



G A O

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United States Government Accountability Office
Washington, DC 20548

October 15, 2004

The Honorable Richard C. Shelby
Chairman
The Honorable Paul S. Sarbanes
Ranking Minority Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Michael G. Oxley
Chairman
The Honorable Barney Frank
Ranking Minority Member
Committee on Financial Services
House of Representatives

Subject: *Local Television Act: Status of Spending for Fiscal Year 2003*

In December 2000, the Congress passed the Launching Our Communities' Access to Local Television Act of 2000 (Local TV Act or act).¹ The act created the Local Television Loan Guarantee Program (Program) and established the Local Television Loan Guarantee Board (Board) to finance projects that will provide access to signals of local television stations to households in areas with limited or no access to such signals from a commercial satellite service or other multichannel video provider. The Board may approve loan guarantees up to 80 percent of loans totaling no more than \$1.25 billion in aggregate. In November 2001, the Congress appropriated \$2 million for administrative expenses to implement the Program.²

Section 1006 of the act requires that we perform an annual audit of the (1) administration of the provisions of the act, and (2) financial position of each applicant who receives a loan guarantee under the act, including the nature, amount, and purpose of investments made by the applicant. In October 2003, we issued our first annual report³ as required by the act. In that report, we addressed program administration and key activities that occurred during fiscal years 2002 and 2003. We

¹ Pub. L. No. 106-553, title X, 114 Stat. 2762A-128 (Dec. 21, 2000) (*codified in part at* 47 U.S.C. §§1101-1110).

² Agriculture, Rural Development, Food and Drug Administration and Related Agencies Appropriations Act, 2002, Pub. L. No. 107-76, title III, 115 Stat. 704, 725 (Nov. 28, 2001).

³ *Local TV Act: Progress Made, but Timeliness and Cost Accounting Issues Need to be Addressed*, GAO-04-134 (Washington, D.C.: Oct. 31, 2003).

reported that the Program had not been established expeditiously as specified by the act and that the full costs of administering the Program were not accumulated and charged to the Program as called for by federal accounting standards. Because the regulations and underwriting criteria that would have provided the overall framework for the Program had not been implemented at the time of our initial review, lending activities were delayed. Therefore, there were no loan guarantee applicants to audit, which was one of our mandated audit objectives under Section 1006 of the act. This second report addresses the status of the \$2 million administrative appropriation and the fiscal year 2003 Working Group⁴ costs.

To determine the status of the \$2 million administrative appropriation and the Working Group costs incurred during fiscal year 2003, we obtained and evaluated information from the Board, including budget, contract and cost data, minutes of Board meetings, and other related information. Further, we reviewed federal accounting standards to determine if Working Group costs were accounted for properly. We did not independently verify or audit the Working Group cost data we obtained from the Board. We conducted our work from March 2004 through September 2004 in accordance with generally accepted government auditing standards. We requested comments on a draft of this report from the Chairman of the Board.

During fiscal year 2002, the Department of Agriculture obligated the \$2 million in appropriated funds by issuing an order to GovWorks for its anticipated needs. GovWorks is a franchise fund established within the Department of the Interior by the Congress and the Office of Management and Budget to offer administrative services to federal agencies. As of the end of fiscal year 2003, GovWorks had awarded, on the Board's behalf, contracts totaling almost \$1.2 million, leaving approximately \$802,000 of the \$2 million administrative appropriation still available for contracting with outside consultants or other administrative expenses. Table 1 summarizes the activity for this appropriation for fiscal years 2003 and 2002.

⁴ The Working Group, which the Board established based on authority granted in the act, consists of senior level officials and staff from the Board members' departments and agencies, including the Departments of Agriculture, Commerce, Treasury, and the Board of Governors of the Federal Reserve System.

Table 1: Status of Administrative Appropriation as of September 30, 2003

Appropriation received by the Department of Agriculture (USDA) during fiscal year 2002 ^{a,b}		\$2,000,000
Less contracts awarded by GovWorks during:		
Fiscal year 2002 – Ernst & Young, LLP for developing underwriting criteria (includes \$20,323 GovWorks fee)	\$ 697,771	
Fiscal year 2003 - Arnold and Porter for legal services ^c	<u>500,000</u>	<u>1,197,771</u>
Amount available for contracting with outside consultants as of September 30, 2003		\$ <u>802,229</u>

Source: GAO analysis based on information obtained from the Board.

^aThe Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act, 2002, appropriated \$2 million for administrative expenses necessary for carrying out the Local Television Loan Guarantee Program, which it directed to be transferred to and merged with the appropriation for Rural Development, Salaries and Expenses, Pub L. No. 107-76, 115 Stat. 704, 725. (Nov. 28, 2001).

^bThe Consolidated Appropriations Resolution, 2003, provided that any balances available from prior years for the Rural Utilities Service, Rural Housing and the Rural Business-Cooperative Services salaries and expenses account be transferred and merged with the fiscal year 2003 appropriation, Pub. L. No 108-7, Div. A, title III, 117 Stat. 26, 28 (Feb. 20, 2003). Pursuant to this provision, the balance of the \$2 million appropriated in fiscal year 2002 was carried forward to fiscal year 2003.

^cThis contract is an indefinite quantity, indefinite delivery contract for fixed-price labor services with a maximum dollar threshold of \$500,000. As of May 27, 2004, no services had been obtained. This contract is subject to an administrative fee based on services provided in an amount no greater than \$15,000.

At the Board's request, GovWorks awarded a \$677,448 contract to Ernst and Young for developing underwriting criteria and a \$500,000 contract to Arnold and Porter for legal services. As of the end of fiscal year 2003, approximately \$598,000, about 88 percent of the contract amount, had been disbursed to Ernst and Young. Because the Board had not used Arnold and Porter's services as of the end of fiscal year 2003, the original amount awarded remained available at fiscal year end.

Separate from the \$2 million appropriation for administrative expenses discussed above, the Board reported that during fiscal years 2002 and 2003, the Working Group incurred approximately \$333,742 in administrative costs for continuing development of the Program regulations and underwriting criteria. Table 2 summarizes these costs for fiscal years 2002 and 2003.

Table 2: Summary of Estimated Administrative Costs Incurred by the Working Group For the Fiscal Years Ended September 30, 2002 and 2003

Entity representing the Board	Estimated costs		Total
	Fiscal Year 2002	Fiscal Year 2003	
USDA Rural Utilities Service	\$53,586	\$158,491	\$212,077
Department of the Treasury	11,202	50,402	61,604
Department of Commerce	8,506	31,123	39,629
Federal Reserve Board	5,155	15,277	20,432
Total estimated costs	<u>\$78,449</u>	<u>\$255,293</u>	<u>\$333,742</u>

Source: GAO analysis based on information obtained from the Board. Information is unaudited.

The respective departments and agencies of the Working Group members absorbed these costs from their own salaries and expense accounts rather than being paid from the \$2 million appropriation. Also, as discussed in our previous report,⁵ the total costs of administering the Program were not accumulated and charged to the Program consistent with federal accounting standards.⁶ For example, Working Group costs reported by the Board did not include fringe benefits and overhead. Again, during fiscal year 2003, such costs incurred by the Board had not been included in reported costs. Without accumulating and reporting the costs of administering the Program, the Board will not be able to satisfy federal cost accounting requirements or be in a position to determine the portion of those costs that are statutorily required to be recovered.

The Board provided written comments on a draft of this report. In its response, the Board commented on the accumulation of Board and Working Group costs for the purpose of establishing loan guarantee origination fees and application fees and the delay of lending activities.

The Board stated that we had not made a distinction between the Working Group's costs to date that have been related to developing regulations and underwriting criteria and otherwise setting up the Program and those costs that are eligible for recovery through loan guarantee origination and application fees. The Board also reiterated a point made in commenting on our prior report. This is, when the Board accepts applications or extends offers for loan guarantees, it will ensure that such administrative costs adhere to managerial cost accounting concepts in accordance with federal accounting standards and related guidance, provided that those costs prove to be material. We agree that the Program development costs should not be

⁵ GAO-04-134, 9.

⁶ Federal Accounting Standards Advisory Board. Statement of Federal Financial Accounting Standards No. 4: *Managerial Cost Accounting Standards*, July 31, 1995.

considered when establishing the loan application or loan guarantee origination fees and have never suggested that they should be.⁷ However, assuming that the Board will eventually process at least one completed application or award at least one loan guarantee, we believe that it needs to establish a methodology to accumulate the costs that the Board and Working Group will incur before applications are accepted. This methodology is needed to meet the statutory requirement that loan application and loan guarantee origination fees be set at a level reasonably expected to offset, but not in the aggregate exceed, these costs. Such a methodology need not be elaborate, as long as it satisfies the basic cost accounting processes prescribed by Statement of Federal Financial Accounting Standards No. 4 (SFFAS No. 4).

Aside from accumulating costs for the purpose of establishing fees, we also continue to believe that appropriate cost information should be available about the Program. As discussed in our previous report, SFFAS No. 4 requires federal agencies to capture the costs of federal programs to assist the Congress in authorizing, modifying, and discontinuing programs and to provide agencies with reliable cost data for making informed managerial decisions and evaluating performance.⁸

Consistent with the previous report, the Board stated that lending activities were delayed because the statute required the Board to procure the services of an independent public accounting firm to assist with developing underwriting criteria and such criteria needed to be developed in accordance with the statute and the regulations. We continue to believe, as stated in our prior report, that the Program has not been established in an expeditious fashion as specified by the act. Based on the criteria stated in the act, the program regulations and the underwriting criteria, which provide the overall framework for the Program, should have been ready for implementation no later than March 2002. Since these key documents were not ready until December 2003, the Board was delayed in initiating the lending activities needed to carry out the objectives of the program. The Board's written comments are presented in the enclosure.

We are sending copies of this report to the Secretaries of Agriculture, Commerce, and Treasury, and the Chairman of the Board of Governors of the Federal Reserve System, members of the Local Television Loan Guarantee Board, and the Director, Office of Management and Budget. We will also make copies available to others upon request. In addition, the report will be available at no charge on the GAO Web site at <http://www.gao.gov>.

⁷ The Local TV Act and implementing regulations require the Board to charge applicants a loan application fee and a loan guarantee origination fee. See Pub. L. No. 106-553, title X, § 1005(n), 114 Stat. 2762A-128-137 (Dec. 21, 2000) (*codified at* 47 U.S.C. § 1104(n)); see also 7 C.F.R. §§ 2201.11(m), (n), 2201.21. The act established the loan application fee “to cover the cost of the Board in making necessary determinations and findings with respect to the loan guarantee application under this act.” The act established the loan guarantee origination fee to cover the administrative costs, including the costs of the Board, associated with the issuance of a loan guarantee. However, the act limits the Board to imposing fees that in the aggregate do not exceed the actual amount of administrative costs under this act.

⁸ GAO-04-134, 9.

We look forward to working with you and your staff on the fiscal year 2004 audit required by the Local TV Act. Should you or your staff have any questions on matters discussed in this report, please contact me at (202) 512-6906 or by e-mail at williamsm1@gao.gov, or Alana Stanfield, Assistant Director, at (202) 512-3197 or at stanfielda@gao.gov. Major contributors to this report include Lisa Crye, F. Abe Dymond, Lauren S. Fassler, Jeff Isaacs, and Christina Quattrociocchi.

A handwritten signature in black ink that reads "McCoy Williams". The signature is written in a cursive style with a large, prominent "M" and "W".

McCoy Williams
Director
Financial Management and Assurance

Enclosure

Comments from the Local Television Loan Guarantee Board



LOCAL Television Loan Guarantee Board
Room 2919-S, Stop 1575
1400 Independence Ave., S.W.
Washington, DC 20250-1575

October 1, 2004

McCoy Williams
Director
Financial Management and Assurance
United States Government Accountability Office
Room 5089
441 G St. NW
Washington, DC 20548

Dear Mr. Williams:

The Government Accountability Office (GAO) recently asked the LOCAL Television Loan Guarantee Board (the Board) for its comments on the second GAO draft report to Congressional Committees on the administration of the provisions of the "Launching Our Communities' Access to Local Television Act of 2000." Specifically, this draft report addresses the status of the \$2 million administrative appropriation and the fiscal year 2003 Working Group costs.

In its report, GAO asserts that Working Group costs, such as fringe benefits and overhead, were not reported and thus the Board will not have the information needed to determine the amount of loan guarantee and application fees needed to cover, but not exceed, the costs of administering the Program. GAO fails to acknowledge that the Working Group's costs to date have not been eligible for recovery through these fees. The Board will only charge an application fee to those applicants whose application has been accepted and that fee will cover the costs of making necessary determinations and findings with respect to that application. See 47 U.S.C. § 1104(n)(1); see also 7 C.F.R. §§ 2201.11(n), 2201.21(a). Moreover, the Board will only charge and collect a loan guarantee origination fee to those borrowers to whom an offer of guarantee is extended and that fee will cover the administrative costs of the Board associated with making such a guarantee regardless of whether the loan closes. See 47 U.S.C. § 1104(n)(2); see also 7 C.F.R. § 2201.21(b). The Working Group's costs to date have been related to developing regulations and underwriting criteria and otherwise setting up the Program. None of these costs have been associated with an application accepted for consideration or the offer of a loan guarantee. Thus the costs incurred by the Board and Working Group to date are immaterial in determining the level of fees to be charged and the need to account for the Working Group's administrative costs in the manner suggested by GAO has not yet occurred. However, when the Board accepts applications or extends offers for loan guarantees, the Board will ensure that such administrative costs adhere to managerial cost accounting concepts in accordance with federal accounting standards and related guidance, provided that those costs prove to be material.

GAO also notes that lending activities were delayed because regulations and underwriting criteria were not implemented at the time of GAO's initial review. As previously reported to GAO, the statute required the Board to procure the service of an independent public accounting firm to develop underwriting criteria and other such matters as the Board considers appropriate. Timing was compromised because the Board followed Federal procurement law in procuring the services of the independent public accounting firm. Timing was further compromised because of the need to develop the underwriting criteria in accordance with the statute and the regulations.

I hope this information is helpful. Please do not hesitate to contact me if GAO has any questions concerning the Board's comments on the report or any issue involving the LOCAL Television Loan Guarantee Program.

Sincerely,



Brian C. Roseboro
Chairman

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