $1 million.
- Comply with the state Steel Products Procurement Act.[8]
- Solicit a minimum of three bids for all contracted construction work.[9]

[7] *See* 72 P.S. § 3919.302.
[8] *See* 72 P.S. § 3919.308(f).
[9] *See* 72 P.S. § 3919.308(f).

Types of entities eligible to apply for RACP funding

According to the Enabling Act,[10] applicants for RACP funds must be one of the following:

- A redevelopment authority.
- An industrial development authority.
- A general purpose unit of local government, which includes:
  - ✓ Cities
  - ✓ Boroughs
  - ✓ Townships
  - ✓ Counties
- A local development district which has an agreement with a general purpose unit of local government under which the unit assumes ultimate responsibility for debt incurred to obtain the 50 percent non-state participation.
- Any public authority established pursuant to Commonwealth laws.
- An industrial development agency certified as such by the Pennsylvania Industrial Development Authority Board.

Allowable RACP expenses

RACP funds are disbursed to project grantees on a reimbursement basis. Stated another way, grantees do not get the funds up front, but instead must spend their own money on allowable costs first. Then, grantees must submit their requests for reimbursement payments, along with supporting information documenting the costs, to the Office of the Budget.

[10] *See* 72 P.S. § 3919.302.

Only after the Office of the Budget reviews this information does it approve a reimbursement payment to the grantee. The Office of the Budget's RACP guidelines state that the following costs are allowable for RACP reimbursement:

- Construction costs.
- Interest during construction when interest is paid as a result of using interim financing for the project.
- Costs for acquiring needed construction permits.
- Land, if purchased and if a certified appraisal is provided.
- Other costs such as acquisition costs and costs related to the abatement of hazardous materials.

Grantees may request reimbursement payments periodically throughout the entire project—meaning through the construction phase and up to final completion of the project—but no more than once a month. The Office of the Budget has the right to withhold reimbursement payments if it determines that the grantee is not complying with the terms of the grant agreement. Further, the Office of the Budget may retain a percentage of funding until after a final close-out audit is completed to ensure that full compliance with all project requirements has been attained.

RACP grant process: The steps

Step 1: Itemization

Itemization. To members of the general public, the term "itemization" as it is used in this process is not self-explanatory. Perhaps for that reason, the Office of the Budget and others familiar with the process often use the term "wish list" to describe what itemization represents, as we describe in this section.

The RACP grant process starts with the Governor, members of the General Assembly, and senior state executives compiling a "wish list" of projects. There is no mandate stating how often this list of wished-for projects should be compiled, but typically this wish list is made every two years. Each time the list is compiled, it is itemized in that year's Capital Budget Project Itemization Act, hence the term "itemization." In this report, we refer to the various Capital Budget Project Itemization Acts generically as "capital budget acts."

Following are some key points to remember about the itemization process:

- ✓ Itemization is *not* the same as funding, nor does itemization mean that a wished-for project will even be approved for funding. But an itemized/wished-for project cannot move forward in the RACP process without first being placed on this "wish list."

- ✓ No expiration date—once projects are placed in a capital budget act, they might be funded at any time in the future, even several years in the future. Alternatively, an itemized project might *never* be authorized for funding.

- ✓ Itemization in a capital budget act includes a brief project description and an estimated project funding allocation.

Step 2: Authorization

Authorization. Using the projects itemized in the capital budget acts, the Governor and members of the General Assembly decide which projects will receive a grant authorization letter. These grant authorization letters are signed by the Secretary of the Budget.

Key points to remember about authorized projects:

- ✓ Can be authorized in *any* year, regardless of the year the project was originally placed on the itemization "wish list."

- ✓ Amount of project funding stated in the grant authorization letter cannot exceed the amount listed in the applicable capital budget act.

- ✓ Not all projects itemized in capital budget acts receive a grant authorization letter so, again, some projects might *never* be authorized for funding.

- ✓ In most cases, every project that receives an authorization letter actually and eventually gets funded. But potential grantees must first apply and be approved (see next step).

Step 3: Application and grant agreement

Application and grant agreement. The grant authorization letter states that, within six months of the letter's date, an applicant must submit a RACP application to the Office of the Budget.

Key points to remember:

- ✓ The application consists of 17 different sections, each requesting information and documentation to be submitted to the Office of the Budget, including match amount, project specifications, project budget, and sources of matching funds.

- ✓ The first section of the application requires the applicant to present economic impacts of the project.

- ✓ Office of the Budget staff typically assists applicants in the completion of the application.

- ✓ Office of the Budget assigns an external consultant to each project for application review. (More information about the external consultants in presented in Finding 11).

- ✓ Redevelopment assistance amount requested in the application cannot exceed the amount stated in the grant authorization letter. The assistance received by the grantee is in the form of reimbursement payments approved by the Office of the Budget for project expenses already paid by the grantee.

- ✓ Grant agreement is executed between the Commonwealth and the applicant, who then becomes the grantee.

- ✓ Grantee is expected to satisfy all special conditions listed in grant agreement within six months.

Step 4: Grant award payments

Grant award payments. The external consultant who is assigned to a project during the application phase is responsible for monitoring the development and construction of the project on behalf of the Office of the Budget. The grantee submits requests for reimbursement for allowable project costs throughout the duration of the project. After Office of the Budget staff reviews and approves the required project cost documentation, the office then notifies the Pennsylvania Treasury Department to issue a reimbursement check or transfer funds for each approved payment request.

Key points:

- ✓ First payment cannot be made until after the grant agreement is executed.

- ✓ Grantees cannot request reimbursement more than once a month.

- ✓ Total grant payments cannot exceed the amount listed in the grant agreement.

- ✓ Consultants submit construction monitoring reports to the Office of the Budget detailing each project's status as well as the project's compliance with applicable laws and grant agreement terms and conditions.

- ✓ Grantee must satisfy special conditions of grant agreement before payment can be made.

Step 5: Project completion and close-out audit

Project completion and close-out audit. Once each project is completed (completion could be in a few months or in many years), the Office of the Budget must conduct a legislatively mandated close-out audit.

Key points:

- ✓ Close-out audit is last time the Office of the Budget looks at the project.

- ✓ Any retained payment is released when the close-out audit is complete and any areas of noncompliance are corrected.

Amount of RACP funding itemized in legislation

As described in Step 1 of the RACP process, the RACP grant process starts with the Governor and members of the General Assembly compiling a "wish list" of projects that are then itemized in capital budget acts. The following table shows the total number of projects and related costs itemized in capital budget acts that were passed during our audit period of July 1, 2005, through June 30, 2011.

Summary of Capital Budget Acts (Wish Lists)		
Legislation itemizing RACP projects	**Number of RACP projects itemized**	**Amount of RACP funding itemized for listed projects**
Act 83 of 2006	1,177	$5,533,652,000
Act 152 of 2006	22	$126,250,000
Act 41 of 2008	1,362	$7,533,808,000
Act 47 of 2010	46	$298,250,000
Act 82 of 2010	1,374	$7,375,792,000
Totals	**3,981**	**$20,867,752,000**

RACP grants awarded over five years

During the period from July 1, 2005, through June 30, 2010, the Office of the Budget entered into grant agreements for 506 projects involving 770 grant authorizations totaling over $1.5 billion. The Office of the Budget can award more than one grant to a project by amending the original grant agreement.

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Total RACP projects, grant authorizations, and amounts awarded from July 1, 2005, to June 30, 2010			
Fiscal year	**Number of projects**	**Number of grant authorizations**	**Total grant authorization amounts**
2005-06	130	152	$417,350,554
2006-07	68	111	$174,789,000
2007-08	100	161	$311,334,267
2008-09	79	125	$243,825,000
2009-10	129	221	$400,102,000
Five-year total	**506**	**770**	**$1,547,400,821**

Of these 770 grant authorizations, 167 authorizations, worth $353.8 million, were awarded to projects in Philadelphia County, and another 143 grant authorizations, worth $265.8 million, were awarded to projects in Allegheny County. See Appendix B for more information on RACP grant authorizations on a county-by-county basis.

Overall comment about this report

Questions have been raised by taxpayers and the media as to why some projects received RACP funds while other projects are not funded. For example, taxpayers questioned why private developers received RACP funds and how much of an economic impact was realized for other projects that received substantial RACP funding.

Unfortunately, officials from the Office of the Budget could not provide answers to the types of questions above because the "Office of the Budget is not privy to the criteria used in the selection process."[11]

Even though the Capital Facilities Debt Enabling Act allows RACP to fund projects with cultural, historical, and civic significance, we nonetheless remained at a loss to understand how the Commonwealth determined RACP funding priorities.

As a result, this audit could not answer questions regarding funding decisions because the Governor and General Assembly made such determinations. State law prohibits the Department of the Auditor General from auditing the General Assembly. Instead, we audited the RACP administrative agency under the Governor's jurisdiction, which is the Office of the Budget. We looked at what that agency did, what it did not do, and what it could have done if it had taken more responsibility and initiative. To that end, it is important to understand that our findings and recommendations are addressed to the Office of the Budget as a whole and specifically to its top leadership, not necessarily or solely to the RACP program staff who takes direction from the leadership.

We discuss throughout this report (and especially in Finding One) that project selection was done behind closed doors with no rationale provided to the public at any time, or to us during our audit, on these selections. Only those decision-makers who were involved in selecting projects to receive RACP funding can answer questions about why certain facilities received grant awards and why others did not.

[11] Written response from Office of the Budget to auditor's questions posed in Information Request #7, dated March 29, 2011.

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Finding One

Despite being the agency responsible for administering the Redevelopment Assistance Capital Program, the Office of the Budget did not know how or why the Governor and members of the General Assembly selected projects for funding because the decision-making process was not transparent.

As we stated in the *Introduction and Background* section of this report, the first step in RACP eligibility is for a project to be itemized in a capital budget act. According to the RACP application handbook, RACP projects are defined as follows:

> Redevelopment Assistance Capital Projects are primarily economic development projects, authorized in the Redevelopment Assistance section of a Capital Budget [and Project] Itemization Act, have a regional or multi-jurisdictional impact, and generate substantial increases in employment, tax revenues or other measures of economic activity. Included are projects with cultural, historical, or civic significance.

More than 3,900 RACP projects totaling nearly $20.9 billion were itemized in five capital budget acts enacted from 2006 through 2010.[12] On an annual basis, millions of taxpayer dollars are funneled into RACP.

After projects are placed in a capital budget act, they are eligible to be selected for RACP funding. Not all projects that are itemized are chosen for RACP funding, but when a project is selected, its selection and funding level are announced through a grant authorization letter that is signed by the Secretary of the Budget.

[12] Act 83 of 2006, Act 152 of 2006, Act 41 of 2008, Act 47 of 2010, and Act 82 of 2010. See table on page 11 of this report.

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During our audit period that spanned just over five years, the Office of the Budget executed grant agreements for 506 projects. These 506 projects involved the Office of the Budget sending 770 RACP grant authorization letters totaling over $1.5 billion in potential grant funding to individuals responsible for the projects (some projects received more than one grant).

In this finding, we discuss the first two steps of the RACP project selection process: first, itemization in a capital budget act and then the receipt of a grant authorization letter.

Selection process for approving RACP funding was not transparent

Although it was the state's Office of the Budget who administered RACP funding, that office did not select the projects that were itemized in the capital budget acts, nor did it select the projects that received RACP grant authorization letters. Rather, the Governor and select members of the General Assembly were responsible for both of these decisions.

We asked Office of the Budget officials what criteria were used to determine which projects to itemize and fund. "The Office of the Budget is not privy to the criteria used in the selection process," was one response. We learned further that, in fact, the Office of the Budget is not involved in the selection process at all. Specifically, that agency's involvement begins only when the Governor's office notifies the Secretary of the Budget which projects were selected for funding. At that point, the Secretary of the Budget signs authorization letters addressed to the applicants, at which point the RACP program staff receive copies of the letters and thereby themselves learn of the decisions.

During our meeting with the then Secretary of the Budget and a senior manager of the Department of Community and Economic Development, the former Secretary of the Budget noted that it was the Governor and certain members of the General Assembly who were responsible for itemizing the projects in the capital budget acts.

Further, neither official provided any information on the rationale or criteria used by the Governor and the General Assembly when they selected projects that received grant authorization letters. The DCED official did state that after a project is itemized, a team of officials from DCED will review the list and provide the Governor with recommendations for projects to authorize. However, there was no guarantee that every project recommended by DCED would actually be authorized by the Governor.

When asked about what records were maintained to support decisions to authorize funding of projects, both officials stated that they were unsure what, if any, documentation was maintained by either the Governor or legislators. Further, even though the grant authorization letters were signed by the former Secretary of the Budget, she told us that the Office of the Budget (at least when she was there) did not have any documentation supporting RACP project selection.

Indeed, during our review of selected RACP project files, we found no information in any of the files documenting how or why the projects were initially selected for inclusion in a capital budget act. We also did not find documentation regarding why these particular projects were later selected to receive grant authorization letters. In fact, in each and every file we reviewed, the earliest dated document was the Office of the Budget's copy of the grant authorization letter.

Funding decisions were made before RACP applications were completed

When we could find no documentation showing how or why the Governor and legislators decided which projects were initially itemized in the capital budget acts and which ones later received RACP grant authorization letters, we asked Office of the Budget staff if the Governor might have had copies of completed RACP project applications to use during the selection process. But we learned that such a scenario would not have been possible because, as the Office of the Budget staff explained to us, a potential grantee would not have completed a RACP application until *after* receiving a grant authorization letter signed by the Secretary of the Budget.

Our review of files confirmed this practice.

In other words, during our audit period, the Governor and the General Assembly itemized more than $13 billion in RACP projects in four capital budget acts—and the Secretary of the Budget sent 770 grant authorization letters for 506 projects totaling $1.5 billion in RACP funding—*before* the potential grantees even submitted their RACP grant applications to the Office of the Budget!

What the state did is akin to awarding a student a full scholarship at a college before reviewing the student's application for admission. Or even more simply stated in the terms of an old proverb, it's like putting the cart before the horse.

A fair and transparent grant selection process would require the Governor, members of the General Assembly, and other state officials to obtain and evaluate project information, such as a completed application, *prior* to selecting projects for funding—not afterwards.

RACP project descriptions were specific in some cases but entirely too vague in others

As part of our audit work, we obtained copies of two capital budget acts (Act 83 of 2006 and Act 41 of 2008) which, together, itemized over $13 billion in RACP projects. In analyzing the projects itemized in these acts, we found that the project descriptions were either very specific or very vague.

We found many instances listed in these acts in which the descriptions stated the specific name of the project, the potential grantee, and the project's exact location. Such cases illustrate good and open government: the project descriptions not only provided the public with an acceptable level of transparency on how taxpayer funds were being used, but they also showed that there was a definitive use for the monies.

However, we also found many other instances in these acts where the project descriptions were vague or generic, naming no specific project or grantee. Those cases illustrate a total lack of government transparency: based on these descriptions, it was impossible for us to determine the exact nature of the projects that the Governor and the General Assembly had deemed eligible for RACP funding.

The following list is just a small sample—lifted verbatim from the two capital budget acts—of the far-too-vague project descriptions:

- "Expansion of manufacturing facility, including construction of new buildings/facilities, site acquisition and remediation and infrastructure improvement" (Lehigh County)
- "Acquisition, construction, infrastructure improvements and other related costs for an economic and community development project" (York County)
- "Construction, acquisition, demolition, redevelopment and other costs associated with South Philadelphia housing" (Philadelphia County)
- "Acquisition, infrastructure, construction and other related costs for the development of a business/industrial park" (Indiana County)

Project descriptions such as those just cited are virtually meaningless to the public. It is a closed government that keeps the general public in the dark while allowing only select members of the Governor's office and the General Assembly to be privy to the details.

Possible reasons for vague descriptions

In seeking the root cause for the lack of transparency in cases where project descriptions were vague or generic, we learned that the lack of specificity can occur when project details have not yet been determined. Rather, the Governor and General Assembly were planning for *future* projects and, in effect, earmarking money for specific geographic areas for *future* use.

Further, broad, vague project descriptions lay the groundwork for any type of project to be developed at a future date while, in the meantime, being authorized now with monies listed in the itemization act. Stated another way, vague or generic descriptions create an almost blank slate for decision-making officials to fill in later when they are ready to do so and have a specific project in mind.

When asked about a reason for such vague project descriptions, staff at the Office of the Budget stated that the projects might not be fully developed and designed; therefore, it would be easier for the Governor and members of the General Assembly to give projects broad descriptions in the capital budget acts. But this response only serves to highlight that the Governor and the General Assembly somehow deem projects worthy *before* they are planned or *before* an entity completes an application.

Some government officials also left in the dark on projects listed in capital budget acts

During our audit work, we found that we and members of the general public are not the only ones for whom RACP-eligible project information is obscured. At times, even some members of the General Assembly are unaware of the RACP funded projects in their districts. For example, we found that a state representative (Philadelphia County) said the following after a project in her district received funding:

> I found out about the "Chelten Plaza" development the same day the community found out- with the abrupt closing of the Fresh Grocer located off Chelten Avenue. Developers should be required to inform the public and the citizen's representatives when a project is about to receive state funding. It would create a layer of transparency while giving the people an opportunity to voice their concerns, or support for a project.[13]

Another state representative (Montgomery County) stated the following when asked about the lack of advanced notice on RACP projects:

> Public notice is crucial, if you represent an area and you're a senator for an area, I think at the very least, you ought to have the ability to weigh in on a project, not have it made in a back room where all of a sudden it's against the wishes of everyone in the neighborhoods, but it's wanted by a few.[14]

We also found examples where local government officials were not aware of RACP projects in their area. Specifically, we noted that local government officials in Franklin County were

[13] State Representative Rosita C. Youngblood, News Release, "Youngblood continues fight to bring transparency, accountability to RACP process," dated November 21, 2011.
[14] Mary Wilson, "Pa. GOP lawmakers seek power to review projects," *NewsWorks*, http://www.newsworks.org/index.php/local/item/33831, February 12, 2012. Legislator quoted was Rep. Mike Vereb.

not aware that a project in their own county had become eligible in 2011 for RACP funding.[15]

According to an article in the Chambersburg *Public Opinion*,[16] a line item in a capital budget act—for "construction, renovations and infrastructure improvements for an industrial facility"—was actually for improvements, including roof replacement, at a Franklin County crane manufacturing plant. In a telling move, the reporter called the project a "mystery project," stating that local politicians and the president of Franklin County Area Development Corporation were unaware of the RACP grant authorization. This example further illustrates the gross lack of transparency surrounding RACP project selection.

The fact that state and local government officials were not even aware of projects that were authorized for RACP funding further points to the lack of transparency and accountability surrounding RACP funding decisions. Public meetings regarding potential RACP projects should be held to ensure that state and local leaders, as well as the public, can provide input regarding the economic impact of the project.

Recommendations

1. The Office of the Budget should work with the General Assembly to amend the Capital Facilities Debt Enabling Act to ensure that the RACP project selection process is transformed into a transparent, accountable process that includes the following components:

    - An announcement that taxpayer funds are available to be awarded.

[15] While our primary work focused on projects funded from 2005 through 2010, we also looked at any projects that received a RACP grant authorization letter in 2011.
[16] Jim Hook, "$2M grant may go back to Pa.," *Public Opinion* (Chambersburg, PA), May 20, 2011.

- An application that must be completed prior to eligibility consideration.
- A public announcement about each eligible project selected for RACP funding and the reasons for the selection.
- At least one public meeting subject to the Sunshine Act hosted by the Office of the Budget staff to give taxpayers the opportunity to provide input on projects' economic impact in communities.

2. The Office of the Budget should work with the General Assembly to ensure that the capital project itemization list includes a *specific* description of the capital project, including the municipality where the project is located.

Finding Two

The Office of the Budget had no control over how long the Governor took to authorize funding for potential projects.

On its website, the Office of the Budget had this to say about making it a priority to fund RACP projects as a way to create jobs and grow the economy:

> Given the current economic conditions throughout portions of Pennsylvania, it will be the priority of the Commonwealth to focus limited available capital funding on those projects that display significant potential for improving economic growth and the creation of jobs….[17]

Also emphasizing economic development were the grant authorization letters sent by the Secretary of the Budget: "As one of the selected recipients of the limited amount of RACP funding available, your organization now has the significant responsibility of ensuring that these funds are utilized for economic development in a timely manner."

Even though both the website and the authorization letters convey the importance of RACP funding and its supposed contribution to economic growth, we found that the Commonwealth caused delays and/or allowed recipients to miss deadlines. Overall, despite the Commonwealth's stated and repeated positions, the economic benefits of RACP projects took years to be realized, if those benefits were realized at all.

Some delays were extensive—*decades long*—from the time a project was deemed eligible for RACP funding (by being listed in a capital budget act, as we discussed in Finding One) until the project received actual RACP funds. Such time delays

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[17] http://www.portal.state.pa.us/portal/server.pt?open=512&objID=4602&&PageID=461665&&mode=2, accessed on November 2, 2011, verified March 20, 2012.

defeated the purpose of improving economic growth and creating jobs during a period when Pennsylvania needed those benefits the most.

Projects could be funded with no expiration date

As we stated in Finding One, the first step of RACP eligibility is for a project to be listed by the Governor and members of the General Assembly in a capital budget act. From that list, the Secretary of the Budget sends grant authorization letters notifying selected applicants that they are eligible to receive RACP funds.

In conducting our audit work, we were surprised to find there was *no expiration date* for applicants to receive RACP funds once the projects were itemized in capital budget acts. In that regard, the capital budget acts aptly lived up to their insider nickname of “wish lists” by correctly suggesting that projects may or may not become reality.

Just as Office of the Budget officials could not explain why projects received grant authorization letters in the first place, they also could not explain why, in numerous cases, projects languished on the wish list for years until the Governor authorized funding.

Once the Governor approves or authorizes funding for a specific project, the Governor’s office notifies the Secretary of the Budget, who, in turn, sends a letter to the applicant to say the Governor approved the project’s funding. While the Secretary of the Budget is responsible for sending the authorization letter, the Office of the Budget has no control over how long the Governor takes to authorize project funding. (Nor, as we explained previously, does the Office of the Budget control which projects are put on the wish list in the first place.)

To determine the length of time between when a project was listed in a capital budget act and when a grant authorization letter was sent, we examined the timing of 473 such letters (each one representing a single project) sent between 2005 and 2010. On average, 1.6 years had passed. The actual time passed for each of the 473 projects ranged from *7 days to 21 years*.

The table below list actual examples of the projects and the time span between the listings and the letters.

Examples of the amount of time elapsed from the date a project was listed in a capital budget act until the grant authorization letter was sent

Project name	County	Date project itemized in a capital budget act	Date grant authorization letter sent	Elapsed time
Robinhood Dell East	Philadelphia	10/21/88	10/20/09	21.0 years
New Granada Theater	Allegheny	12/28/92	04/28/08	15.3 years
Biberman Building Redevelopment	Philadelphia	12/28/92	11/08/07	14.9 years
Shoppes at LaSalle University	Philadelphia	12/28/92	06/05/07	14.4 years
Lancaster Ave. Revitalization	Philadelphia	07/08/94	04/28/06	11.8 years
Simons Recreation Center II	Philadelphia	07/08/94	02/23/05	10.6 years
Leg Up Farm	York	06/22/00	04/27/09	8.9 years
Annville Streetscape II	Lebanon	06/25/99	06/05/06	7.0 years
Market Square Fifth and Forbes	Allegheny	10/30/02	11/20/08	6.1 years
Advanced Communications	Dauphin	06/22/00	03/30/06	5.8 years
Jefferson Hills Former Westinghouse Site	Allegheny	10/30/02	03/27/07	4.4 years
Redevelopment Bakersville	Somerset	07/07/06	07/14/06	7.0 days

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As shown in the preceding table, there is no consistency in the timeliness of RACP funding. Again, RACP allows all projects listed in any capital budget act to be eligible for grant funding at any time in the future, regardless of the amount of time that may pass.

The lack of expiration dates and the resulting inconsistencies illustrate the significant latitude afforded to the Governor and the General Assembly by the capital budget acts. As we discussed earlier, these public officials are already following no known rationale in selecting projects to be funded with RACP's taxpayer dollars; now, as we have just shown, those same officials are also operating with no required time frames.

Ultimately—and ironically—it seems that the time delays directly contradict the Commonwealth's stated position that economic development from RACP projects is a priority, and that RACP grant recipients should use their economic development funds in a timely manner.

Recommendation

3. The General Assembly should place expiration dates on projects listed in the capital budget acts to limit the amount of time a potential project could be eligible for funding and to show that economic development is a priority that must not be delayed. The time constraints should be consistently applied to all RACP projects itemized in the acts.

Finding Three

Once projects were authorized, the Office of the Budget allowed applicants to miss deadlines, sometimes allowing years to pass before contracts were signed.

Up to this point, we have discussed how the Governor's office and the General Assembly essentially had free rein in how RACP dollars were applied. Now, in this finding, we discuss the Office of the Budget's role as the RACP administrator.

We noted earlier that the Office of the Budget said it did not know the selection criteria, if any, that the Governor's office and the General Assembly used to determine the wished-for project listings. But the Office of the Budget *did* have control of the process once the grant authorization letters were sent. Specifically, for each project, the Office of the Budget was responsible for receiving the completed application, processing it, executing a grant agreement, and ensuring that the grantee stayed within the six-month time frame for meeting the special terms and conditions of the grant agreement.

Despite those critical responsibilities, the Office of the Budget did not perform well with regard to its most basic job at the very beginning of the process—ensuring that the grantees complied with application deadlines. We discuss that substandard performance (broken down by responsibility and time frames) in the sections that follow.

Application time frames were not enforced

In the grant authorization letters, the Secretary of the Budget directed responsible entities to prepare and submit their grant applications to the Office of the Budget within 180 days of the date of the letter. The RACP grant authorization letters we reviewed each stated the following:

> As one of the selected recipients of the limited amount of RACP funding available, your organization now has the significant responsibility of ensuring that these funds are utilized for economic development in a timely manner. Therefore, it will be the policy of this Administration to require that all recipients of RACP funding **MUST** submit their application **within six months** of the date of this letter. Failure to submit the required RACP application within this timeframe may lead to the termination of any commitment of funding contained herein. [Emphasis in bold added.]

In order to determine if applications were submitted within the six-month time frame that was conveyed to applicants, we reviewed the timing of 25 applications submitted to the Office of the Budget between 2005 and 2010. These 25 applications included our core test group of 14 applications (for which we conducted detailed testing in all aspects of RACP administration, not just timing), plus an additional 11 applications tested for timing only.

Of the 25 tested applications, we found that 15, or 60 percent, were submitted *more* than 180 days from the date of the grant authorization letter. The breakdown is as follows:

- Of four applicants who were allowed to breach the 180-day time frame the longest, three were more than 16 months late in submitting their applications, while the other applicant was 12.5 months late.

- Of the 11 remaining late applicants, their tardiness ranged from only a week to more than 3 months.

Despite the late submissions for 60 percent of the tested applications, and despite the fact that the Office of the Budget could have terminated its funding commitment to applicants who were six months late, such applicants suffered no repercussions. As we learned, the Office of the Budget did not send warning letters as part of a standard RACP operating procedure.

Office of the Budget officials whom we interviewed defended their inaction by saying that only the Governor could decide to terminate a grant. When they said they knew of no such instance, we asked when and how they informed the Governor of late applicants so he would know to make those decisions. In response, the officials said there were no notification procedures (from the Office of the Budget to the Governor) in effect.

Our concern—and what should concern the Office of the Budget—is an obvious unwillingness to take responsibility in such an important matter. That unwillingness is evident in several Office of the Budget disconnects: (1) officials who, on one hand, say only the Governor can terminate a funding commitment but, on the other hand, don't tell him of applicants who should be subject to those decisions and (2) officials who first tell potential RACP recipients that funding commitments might be terminated for not meeting deadlines, but then not following through with warning letters if the deadlines are missed.

On a positive note concerning the Governor's office, Office of the Budget officials told us they learned late in our field work (May 2012) that, almost four years ago, the then-Governor *had* decided to terminate 17 funding commitments when potential grantees did not submit their applications. As evidence, the Office of the Budget gave us copies of those 17 termination letters, all signed in December 2008 by the then-Secretary of the Budget. Each termination letter referenced a prior letter dated three months earlier, also from the then-Secretary, warning that a termination could occur.

Although the impetus behind this apparent one-time 2008 initiative is not entirely clear, Office of the Budget officials said it resulted from the Governor's request to look at potential grantees with missed deadlines. Approximately 200 such missed-deadline letters went out, resulting ultimately in the 17 above-referenced terminations for failure to file applications and another 8 for failure to meet special conditions. We will discuss the latter 8 in the next few pages.

Bottom line is this: The Office of the Budget maintained throughout our audit that only the Governor can *make* decisions about terminations. While that position may be accurate, it should not be an excuse for the Office of the Budget's lack of initiative in sharing information and potential strategies with the Governor. Stated simply, the Office of the Budget should not simply wait for the Governor to ask for important information. Clearly there is precedent to show that that the Governor's office was interested—at least in 2008—in seeking potential termination-causing information and acting on it. Thus, when potential RACP recipients are not living up to grant requirements, the Office of the Budget should be proactive in suggesting actions to the Governor's office and in providing the Governor with information he needs to be fully informed.

Months spent processing applications and executing grant agreements

After receiving an application, the Office of the Budget was responsible for processing the application and executing a grant agreement with project representatives. We found that this process could take months.

When we discussed the review process with Office of the Budget officials, they told us they contract with outside consultants for application review (and for project monitoring, too, as we discuss later). According to officials, they cannot control how long it takes the contracted consultant to gather and review all required information and then prepare an application review report for the Office of the Budget. The review process takes time, said the officials, because applicants must obtain financing and meet all other application requirements.

With regard to the grant execution phase, Office of the Budget officials said that each grant agreement can be unique with its own special conditions. After the draft agreement is prepared, the process of obtaining the signatures of project officials and numerous Commonwealth officials can take several weeks. Still, the Office of the Budget officials said they "endeavor to complete these processes as fairly, reasonably, responsibly and quickly as possible."

In order to determine how long it took the Office of the Budget to process applications and execute grant agreements, we reviewed the project application process for that same group of 25 applicants previously discussed. We found that, on average, the Office of the Budget took approximately 6.5 months to process applications and execute grant agreements. The shortest time frame was 3.3 months and the longest was 10.5 months.

No enforcement of time constraints for grantees' compliance with special terms and conditions

The grant authorization letters provide another time frame for the RACP recipient, stating:

> Once the grant agreement is fully executed for the RACP funding, your organization will then have a maximum of **six months** to meet the terms and conditions of the grant agreement and begin construction of the aforementioned project. Failure to begin construction of the project within six months of the final execution of the grant agreement may lead to the termination of the funding commitment. [Emphasis added.]

In addition to communicating this six-month requirement in the grant authorization letter, the Office of the Budget also communicated the requirement in the actual grant agreement document. Specifically, Appendix B of the grant agreement requires the grantee to comply with the special conditions "no later than six months after the execution date of this agreement." The consequence of failing to meet this requirement is also outlined in the grant agreement:

> Failure to submit documentation indicating completion of each Special Condition within the time period as originally specified, or modified, may constitute a default under the terms of the grant agreement and could lead to a termination of the Redevelopment Assistance Capital grant.

Despite these requirements, we found that the Office of the Budget did not adequately enforce this time requirement. During our detailed review of 14 RACP grant award files, we found only 4 instances in which the grantee met the six-month time requirement. In the remaining 10 cases, the Office of the Budget provided the grantees with numerous extensions. Six of the ten achieved compliance with their special terms and conditions eventually, but only after a range of 7 to 16 months *after* the agreement date, and only after working in conjunction with the Office of the Budget and its consultants.

Regarding the other four grantees that did not meet their special terms and conditions within the required time frame, and when it appeared that little progress was being made, the Office of the Budget, in accordance with Article 13 of the grant agreements,[18] sent written notification to the grantees communicating the following:

[18] Grant Agreement, Article 13, Clause A, requires the Office of the Budget to provide the grantee 30 days prior written notice specifying the effective date of termination. Further, Clause B provides the grantee with the right to "cure" the default within 30 days of receipt of the notice of termination.

> Failure to satisfy the special conditions contained in the agreement within 30 days of the date of the letter will result in the termination of the RACP grant agreement.

As of June 30, 2011, or more than two and a half years after the four sampled grantees were supposed to have met their special terms and conditions, three of the four still had not done so. (Two of the three had also submitted their applications after the six-month deadline as well.)

To be clear, and in fairness to the Office of the Budget, we note here that no reimbursement monies were paid to any of the grantees in our test group *until* they met their special terms and conditions, meaning that *no* monies went to those three sampled grantees who as of June 30, 2011, had *still* not met their special terms and conditions. The grant agreements for those three grantees will expire at the end of 2012,[19] at which time the Office of the Budget must decide whether to renew the grant agreements or terminate the projects altogether.

In saying that the Office of the Budget must decide whether to renew or to terminate the projects, however, we note that the Office of the Budget's threats to terminate were once again largely empty because the Office of the Budget did not actually follow through with terminations. In fact, when we looked for terminations for failure to meet specials conditions, we found that just 8 terminations occurred. Moreover, those 8 terminations occurred only when the Governor's office took the previously discussed 2008 initiative in which he asked the Office of the Budget to review missed deadlines. (Overall, then, there were 25 terminations in that 2008 initiative—the 8 just mentioned plus the 17 discussed earlier for the potential recipients who did not submit applications.)

[19] Unlike the "wish list," which never expires, grant agreements typically expire after five years. In other words, the grantees have five years to complete the project and request reimbursement payments.

As before, the Office of the Budget took the position that its hands were tied because only the Governor could make termination decisions.

Our concerns about the Office of the Budget's position are the same as those we discussed earlier in this finding. To repeat: While that position may be accurate, it should not be an excuse for the Office of the Budget's lack of initiative in sharing information and potential strategies with the Governor. Stated simply, the Office of the Budget should not simply wait for the Governor to ask for important information. Clearly there is precedent to show that that the Governor's office was interested—at least in 2008—in seeking potential termination-causing information and acting on it. Thus, when potential RACP recipients are not living up to grant requirements, the Office of the Budget should be proactive in suggesting actions to the Governor's office and in providing the Governor with information he needs to be fully informed.

As RACP administrator, the Office of the Budget has demonstrated a history of communicating deadlines and then failing to enforce them while attempting to place responsibility elsewhere—as with the Governor's office. Accordingly, applicants and/or grantees might reasonably believe that, if the deadlines are meaningless, so are other program requirements. The overall result is that all those involved—whether applicants, grantees, the Office of the Budget, or the Governor's office—escape accountability for billions of taxpayer dollars.

Recommendations

4. The Office of the Budget should ensure that applicants submit RACP grant applications within the six-month time frame stated in the grant authorization letter. If applications are late, the Office of the Budget should first determine and document the reason for the delay, take the initiative to inform the Governor's office, and if necessary

seek authorization from the Governor to enforce the deadlines with sanctions or to otherwise terminate the funding authorization.

5. The Office of the Budget should ensure that grantees comply with the special terms and conditions of Appendix B within the six-month time period stated in the grant agreement. If grantees fail to do so, the Office of the Budget should determine the cause for the delay, take the initiative to inform the Governor’s office, and if necessary seek authorization from the Governor to terminate the grant as long as the grantee is first given 30 days to “cure” its default as required by the agreement.

Pa. Office of the Budget: Poor Administration of the Redevelopment Assistance Capital Program

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
June 2012

Finding Four

The Office of the Budget failed to enforce the stated requirement for RACP project applicants to include economic impact statements in their applications.

Although RACP was established in 1984 as a tool for economic development, the Commonwealth waited until 2003 to require applicants to include an economic impact statement in the application packet.

As incongruous as it may appear to go almost 20 years without requiring an economic impact statement as part of the application packet, that failure is not surprising in view of our discussion in Finding One. As we pointed out, the Governor and members of the General Assembly listed projects in capital budget acts without the benefit of even an application, much less one without an economic impact statement. Applications were required after the fact—that is, only *after* projects received their grant authorization letters from the Secretary of the Budget.

Clearly, by requiring economic impact statements as part of the application packet, the statements could not have been used in the selection process. Thus, even the economic impact statements required since 2003 served merely as window dressing for the Office of the Budget to suggest that economic impact is part of the RACP program. Stated in the most direct terms, we found that economic impact statements have served no purpose other than to be filed away as an after-the-fact attempt to show that economic impact was somehow considered in the RACP process.

Despite this pretense, applicants since 2003 have been provided with the following instructions when completing their RACP applications:

> all applications shall thoroughly discuss the regional and/or multi-jurisdictional **economic impact** of the project, and applicants must provide all available and projected information about the areas below. Explain any assumptions.[20]

According to the application handbook, the areas of economic impact that must be addressed in the application are as follows:

1. Number of direct permanent, non-construction jobs created by project.
2. Number of indirect permanent jobs created by support/supplier industries and secondary industries attracted by the project.
3. Average wage for direct and indirect jobs.
4. Economic circumstances of the host municipality's and county's population.
5. Project's potential to enhance regional vitality.
6. Annual spending generated by the project during normal operations. Exclude construction spending.
7. Annual spending that would be generated by support/supplier industries and secondary businesses attracted to the project.
8. Total state and local tax generation (payroll, sales, real estate, etc.).
9. Benefit to regional population, either directly or indirectly, from the project as a result of its day-to-day operations.
10. Blighted area and/or facility elimination and/or reuse.

Despite the fact that the Governor and the General Assembly selected projects for funding without such information, we tested 14 grant application files to determine the extent to

[20] Redevelopment Assistance Capital Program, Application Handbook, June 2008 (emphasis added).

which applicants provided it. Our testing was important to determine the extent to which the Office of the Budget at least <u>attempted</u> to ensure that applicants met requirements. It was also our expectation that the Office of the Budget would eventually use the economic impact statements to see if projects ultimately accomplished what applicants said would be accomplished.

In examining the 14 grant application files, we found that 5 of them—or more than one-third—lacked various economic impact statement documents. In fact, one sub-grantee, a college, failed to comply with <u>any</u> required economic impact statement information for its science center under construction. Another sub-grantee, a hospital, provided information on only one of the ten economic impact areas for its emergency room renovations. Three other sub-grantees failed to submit economic impact statements to address three of the ten areas. These three sub-grantees failed to provide information related to economic impact areas numbers 3, 7, and 8 from the list on the preceding page.

When we asked Office of the Budget staff about the deficiencies in the economic impact statements for these five deficient applications, the officials explained that the missing information simply was not submitted and that applicants are not mandated by any laws to submit such information. These officials went on to state that the Office of the Budget executed grant agreements and moved forward with these projects without the economic impact information.

Overall, as we have stated at the beginning of this finding, the "requirement" for an economic impact statement has been used as nothing more than window dressing.

Recommendation

6. The Office of the Budget should reject any application that does not contain a fully completed economic impact statement.

Finding Five

The Office of the Budget failed to measure or monitor the economic impact of RACP projects.

As we have already mentioned, the Office of the Budget has said that RACP funding priority was given to projects with "significant potential for improving economic growth and the creation of jobs." The Capital Facilities Debt Enabling Act mirrors this position in its definition of RACP projects:

> … [E]conomic development projects which generate substantial increases in employment, tax revenues or other measures of economic activity.[21]

Likewise, the RACP grant authorization letters signed by the Secretary of the Budget informed each recipient of the following:

> RACP funding is intended to provide much needed economic stimulus to the Pennsylvania economy and it is intended to assist in the immediate creation of quality family-sustaining jobs for Pennsylvanians.

And finally, as we stated in the previous finding, it was our expectation that the Office of the Budget would eventually use the applicant's required economic impact statements to see if projects ultimately accomplished what applicants said would be accomplished. Despite these apparent attempts to prioritize and document economic benefits, we found that neither the Office of the Budget nor any other state government entity actually ***measured*** the economic impact of RACP projects once they were completed.

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[21] 72 P.S. § 3919.302. This act also states that RACP projects include those with a cultural, historical, or civic significance, as well as those which have a regional or multijurisdictional impact.

The RACP grant agreements between the Commonwealth and the grantees included no requirements for grantees to provide economic impact status reports or any other economic impact reports. Nor did the agreements say that the Office of the Budget or any other state agency was required to measure the economic impact of RACP projects as those projects moved forward.

In short, despite the millions of taxpayer dollars at stake, the state did not monitor the economic impact of the projects that were being funded.

When we asked Office of the Budget officials why they did not monitor RACP projects in progress—i.e., on an on-going basis prior to completion—for their potential economic impact, the officials said they had no grounds or basis to hold the grantees accountable for economic impact claims. In short, the officials said they didn't do monitoring of projects in progress because there was no written requirement to do so.

It should not take a written requirement for state officials to see the importance of measuring the economic impact potential of a program that is supposed to grow the economy. The Office of the Budget's admitted failure to require the information that would form the basis for such measurement—and the failure of that office to monitor the economic claims of applicants who are still allowed to proceed without providing such information—is inexplicable. Without such monitoring, neither the state nor the grantees are held accountable to the taxpayers whose millions of dollars helped to fund RACP projects that have supposedly benefited communities across the state.

The Office of the Budget also failed to measure the economic impact of RACP projects once they were completed

Since the Office of the Budget did not conduct on-going monitoring related to the potential economic development of projects in progress, we expected that surely there would be a measurement of economic impact once the projects were completed. But such was not the case.

Once the construction is completed and RACP projects are finalized, the Office of the Budget is required to conduct a close-out audit of each project. These audits include an examination of grant receipts and expenditures, a determination of compliance with the terms and conditions of the grant agreement, and a review of the documentation supporting the grantee's payment requests. Generally, these close-out audits are conducted at the project site.

We did find that close-out audits were completed (close-out audits are discussed in more detail in Finding Eight of this report). However, the close-out audits contained <u>no</u> procedures to determine projects' economic impacts, whether or not the applicants had claimed such impacts during the application process. Again, despite the millions of taxpayer dollars at stake, the state demonstrated no apparent interest in the economic impact of projects in a program that was touted as having such an impact.

Unfortunately, the Office of the Budget's close-out audits represent the final opportunity for the Office of the Budget to determine the economic benefits, if any, of RACP projects. We say "final opportunity" because, after such audits, the Office of the Budget closed the project files and no further monitoring or follow-up occurred.

No consequences for grantees' failure to generate positive economic impact in terms of jobs and/or increased tax base

Because the Office of the Budget did not monitor RACP grantees' progress towards economic impact goals, if any were even provided in the application, the Office of the Budget did not know if these grantees met their economic impact goals. Even if the Office of the Budget had monitored the status of the economic impact goals, there were no written consequences to the grantee for failure to realize the economic impact claims made on the application.

The Office of the Budget has failed to take any actions to measure the economic impact of any RACP project or even to ensure that the economic impact claims made by RACP applicants are realized.

Overall, the state has failed to monitor the economic impact of RACP projects throughout their entire life cycle, whether at authorization, application, funding, or completion. <u>No</u> <u>one</u>—including the Office of the Budget and the applicants themselves—is held accountable to the taxpayers who fund these projects.

Recommendations

7. The Office of the Budget should consider including provisions in its standard RACP grant agreement to measure economic impact and to require the grantee to return the grant award, or portions thereof, if significant expectations of positive economic impact are not met.

8. The Office of the Budget should include steps in its close-out audit procedures to measure the extent to which completed projects are capable of meeting expected economic impact goals as stated in the applications.

Finding Six

The Office of the Budget ensured that applicants were eligible. However, the primary applicant in most cases is a conduit for another entity to obtain grant funding, and those other entities have no eligibility requirements.

The Capital Facilities Debt Enabling Act defines RACP applicants as one of the following:

- A redevelopment authority
- An industrial development authority
- A general purpose unit of local government
- A local development district
- Any public authority established pursuant to the laws of the Commonwealth
- An industrial development agency as certified by the Pennsylvania Industrial Development Authority Board[22]

This eligibility requirement is placed on the primary applicant (as we will refer to it here), which is the entity that enters into a grant agreement with the Commonwealth and becomes the RACP grantee. We reviewed the grant award documentation for 288 grants awarded from July 1, 2005, through June 30, 2010, and we found that each grantee appeared to be eligible based on one of the definitions listed in the Capital Facilities Debt Enabling Act.

Looking further, however, we found that the overwhelming majority of grantees entered into cooperative agreements with other entities that became what we will call “sub-grantees” for the RACP funding. This finding was not surprising when we consider that eligible entities include development authorities

[22] 72 P.S. § 3919.302.

whose primary purpose is to serve as a pass-thru entity to help businesses obtain government financing for development. In other words, with the establishment of the state eligibility criteria, the General Assembly intended for a business other than the applicants to be the true beneficiaries of RACP funds.

It is not our position that having a "sub-grantee" is wrong; that type of analysis was not expected to be part of this audit. However, by allowing development authorities to be eligible applicants for RACP funding, the General Assembly has created another element of non-transparency in the RACP program. In short, the true beneficiaries are not listed as the grantees, and once again the citizens of the Commonwealth do not know who is benefiting from their tax dollars.

RACP places no eligibility restrictions on sub-grantees receiving RACP grants

While the Capital Facilities Debt Enabling Act clearly defines the type of entity that can be an applicant for RACP funding, neither the act nor the Office of the Budget place any restrictions on the eligibility of sub-grantees to receive RACP funds. Therefore, numerous private developers and other for-profit businesses received RACP funding.

When a RACP applicant passes the funding on to another beneficiary, the Office of the Budget requires the applicant and the beneficiary sub-grantee to sign a cooperative agreement. Through the activation of that cooperative agreement, the applicant assigns all project administrative duties and legal mandates onto the sub-grantee.

In order to determine the extent to which applicants entered into cooperative agreements with sub-grantees and the types of entities that were sub-grantees, we requested and obtained from the Office of the Budget the names of the sub-grantees involved in 39 RACP projects. The 39 projects consisted of the 14 in our core test group and 25 others that were randomly selected from an Office of the Budget's RACP project listing. We found no sub-grantee in 4 of the projects; therefore, no cooperative agreement was necessary. The other 35 projects —or 90 percent—had sub-grantees.

A breakdown of the 35 sub-grantees, by type of entity, is as follows:

Sub-grantee entity types (35 reviewed)	
Business Type	**Number**
Private for-profit business	17
Non-profit organization	8
Economic development council	5
College	3
Labor union	2

With regard to the private for-profit businesses, we found that some were privately owned companies, some were property management companies, and one was a movie theater. Some of these companies were structured as limited partnerships, while others were limited liability companies.

When we asked Office of the Budget officials how private for-profit businesses could receive RACP funds, they stated that since no guidelines were in place defining an eligible sub-grantee, the Office of the Budget did not deny applications based on such sub-grantees. The officials further said that the Office of the Budget checked only to see that the grantees signed cooperative agreements with the sub-grantees. It was the Office of the Budget's position that the grantees were responsible for ensuring that sub-grantees were capable of meeting the responsibilities outlined in grant agreements.

We could find no explanations as to why the RACP enabling legislation or the Office of the Budget did not establish any eligibility requirements for sub-grantees and as to why millions of tax dollars were awarded to companies that have millions, possibly billions, in assets and earnings, while many cash-strapped public projects go without state funding.

Just because program legislation does not require sub-grantees to meet program eligibility does not mean the Office of the Budget could not establish eligibility requirements for the sub-grantees. The lack of any requirements specific to sub-grantees opens the door to many concerns regarding the entities which ultimately benefit from the RACP grants.

Taxpayers have every reason to be concerned that eligibility criteria apply to grantees but not to sub-grantees, especially when sub-grantees are the ultimate beneficiaries of the funding.

Amendments to the Capital Facilities Debt Enabling Act are currently being considered by the General Assembly. But, adding eligibility requirements for sub-grantees is not currently included in the amendments being considered.

Recommendations

9. The Office of the Budget should work with the General Assembly to amend the Capital Facilities Debt Enabling Act to place eligibility requirements on those entities that are sub-grantees receiving RACP funds.

10. While working with the General Assembly as recommended above, the Office of the Budget should explore whether on its own it can establish eligibility criteria for sub-grantees and, if so, establish such criteria.

Finding Seven

The Office of the Budget did not provide the public with information about RACP-funded projects, including grantee or sub-grantee.

As we discussed in Finding One, it was difficult for the public to determine what projects were eligible for RACP funds because of the broad, vague, and generic descriptions listed in the capital budget acts. In addition, it was also difficult—if not impossible—for the public to determine the names of the RACP grantees and sub-grantees.

While the Capital Facilities Debt Enabling Act does not require the Office of the Budget to provide the public with the names of the grantee or sub-grantee, it also does not preclude the Office of the Budget from providing the public with this information.

During the five years of our audit period alone, the Office of the Budget executed agreements for 770 RACP grants totaling more than $1.5 billion for 506 projects. Yet neither the Office of the Budget nor any other Commonwealth entity listed any information regarding these projects on a state website, or in any other manner.

Such a posting would have allowed taxpayers to see which entities received RACP funds. Again, RACP selections are not transparent at the very start of the process so it is incumbent upon the Office of the Budget to provide layers of transparency wherever it can and to provide the public with as much information as possible on how tax dollars are spent.

Public access to grant award announcements from a single source—such as the Office of the Budget's website—would provide transparent and accountable information to the public, who should not be forced to research newspapers and other Internet sites in the hopes of finding information about RACP funding.

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A recent change with regard to Internet postings has occurred since Governor Tom Corbett came into office. Under his administration, which began January 20, 2011, a listing of RACP projects approved by Governor Corbett has been posted to the Office of the Budget's website. This listing includes the project name, grant number, dollar amount, county, and the date grant funding was approved. [Note: As of February 15, 2012, Governor Corbett approved more than $1 billion in RACP grants, but it's important to note that all such approvals were actually *re-approvals* of projects from the prior administration; Governor Corbett had frozen those projects until he could review them. According to the Office of the Budget, Governor Corbett himself has not approved any *new* projects as of the February 2012 date.]

While such a posting is a good start, the site still fails to provide the public with the name of the grantee and sub-grantee for each of the projects. It is the public's right to know who receives taxpayer dollars, and it is the Office of the Budget's duty to provide that information.

Recommendation

11. The Office of the Budget should include on its website information on each RACP project awarded grant funding, including the names of the grantee and sub-grantee of each project.

Finding Eight

The Office of the Budget did not conduct project close-out audits of completed projects in a timely manner. Therefore, the Office of the Budget was slow in determining if taxpayer dollars were properly accounted for and if grantees met applicable legal and grant agreement requirements.

As we have noted throughout this report, the Office of the Budget is responsible for the administration, oversight, and monitoring of RACP. In previous findings, we presented the results of our work related to important actions that the Office of the Budget should have taken to go beyond just minimal compliance requirements in order to exhibit better performance, greater accountability, and much needed transparency.

The next four findings are different. We are now presenting the results of our work related solely to compliance issues—that is, how the Office of the Budget performed in carrying out specifically prescribed duties.

In this finding, we discuss the Office of the Budget's poor performance in conducting required close-out audits of the selected projects.

The Capital Facilities Debt Enabling Act states the following:

> Redevelopment assistance capital projects shall be reviewed at regular intervals by the Office of the Budget or its designated agent during the funding phase to ensure financial and program compliance. **A final close-out audit shall be performed by the Office of the Budget or its designated agent for all projects.**[23]

[23] 72 P.S. § 3919.318(g). [Emphasis added.]

Close-out audits should determine the economic impact of RACP projects, as we discussed in Finding 5, and as taxpayers have every right to expect. But the close-out audits do <u>not</u> make such a determination. What they do include is an examination of grant receipts and expenditures, a review of compliance with the terms and conditions of the grant agreement, and a review of the documentation supporting the grantees' payment requests.

While much of the documentation reviewed during close-out audits was the same documentation as that reviewed by the consultants during the project monitoring phase, close-out audits during our audit period were performed by Office of the Budget staff. More specifically, during the five-year period of July 1, 2005, through June 30, 2010, the Office of the Budget staff completed 260 close-out audits of RACP projects.

When we asked the Office of the Budget to provide us with a list of all projects that were completed and awaiting a close-out audit as of June 30, 2010, Office of the Budget officials provided us with a list of 51 projects. Of the 51 projects still awaiting these close-out audits, 3 had been finished for nearly two years, 5 had been completed for nearly one year, and the remaining 43 had been completed for less than one year (between 11 months or as recently as one week prior to our cut-off date of June 30, 2010).

When we asked why there was a delay in completing many of the close-out audits, Office of the Budget officials stated that they experienced a shortage of staff for a period of time and was therefore prevented from completing the close-out audits in a timely fashion.

Although there is no required time frame in which these close-out audits must be completed, their primary purpose is to ensure both the Office of the Budget and the public that RACP funding was properly accounted for and that grantees met all applicable legal and grant agreement requirements.

Accordingly, when the Office of the Budget fails to conduct such audits promptly—i.e., as soon after project completion as possible—then the Office of the Budget cannot know if the grantee continued to maintain compliance with its grant agreement throughout the final stages of the project, and whether the final product was being used for its intended purpose. As a result, the Office of the Budget is not being as accountable to the public as it could be if the audits were conducted sooner.

Close-out audits take on added importance with regard to projects/grantees that have not yet received 100 percent of their requested reimbursements. Office of the Budget staff stated that there can be instances in which the Office of the Budget identifies, either through a review of the consultants monitoring reports or from the review of the reimbursement requests, grantees that have not complied with all provisions of their grant agreements or have not provided adequate documentation to support reimbursement requests. In those cases, the Office of the Budget holds off on making a final reimbursement until after the applicable close-out audit is finalized, thus providing leverage to ensure that any areas of noncompliance are corrected.

When close-out audits are not conducted promptly, RACP grantees who have not fully complied with program requirements may delay doing so until the audits are finally conducted.

Recommendation

12. The Office of the Budget should take immediate action to complete all outstanding close-out audits and complete all future audits in a timely manner.

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Finding Nine

The Office of the Budget failed to monitor completed RACP projects for continued compliance with the grant agreement's terms and conditions.

As the RACP program administrator, the Office of the Budget must ensure that grantees comply with the terms of their grant agreements during all phases of the projects—including after the projects' completion.

Unfortunately, and contrary to its responsibility, the Office of the Budget did not monitor RACP projects once the final close-out audit was completed. Such monitoring is critical because certain actions a grantee takes once the project is finished can violate the grant agreement, and thus compromise the intent of RACP.

For example, Article 8 of the standard RACP grant agreement, titled *Tax Exempt Responsibilities of Grantee*, places restrictions on the grantees with regard to selling or transferring a RACP-funded project to a nongovernmental entity. Those restrictions remain in effect for up to 70 years from project completions.[24]

Article 8, section (C), of the standard grant agreement also states the following:

> In the event of any breach of the provisions of this Article 8 by the GRANTEE, the grantee shall immediately repay to the Commonwealth any and

[24] Article 8, clause (B)(2) states, in part, that the grantee "shall not sell, transfer or convey the PROJECT to a nongovernmental entity for a consideration whose value exceeds the fair market value of the PROJECT less the amount of this CONTRACT and any amendments thereto…." In addition, Article 8, clause (C) also states that "the provisions of this Article 8 shall survive the expiration or earlier termination of this CONTRACT and shall remain in effect until the earlier of (i) seventy (70) years from such date of expiration or termination or (ii) the date upon which all bond indebtedness used to finance the payments made hereunder is fully paid and discharged by the Commonwealth."

> all amounts paid by the Commonwealth to the GRANTEE under this CONTRACT....

Because RACP is funded with tax-exempt debt, the Commonwealth has taken steps to ensure that it complies with all state tax laws by incorporating Article 8 into the RACP grant agreements. Therefore, the Office of the Budget should take all necessary steps to ensure each grantee complies with this provision. But as previously discussed, the Office of the Budget does not monitor projects after the close-out audit is completed.

Office of the Budget officials have stated that they believe their monitoring of a grantee's compliance with the RACP grant agreement ceases at the conclusion of the close-out audit. We disagree. Specifically, the Office of the Budget should continue to monitor those projects that received RACP funds to ensure that the projects comply with post-funding provisions of the grant agreements. Otherwise, the post-funding provisions serve no apparent purpose.

Likewise, the grant agreements place restrictions on the profit or loss amount that can be generated when a RACP-funded project is sold. Only by continual monitoring of the project can the Office of the Budget know if a project site has been sold and, if so, for what amount.

The selling of RACP-funded projects is not a new concern for the Pennsylvania Department of the Auditor General. In 2007 we released a special audit of the Office of the Budget's oversight of the RACP grant for the Mountain Laurel Center for the Performing Arts. Because that facility was sold, we recommended that the Office of the Budget modify all future RACP grant agreements to allow the Commonwealth to recover grant funds if land or facilities purchased, constructed, or renovated with Commonwealth funds were sold or transferred to a for-profit entity for private use or for purposes not in line with the original grant. We also recommended that the Office of the Budget ask the General Assembly to include the same language in RACP legislation.

At the time of this report's release, the Office of the Budget has continued to execute grant agreements without including our recommended language.[25] This failure to implement our past recommendations, in addition to the failure to monitor RACP projects after the close-out audits, means that the Office of the Budget has significantly weakened the state's ability to recoup RACP funds in the event a facility is sold for a profit or is not being used for its intended purposes.

Recommendations

13. The Office of the Budget should implement procedures to monitor RACP-funded projects on a routine basis after the close-out audits have been conducted to ensure that all post-funding terms placed in the RACP grant agreements are met.

14. The Office of the Budget should modify all future RACP grant agreements to allow the Commonwealth to recover grant funds if land or facilities purchased, constructed, or renovated with Commonwealth funds were sold or transferred to a for-profit entity for private use or for purposes not in line with the original grant.

15. The Office of the Budget should work with the General Assembly to amend the Capital Facilities Debt Enabling Act to include language that allows the Commonwealth to recover grant funds if land or facilities purchased, constructed, or renovated with Commonwealth funds were sold or transferred to a for-profit entity for private use or for purposes not in line with the original grant.

[25] The Office of the Budget did not address this recommendation in its response to that 2007 report.

Finding Ten

The Office of the Budget failed to report project information to the General Assembly as required, thus leaving the legislators without important information needed to make informed financial decisions.

The Capital Facilities Debt Enabling Act[26] requires the Secretary of the Budget to provide certain members[27] of the General Assembly with a quarterly report—within ten days of the expiration of each quarter—detailing RACP projects and addressing "at least" all the following:

1. An itemized list of RACP projects approved for release and construction in the preceding quarter.
2. An estimate of the amount of funds remaining under the Commonwealth's debt cap[28] for RACP projects.
3. An estimate of the total amount of outstanding debt related to RACP projects.
4. An estimate of the amount of outstanding debt related to RACP projects which will be paid or refinanced in the succeeding four quarters.

We asked the Office of the Budget for copies of the quarterly reports for the period of July 1, 2005, through June 30, 2011. Based on the requirements, there should have been 24 individual reports, each issued within 10 days of the end of the applicable quarter. For the first half of the period we reviewed, and with one exception (third quarter of 2005), the Office of the Budget issued most reports on time as required. Since the last quarter of 2008, the Office of the Budget consistently failed the timeliness requirement as illustrated in the table that follows.

[26] 72 P.S. § 3919.313(a).
[27] The act provides that the report be sent to the chairman and minority chairmen of the Senate and House Appropriations Committees.
[28] *See* 72 P.S. § 3919.317(b), as most recently amended by Act 48 of 2010, which provides for a cap of $4.05 billion.

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Quarterly reports:
Office of the Budget failed timeliness requirement for last 2+ years and then attempted to catch up with a combined report for 6 quarters

Lateness and failure to report illustrate further lack of accountability, transparency

	Year	**Quarter**	**Timely or Late, plus comments**	
1	2005	3rd quarter	no report issued.	
2		4th quarter	timely	
3	2006	1st quarter	late by 4 months	one report—two quarters combined
4		2nd quarter	late by 1 month	
5		3rd quarter	timely	
6		4th quarter	timely – early by 1 week	
7	2007	1st quarter	almost timely – late by 1 week	
8		2nd quarter	almost timely – late by 1 week	
9		3rd quarter	timely – early by 1 day	
10		4th quarter	timely – early by 1 day	
11	2008	1st quarter	timely – early by 1 week	
12		2nd quarter	timely – early by 1 week	
13		3rd quarter	timely – early by 1 week	
14		4th quarter	late by 2 months	
15	2009	1st quarter	late by 5 months	one report—two quarters combined
16		2nd quarter	late by 2 months	
17		3rd quarter	late by 1 month	
18		4th quarter	late by 1 month	
19	2010	1st quarter	late by 6 months	one report—two quarters combined
20		2nd quarter	late by 3 months	
21		3rd quarter	late by 16 months	one report—six quarters combined in an apparent attempt to catch up
22		4th quarter	late by 13 months	
23	2011	1st quarter	late by 10 months	
24		2nd quarter	late by 7 months	
25		3rd quarter	late by 4 months	
26		4th quarter	late by 1 month	

As the table shows, the pattern of poor performance by the Office of the Budget began in late 2008, culminating with its failure to release *any* reports for 2011 until it combined six entire quarters into one report released in mid-February 2012 as our audit work was nearing completion. [As we previously noted in Finding Seven, Governor Corbett did not approve any new RACP projects since he took office in January 2011. However, even though no new projects were approved, the Office of the Budget should not be releasing itself from the quarterly requirement to provide program information to the General Assembly.]

Without the benefit of such important information from the Office of the Budget as required, the General Assembly—which is responsible for approving millions of dollars in general obligation bond issues for RACP projects—has nonetheless increased the Commonwealth's debt ceiling by billions of dollars. Legislators thus did not have the information needed to make fully informed decisions on debt financing and refinancing.

In reviewing the reports that the Office of the Budget ***did*** complete from October 1, 2005, through June 30, 2010, and submitted to the General Assembly as required, as well as the latest report dated February 15, 2012, we found that each required item was included.

With regard to the first required item—an itemized list of RACP projects approved for release and construction—we found that this list included the name of the project, the approved grant amount, the grant approval date, and the county in which the project is located. However, these quarterly reports are limited because they do not include information on the grantees and sub-grantees. Given that the Enabling Act provides that the reports should address "at least" all of the outlined topics, the Office of the Budget staff should not only meet the basic minimum requirements but also strive to meet the intent of the act to provide additional pertinent information where necessary. Again, as we discussed in Finding One, not all government officials are aware of all RACP-funded projects; nor is the public provided with sufficient information about these projects. Overall, a lack of transparency was evident throughout the RACP process from start to finish.

Recommendations

16. The Office of the Budget should ensure that it complies with the Enabling Act by preparing its quarterly reports and providing them to the General Assembly as required.

17. The Office of the Budget should meet the intent of the Enabling Act by providing additional germane information including the names of grantees and sub-grantees on the list of projects it provides to the General Assembly as part of each quarterly report.

Finding Eleven

The Office of the Budget ensured that projects were adequately monitored throughout the construction phase. Also, the Office of the Budget properly reviewed expense documentation and made appropriate approvals for reimbursement payments.

In order to determine the extent to which the Office of the Budget monitored the construction progress of RACP projects as well as the applicants' compliance with grant agreements during the construction phase, we examined 14 project files and all supporting documentation in those files. We reviewed the authorization letters, the grant agreements, the applications, construction monitoring reports, payment requests, and documentation supporting requests for payments.

The Office of the Budget used consultants—based on specific areas of expertise--to process RACP applications and for construction monitoring

The Office of the Budget did not have staff with sufficient expertise in the construction industry so it hired outside consultants to review RACP applications and to monitor project construction. Specifically, during our audit period of July 1, 2005, through June 30, 2010, the Office of the Budget contracted with 15 engineering consulting firms at a cost of more than $12.5 million for these services.

Office of the Budget officials explained to us that they assigned consultants to projects based on each consultant's area of expertise and availability, as well as on the number of projects already assigned to each particular consulting firm. Each consulting firm was responsible for multiple RACP projects at a time.

In examining the 14 RACP project files that we selected, we found that each consulting firm conducted a detailed review of each RACP application and, upon completion of the review, submitted an application review report to the Office of the Budget.

We also found that, in monitoring RACP projects, the consultants completed construction monitoring reports and submitted such reports to the Office of the Budget. These reports documented each grantee's compliance and/or non-compliance with the grant agreement as construction on the project progressed. From our review of the reports, we were able to determine that the consultants made periodic visits to the RACP-funded project sites.

The number of construction monitoring reports in each project file varied depending on the size of the project. For the 14 files we reviewed, we found between 1 and 11 monitoring reports, with an average of 4 monitoring reports among the files we reviewed.

Based on our professional judgment, the consultants' construction monitoring reports appeared to be detailed and thorough, providing the Office of the Budget with information and documentation on each grantee's project status and compliance with the grant agreement. Based on our sample, the Office of the Budget thus ensured that those grantees constructed their projects in compliance with the terms and conditions of their grant agreements.

The Office of the Budget used its staff to review payment requests; reviews were completed as required before grantees were reimbursed

The Office of the Budget did *not* use consultants to process grant payment requests. Instead, based on our detailed examination of the 14 selected files, we found that the Office of the Budget itself processed requests for grant payments.

Because RACP is a reimbursement program, grantees are required to seek reimbursement from the Office of the Budget for project expenses already paid, as opposed to payment for yet-unpaid expenses. The reimbursement requests can be made as frequently as once a month, but not more often.

Typical reimbursable costs include those for permits, land, construction, and interest paid during construction. Conversely, non-reimbursable costs include those for future physical maintenance and operations, as well as costs for legal, accounting, financing, architecture, engineering, and other administrative-type services.

Based on our extensive review of the 14 sampled files, we found that grantees' payment requests contained sufficient documents showing both actual and estimated costs, thus providing the Office of the Budget with evidence it needed to determine the correct reimbursement amounts.

In addition to finding that the grantees submitted sufficient documentation regarding the *amount* of their reimbursable costs, we found that the Office of the Budget required the grantees to go a step further and to *certify* that such costs were documented, accurate, and eligible. In 11 of the 14 files we examined, we found that grantees, sub-grantees, and architects and engineers all submitted statements verifying the accuracy of applicable costs. The three remaining files contained no reimbursement requests as of June 30, 2011, because the grantees were still not in compliance with special conditions of their grant agreement. (These three projects were discussed in greater detail in Finding 3.)

Overall, we concluded that, with regard to the specific sampled files, the Office of the Budget ensured it had obtained sufficient documentation to support costs, and it properly reviewed expense documentation and made appropriate approvals for reimbursement payments.

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Appendix A

Objectives, Scope, and Methodology

The Department of the Auditor General conducted this special performance audit in order to provide an independent assessment of the Office of the Budget's administration of RACP.

We conducted this audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to 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.

Objectives

The overall objective of this special performance audit was to evaluate the Office of the Budget's administration of RACP, and specifically to answer the five questions enumerated below:

1. Are RACP grant applications complete, and do they contain all the required information? (See Finding 4)

2. Do RACP applicants meet program eligibility requirements? (See Finding 6)

3. How does the Office of the Budget determine that the economic impact, as stated in the grant application, is realized? (See Findings 4 and 5)

4. How does the Office of the Budget monitor the projects in progress and ensure that projects comply with the grant agreements? (See Findings 8, 9, and 11)

5. What actions does the Office of the Budget take against grantees if they fail to meet the grant agreement requirements? (See Finding 3)

Before we could answer those five questions, however, and in attempting to understand the nature and profile of RACP and the Office of the Budget's administrative role, we quickly found a disconnect between what the Office of the Budget knew and what it should have and could have known of the decisions and processes that preceded its direct involvement. This disconnect—and the Office of the Budget's lack of initiative to pursue answers—led to our findings of little or no transparency regarding the selection of RACP projects *before* they got to the Office of the Budget (See primarily Findings 1 and 2). The same lack of initiative led to our finding of insufficient transparency at the Office of the Budget *after* the projects got there (See primarily Finding 7). In fact, the lack of transparency is discussed throughout the report.

Scope

When we began our audit, our original scope focused on all RACP projects that were awarded grants from July 1, 2005, through June 30, 2010, with grant payments made through September 30, 2010.

As we explained in our engagement letter to the former Secretary of the Budget, dated August 26, 2010, our objectives may be adjusted over the course of the audit in accordance with generally accepted government auditing standards (GAGAS).[29] For example, GAGAS Standard 7.07 states, in relevant part, the following: "Planning is a continuous process throughout the audit. Therefore, auditors may need to adjust the audit objectives, scope, and methodology as work is being completed."

On July 7, 2011, we informed the Office of the Budget that we had expanded our scope to include grants authorized from July 1, 2010, through June 30, 2011. This scope expansion enabled us to review the listing of grants re-authorized after the change

[29] *Government Auditing Standards*, July 2007 revision, issued by the Comptroller General of the United States, United States Government Accountability Office, Washington, D.C.

of [Governor's] administration in January 2011 and also to obtain updated information as noted in the report.

Methodology

We designed the methodology to obtain sufficient, appropriate evidence to address the above-listed audit objectives, to reduce audit risk to an acceptable level, and to provide reasonable assurance that the evidence is sufficient and appropriate to support our findings and conclusions.

The methodology we used during this audit included the following activities:

- Interviewed officials from the Office of the Budget including staff from the Bureau of Revenue, Capital and Debt responsible for the administration of RACP.

- Obtained and examined the Office of the Budget's procedures pertaining to its oversight and administration of RACP.

- Obtained and reviewed the Capital Facilities Debt Enabling Act.

- Evaluated the transparency and fairness of the process for itemizing and authorizing RACP projects for grant funding.

- Obtained a sample of RACP project files and performed a detailed review of documentation supporting the authorization, application, grant agreement, and grant award to each applicant.

- Obtained and examined listings of RACP grants that were awarded from July 1, 2005, through June 30, 2011.

- Examined the time elapsed between project itemization and grant authorization.

- Evaluated the eligibility of projects, grantees, and sub-grantees as defined in the Capital Facilities Debt Enabling Act.

- Examined the services provided, and the reports prepared, by outside consultants on contract with the Office of the Budget to assist budget staff with project monitoring and application review responsibilities.

- Examined the expenses incurred by the Office of the Budget relating to outside consultants.

- Examined documentation supporting grant payments made by the Office of the Budget to grantees.

- Examined actions taken by the Office of the Budget to measure the economic impact of RACP projects.

- Examined the Office of the Budget's close-out audit procedures and reviewed a sample of audits completed by the Office of the Budget.

- Determined the nature of RACP projects as well as the names of grantees and sub-grantees for these projects.

Findings and Recommendations

We developed 11 findings during our review of the Office of the Budget's performance related to RACP, and we present 17 recommendations. We will follow up within the next 12 to 24 months to determine the status of our findings and recommendations.

Our expectation is that the findings and recommendations presented herein will improve the Office of the Budget's administration of RACP and will provide a framework for corrective action where necessary.

Appendix B

RACP grant agreements for the period July 1, 2005, through June 30, 2010

RACP grant agreements for the period July 1, 2005, through June 30, 2010
continued on next two pages

County	Number of projects funded	Number of grant authorizations	Total amount of grant funding authorized for these projects	Amount actually paid for projects as of September 30, 2010
Adams	1	1	$10,000,000	$10,000,000
Allegheny	88	143	265,841,554	172,185,122
Armstrong	3	3	4,000,000	1,821,268
Beaver	13	17	22,800,000	16,426,794
Bedford	1	1	5,000,000	5,000,000
Berks	11	26	36,350,000	18,523,824
Blair	5	7	14,050,000	11,260,499
Bradford	2	2	16,500,000	16,500,000
Bucks	13	17	21,450,000	11,750,000
Butler	5	5	6,259,000	3,944,657
Cambria	7	12	19,500,000	16,928,808
Cameron	0	0	0	0
Carbon	4	4	3,950,000	3,795,706
Centre	4	7	17,250,000	13,750,000
Chester	6	7	16,000,000	2,887,948
Clarion	1	2	2,700,000	2,700,000
Clearfield	7	9	28,100,000	15,542,500
Clinton	5	7	10,252,000	7,250,000
Columbia	2	2	1,200,000	1,200,000
Crawford	4	6	7,050,000	6,950,000
Cumberland	3	4	36,250,000	31,702,416
Dauphin	10	18	71,200,000	64,372,731
Delaware	13	21	61,750,000	37,073,303

RACP grant agreements for the period July 1, 2005, through June 30, 2010
continued

County	Number of projects funded	Number of grant authorizations	Total amount of grant funding authorized for these projects	Amount actually paid for projects as of September 30, 2010
Elk	2	2	4,300,000	300,000
Erie	9	15	33,800,000	27,014,347
Fayette	5	6	8,100,000	6,635,932
Forest	0	0	0	0
Franklin	0	0	0	0
Fulton	1	1	3,000,000	3,000,000
Greene	4	5	10,050,000	8,266,652
Huntingdon	0	0	0	0
Indiana	7	8	6,750,000	5,000,000
Jefferson	1	2	2,000,000	1,628,549
Juniata	0	0	0	0
Lackawanna	13	16	74,114,000	42,942,540
Lancaster	19	25	57,900,000	43,449,425
Lawrence	3	4	6,100,000	100,000
Lebanon	3	4	5,200,000	4,200,000
Lehigh	18	34	52,075,000	33,447,187
Luzerne	16	21	36,000,000	19,838,541
Lycoming	7	7	15,500,000	9,462,500
McKean	1	3	4,000,000	4,000,000
Mercer	2	2	2,750,000	968,196
Mifflin	1	1	2,000,000	663,399
Monroe	1	1	5,000,000	0
Montgomery	26	28	50,930,000	27,217,866
Montour	0	0	0	0

Pa. Office of the Budget: Poor Administration of the Redevelopment Assistance Capital Program

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
June 2012

RACP grant agreements for the period July 1, 2005, through June 30, 2010
continued

County	Number of projects funded	Number of grant authorizations	Total amount of grant funding authorized for these projects	Amount actually paid for projects as of September 30, 2010
Northampton	13	28	40,600,000	13,648,127
Northumberland	3	5	5,000,000	1,444,690
Perry	0	0	0	0
Philadelphia	97	167	353,779,267	213,330,258
Pike	2	2	1,500,000	500,000
Potter	0	0	0	0
Schuylkill	2	2	4,000,000	199,305
Snyder	1	2	4,500,000	0
Somerset	3	3	2,500,000	2,000,000
Sullivan	1	1	1,000,000	1,000,000
Susquehanna	0	0	0	0
Tioga	0	0	0	0
Union	0	0	0	0
Venango	1	1	500,000	0
Warren	2	2	2,400,000	2,090,358
Washington	13	21	23,000,000	18,218,009
Wayne	0	0	0	0
Westmoreland	13	21	24,350,000	21,266,643
Wyoming	0	0	0	0
York	8	9	27,250,000	18,313,888
Totals	**506**	**770**	**$1,547,400,821**	**$1,001,711,988**

Appendix C

List of 14 Project Files Tested for This Audit

The tables that follow list the 14 RACP project files that our auditors tested for certain compliance issues as described in this audit report.

Please note that, although we could test for certain compliance issues, the lack of transparency—as discussed throughout this report—prevented us from conducting testing related to *how* or *why* these projects were selected by the General Assembly and the Governor for RACP funding.

List of 14 Project Files Tested for this Audit

Audit test file no. and county	Project name,* applicant, and sub-grantee	Capital Budget Act(s) (and amount listed in Act)	Total amount of funding authorized (and date first authorized)	Total grant funding received by sub-grantee as of 09-30-10	Project description**
1 **Berks**	Project Name: Reading Movie Theater Applicant: City of Reading Sub-grantee: Reading Movies, LLC	Act 2002-131 ($4.0 million) Act 2006-83 ($4.0 million)	$4.35 million (6/8/2006)	$4.35 million	Construction of an IMAX and 10-screen movie complex.
2 **Allegheny**	Project Name: Pittsburgh Children's Home Applicant: Urban Redevelopment Authority of Pittsburgh Sub-grantee: The Children's Home of Pittsburgh	Act 2004-40 ($12.0 million)	$5.5 million (2/9/2006)	$5.5 million	Construction of a three-story building and 92-space parking lot to allow for expansion of the Adoption program, Transitional Infant Care Hospital, and the Child's Way program.
3 **Bucks**	Project Name: St. Mary's Medical Center Applicant: Redevelopment Authority County of Bucks Sub-grantee: St. Mary's Medical Center	Act 2004-40 ($10.0 million) Act 2006-83 ($21.55 million) Act 2008-41 ($2.25 million)	$5.75 million (4/18/2005)	$1.5 million	An expansion and renovation of the Orthopedic Care/Surgical Services Facility.
4 **Allegheny**	Project Name: African American Cultural Center Applicant: Urban Redevelopment Authority of Pittsburgh Sub-grantee: August Wilson Center for African American Culture	Act 2000-27 ($15.0 million) Act 2006-83 ($10.0 million)	$9.45 million (3/17/2006)	$9.45 million	The August Wilson Center for African American Culture plans to be a state-of-the-art performing art center in downtown Pittsburgh. The facility will contain art galleries, classrooms, a 500-seat theater, as well as a shop and café to be used as a hub for art, performance, education, and community events.

**Project name was provided by the Office of the Budget*

***Project description was obtained from the Application Review Report prepared by a contracted consultant and on file with the Office of the Budget*

List of 14 Project Files Tested for this Audit

Audit test file no. and county	Project name,* applicant, and sub-grantee	Capital Budget Act(s) (and amount listed in Act)	Total amount of funding authorized (and date first authorized)	Total grant funding received by sub-grantee as of 09-30-10	Project description**
5 **Allegheny**	Project Name: Alle-Kiski Hospital Renovation Applicant: Redevelopment Authority of Allegheny County Sub-grantee: Alle-Kiski Medical Center	Act 2006-83 ($5.0 million)	$2.5 million (10/30/2006)	$1.99 million	Renovate and enlarge the Emergency Department by doubling the square footage and the number of exam/treatment rooms.
6 **Bucks**	Project Name: Port of Bucks Renovation Applicant: Redevelopment Authority of County of Bucks Sub-grantee: Kinder Morgan Terminals	Act 2006-83 ($9.2 million)	$.7 million (10/4/2006)	$0	Major improvements to Kinder Morgan Terminals leased dock infrastructure. Overhead lighting towers are planned for the dock and working areas of the terminal, along with structural repairs to the dock facility and paving the work surface.
7 **Luzerne**	Project Name: Wilkes-Barre Riverfront Commons Applicant: Luzerne County Sub-grantee: None	Act 2006-83 ($17.5 million)	$3.5 million (01-02-2007)	$3.19 million	A major riverfront revitalization effort. The project will provide flood protection, recreational opportunities, and economic development in the city of Wilkes-Barre

Project name was provided by the Office of the Budget

***Project description was obtained from the Application Review Report prepared by a contracted consultant and on file with the Office of the Budget*

List of 14 Project Files Tested for this Audit

Audit test file no. and county	Project name,* applicant, and sub-grantee	Capital Budget Act(s) (and amount listed in Act)	Total amount of funding authorized (and date first authorized)	Total grant funding received by sub-grantee as of 09-30-10	Project description**
8 **Allegheny**	Project Name: Grandview Avenue Renovations Project Applicant: Urban Redevelopment Authority of Pittsburgh Sub-grantee: City of Pittsburgh	Act 2006-83 ($400,000)	$400,000 (1/2/2007)	$0	Improve streetscape along the ridge of Mt. Washington overlooking downtown Pittsburgh by replacing streetlights, installing interpretive signage, and reconstruct four overlooks.
9 **Northampton**	Project Name: Historic Bethlehem Partnership Applicant: City of Bethlehem Sub-grantee: Historic Bethlehem Partnership	Act 2006-83 ($4.0 million)	$3.0 million (1/19/2007)	$0	Improvements to five sites in Bethlehem that are currently being used as tourist attractions. A sixth site may be a renovation of an existing building or construction of a new building to be used as a resource center.
10 **Lehigh**	Project Name: Muhlenberg College of Science Applicant: City of Allentown Sub-grantee: Muhlenberg College	Act 2006-83 ($2.0 million)	$1.2 million (10/4/2006)	$1.2 million	Renovate an existing building and construct a new addition to an existing science building on campus.
11 **Berks**	Project Name: Albright College Science Center; Applicant: Reading City; Sub-grantee: Albright College	Act 2008-41 ($7.0 million)	$6.0 million (9/26/2008)	$2.57 million	Construction of a new four-story addition, including greenhouse, to an existing science building on campus. Renovations will also be made to existing building.

**Project name was provided by the Office of the Budget*

***Project description was obtained from the Application Review Report prepared by a contracted consultant and on file with the Office of the Budget*

List of 14 Project Files Tested for this Audit

Audit test file no. and county	Project name,* applicant, and sub-grantee	Capital Budget Act(s) (and amount listed in Act)	Total amount of funding authorized (and date first authorized)	Total grant funding received by sub-grantee as of 09-30-10	Project description**
12 Schuylkill	Project Name: Schuylkill Women in Crisis Applicant: Schuylkill County Commissioners Sub-grantee: Schuylkill Women in Crisis	Act 2008-41 ($1.0 million)	$1.0 million (8/25/2008)	$199,305	Construction of a three-story addition to the existing 100-year old building, including a small parking lot, to expand shelter housing for domestic violence victims.
13 Allegheny	Project Name: Father Ryan Arts Center Applicant: Redevelopment Authority of Allegheny County Sub-grantee: Focus on Renewal Sto-Rox Neighborhood Corp.	Act 2008-41 ($1.5 million)	$500,000 (11/24/2008)	$500,000	Renovate an existing building to provide dance, music, theater and a visual arts studio.
14 Allegheny	Project Name: Steamfitters Local 449 Expansion; Applicant: Urban Redevelopment Authority of Pittsburgh Sub-grantee: Steamfitters Local Union 449	Act 2008-41 ($2.5 million)	$750,000 (12/17/2008)	$250,000	Construct of a two-story addition to an existing building, including a new elevator, as renovation to the training Construct of a two-story addition to an existing building, including a new elevator, as renovation to the training facility.

**Project name was provided by the Office of the Budget*

***Project description was obtained from the Application Review Report prepared by a contracted consultant and on file with the Office of the Budget*

Appendix D

Response to Audit from Office of the Budget

A copy of the full response from the Office of the Budget appears on the next four pages.

COMMONWEALTH OF PENNSYLVANIA
GOVERNOR'S OFFICE OF THE BUDGET
HARRISBURG

PETER TARTLINE
EXECUTIVE DEPUTY SECRETARY
OFFICE OF THE BUDGET

June 7, 2012

The Honorable Jack Wagner
Auditor General
Room 302, Finance Building
Harrisburg, PA 17120

Dear General Wagner:

The Department of the Auditor General's (AG) Special Performance Audit of the Governor's Office of the Budget's (OB) administration of the Redevelopment Assistance Capital Program (RACP) recommends changes and actions. As illustrated in our response, OB has been in the process of making significant changes to the RACP program. Therefore, in certain instances, we both expected the AG's findings and agreed with them. What was unexpected and disappointing was the less than constructive tone of the report and, in some cases, the lack of meaningful recommendations.

The Corbett administration, from its inception, realized that changes and improvements to RACP were imperative. Over the course of the two years that it took the AG to conduct their audit, the Corbett administration froze 750 RACP projects, authorized no additional projects, reviewed the administration of the RACP program and the feasibility of the frozen projects, and redesigned the RACP program. The redesign of the RACP program was publicly unveiled on June 1, 2012. Notable changes include:

- Reducing funding available for RACP, capping the program at $125 million annually;
- Funding being made available via publicized, semi-annual funding rounds that introduce regularity to the selection process; and
- Redesigning the selection process so that there is transparency in how projects are scored and who is selecting them.

The RACP redesign is now available on its web site at www.budget.state.pa.us. Additional details are provided in our responses to specific findings below.

Finding No. 1

The Corbett administration recognized that the selection process required significant and meaningful improvements. The redesign of RACP was recently added to the RACP web site. Some of the key highlights of this now transparent process are:

- Projects will be selected for funding on a merit-based, objective scoring methodology. Candidates for RACP funding will be required to submit a business plan that addresses the following criteria: job creation/retained, community impact, strategic clusters for development, financial impact/long-term sustainability and construction shovel readiness.

The Honorable Jack Wagner
June 7, 2012
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- After business plans have been analyzed and scored, a Selection Committee, consisting of seven (7) members from various state agencies, will decide which projects will be awarded RACP funding.
- Funding will be made available on a semi-annual basis. Funding will be limited to approximately $125 million per year.
- A list of all applicants per funding round will be posted to the web site.
- All selected projects per funding round will be posted to the web site.

Finding No. 2
The Corbett administration recognized that the program had strayed considerably from its intended purpose of encouraging and assisting in regional economic development projects. The redesign of RACP targets large, regional economic development projects that are transformative in nature. Some of the key highlights are:

- Projects that have the greatest impact on job creation/retention.
- Projects that generate new tax revenue.
- Projects that demonstrate long-term sustainability.
- Projects that are shovel-ready will be given a greater priority.
- An emphasis to a project's economic impact has been added as it is the primary scoring category.
- All projects remaining on the Capital Budget Project Itemization list will have to meet new program criteria.

The current Capital Budget Project Itemization list, in all likelihood, includes the types of large, transformative projects the administration intends to fund, assuming those projects are ready to be constructed within the next year.

Finding No. 3
With an emphasis on shovel ready projects as part of the scoring matrix, the Corbett Administration is demonstrating its commitment to funding projects that can more quickly add family sustaining jobs to the Pennsylvania economy. This commitment produces a selection and application process which is inherently more compressed. In fact, semi-annual funding rounds will be publicized on the web site to include a schedule for public educational seminars, business plan submissions, selection results and application submissions. Given construction starts within one year of business plan submissions and the imminent need for funding, the application process and grant development execution will be greatly expedited.

Finding No. 4
The Corbett administration is emphasizing the importance of the economic impact of RACP projects. Business plan tabs requiring economic development information will be analyzed to determine the project's merits. Failure to include the required information will result in lower scores and, possibly, rejection.

Finding No. 5
OB intends to evaluate economic impact data through submissions by the project. This will be done post-project completion in conjunction with the close-out audit process.

The Honorable Jack Wagner
June 7, 2012
Page 3

Additionally, relative to this finding, the AG recommends that OB consider requiring grantees to return grant awards if significant expectations of positive economic impact are not met. RACP grants are funded from the proceeds of tax-exempt general obligation bonds that are issued by the Commonwealth of Pennsylvania. Modification of grant agreements by OB to allow the recovery of grant funds is likely not permissible under current federal tax law. Such action may violate federal tax laws related to the tax exempt status of the bonds. A general obligation bond issue of the commonwealth can lose its tax exempt status if it attempted to recoup a RACP grant once it was validly issued and disbursed. The basis of this determination lies within the various sections of the federal tax code pertaining to private activity bonds. In general, private activity bonds do not receive the benefit of a federal tax exemption. As your report indicates, a number of RACP grants are provided for economic activity that would ultimately be deemed by the IRS to be private activity. The commonwealth can issue tax-exempt bonds for this purpose because RACP is a grant program and there is no repayment of the grant. Any sort of "clawback" provisions on a RACP grant would likely lead to the grant being deemed a private loan by the IRS, and therefore; the bond from which the RACP grant proceeds were derived would lose its tax exempt status. Loss of the federal tax exemption on the commonwealth's general obligation bonds could cost the commonwealth tens of millions of dollars each year in additional debt service costs.

Finding No. 6

Given the current economic conditions throughout Pennsylvania, it will be the priority of the Corbett administration to focus limited available capital funding on those projects that display significant potential for improving economic growth and creation of jobs. Any decision to include eligibility requirements on sub-grantees in addition to those requirements already in place for grantees could deter entities, including for profit and not-for-profit organizations, from investing in Pennsylvania.

Finding No. 7

The Corbett administration recognized that transparency had to be a key feature of the RACP redesign and that the web site would need to play an important role in that process. As the AG notes in its audit report, the administration began posting additional program information to the web site. As part of the RACP redesign, OB will now post to its web site a listing of candidates applying for grants and those projects selected for funding. Information to be posted by OB on the web site will include: the project name, the candidate applying for RACP funding, the county and municipality which contains the project, the grant amount requested by and awarded to the candidate, and a project description. Those projects not selected for funding will also be posted to the web site. The web site will be updated for new candidates as each funding round occurs.

Finding No. 8

While OB acknowledges that timely audit information is essential, the AG makes no attempt to define what timely is or might be. OB, like every other state agency, is continuously asked to do more with less. RACP closeout audits are no exception. As noted by the AG, the RACP program grew significantly during their audit period. At the same time, OB went through a financial transformation within its Comptroller's Office. During the course of this financial transformation and the two years to follow, three different audit organizations within OB were responsible for conducting these closeout audits. Each time there was a transition of these audit responsibilities, there were inefficiencies that needed to be overcome due to knowledge transfer. As a result of these transitions, some closeout audits may have been delayed. However, as the AG acknowledges in Finding No. 11, OB continued to provide for the monitoring of projects throughout the construction phase and reviewed expense documentation for appropriate

The Honorable Jack Wagner
June 7, 2012
Page 4

approvals for reimbursement payments. Thus, OB continued to ensure accountability of tax payer dollars even when closeout audits may have been delayed. The Corbett administration immediately recognized that RACP's growth was unsustainable and has announced its intention to dramatically reduce RACP funding levels to $125 million annually. This strategy will promote regular, more even and substantially reduced workflows throughout all of RACP's administrative functions.

Finding No. 9

One of the goals of RACP projects is to spur economic development in a region. Recouping RACP funding from projects that, in good faith, were thought to spur economic development, will ultimately have a negative effect on a region and its populace. It's quite likely that many of these projects will not have the funding available to pay back the commonwealth. Limited financing options are one of the reasons many projects seek out RACP funding. The recouping of grant funds from projects that failed to meet expectations will likely force the closure of projects around the state.

In addition, please see our response to Finding No. 5, as we believe adding "clawback" provisions to RACP grant agreements would have a negative impact on the tax exempt status of the commonwealth's general obligation bonds.

Finding No. 10

OB submitted a report to the specified members of the General Assembly on February 15, 2012, that included program activity and other required information from June 30, 2011 through the date it was sent. That report noted activity attributable to the prior administration and clearly indicated that the Corbett administration had not yet authorized any RACP grants. The Corbett administration immediately recognized the need for substantive and meaningful changes to RACP and as it began to evaluate the unprecedented number of projects authorized by the prior administration that were frozen at the beginning of its administration, it began to develop the framework for a RACP redesign that is now embodied on the RACP web site. Two of the key features of that redesign are transparency and rigorous monitoring, measurement and reporting. OB expects the reports to the General Assembly to be submitted as intended by Capital Facilities Debt Enabling Act.

If you have any additional questions, please feel free to contact me at (717) 787-2542.

Sincerely,

Peter J. Tartline
Executive Deputy Secretary

cc: Anna Maria Kiehl
John Kaschak
Rick Dreher
Steve Swalm
Thomas Carter

Appendix E

Press release from Office of the Budget

On June 5, 2012, via the press release that we have reprinted on the next two pages, the Secretary of the Budget announced what he called "sweeping reforms" of the Redevelopment Assistance Capital Program.

The announcement came just two days before the Secretary's office provided a formal written response to our audit and clearly represents reform planning and/or work in progress during our field work. As we noted in the Results in Brief section of this report, this significant information was *not* provided to us during our field work or during any of our meetings.

While the announced program redesign appears to address various findings that we report and recommendations that we made, only time—plus a future audit—will confirm the veracity and effectiveness of any such changes.

pennsylvania
OFFICE OF THE BUDGET

News for Immediate Release

June 5, 2012

Redevelopment Assistance Capital Program Redesigned to Focus on Economic Growth, Transparency

Harrisburg – Pennsylvania Budget Secretary Charles Zogby today announced sweeping reforms to the Redevelopment Assistance Capital Program, or RACP, which will now be known as the Pennsylvania Economic Growth Initiative.

The revised and improved program now features a strategic, merit-based selection process that focuses public investments on projects that have a clear, positive economic impact for the state and local communities, with a priority on attracting and retaining jobs.

"These important changes are much more than just a new name for an old program; they reflect Governor Corbett's insistence on positioning Pennsylvania to better compete in a global economy," Zogby said. "This program will allow us to invest in communities by focusing on projects that will create jobs and strengthen our economy."

The redesigned program will have a clearly defined application process with published guidelines and procedures, a merit-based evaluation and selection system, increased transparency, and will maintain thorough monitoring, measurement and reporting, including posting all applicants and selected projects on the Office of Budget's website.

The new process will introduce regularity and dependability to the selection and release of program funds. Projects will now be selected through an objective, merit-based system which will prioritize large, regional economic development projects; projects promising the greatest financial benefit to Pennsylvania's economy; projects that will have the greatest impact in job creation and retention; projects that maximize generation of new tax revenue and projects that demonstrate long-term sustainability.

The program will also prioritize "shovel-ready" projects set to begin construction in 365 days or fewer; and will favor those projects that leverage maximum private investment.

"This newly improved program will allow us to retire old debt instead of saddling it onto our children," Zogby said.

Zogby said that under previous administrations, RACP spending had grown to a level of debt borrowing that had become unsustainable for the state and its taxpayers, growing from $400 million in 1986 to slightly more than $4 billion in 2010. He also said that the program had strayed considerably from its intended purpose of encouraging and assisting in regional economic development projects.

The funding will now be set at about $125 million each year, with releases being set at a much lower level than in previous years. All projects still on the legislative authorization list will have to meet the new program criteria.

For more information, visit the Budget Office online at www.budget.state.pa.us and select the Redevelopment Assistance Capital Program link. For statutory and legislative purposes, the program will continue to be known as the Redevelopment Assistance Capital Program.

Media contact: Eric Shirk, 717-783-1116

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Pa. Office of the Budget: Poor Administration of the Redevelopment Assistance Capital Program

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
June 2012

Audit Report Distribution List

This report was distributed to the following individuals upon its release:

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Mr. Rick Dreher
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Office of the Budget

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