



MICHIGAN

OFFICE OF THE AUDITOR GENERAL

AUDIT REPORT



THOMAS H. MCTAVISH, C.P.A.
AUDITOR GENERAL

The auditor general shall conduct post audits of financial transactions and accounts of the state and of all branches, departments, offices, boards, commissions, agencies, authorities and institutions of the state established by this constitution or by law, and performance post audits thereof.

– Article IV, Section 53 of the Michigan Constitution

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Michigan
Office of the Auditor General
REPORT SUMMARY

*Performance Audit
Clean Michigan Initiative
Environmental Protection Programs
Department of Environmental Quality*

Report Number:
761-0217-12

Released:
November 2012

The Department of Environmental Quality (DEQ) administers environmental protection programs funded by the Clean Michigan Initiative (CMI) bond. These programs include the Brownfield Redevelopment and Environmental Cleanup Program, Waterfront Redevelopment Program, Remediation of Contaminated Lake and River Sediments Program, Nonpoint Source Pollution Prevention and Control Program, Clean Water Fund Program, and Pollution Prevention Program. This performance audit was required by Section 324.19615 of the Michigan Compiled Laws.

Audit Objective:

To assess the effectiveness of DEQ's efforts to ensure that the use of CMI funds complies with laws, regulations, and contract requirements.

Audit Conclusion:

DEQ's efforts to ensure that the use of CMI funds complies with laws, regulations, and contract requirements were effective. Our audit report does not include any reportable conditions related to this audit objective.

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Audit Objective:

To assess the effectiveness of DEQ's efforts to ensure that recipients of CMI funds comply with project outcome requirements.

Audit Conclusion:

DEQ's efforts to ensure that recipients of CMI funds comply with project outcome requirements were effective. Our audit report does not include any reportable conditions related to this audit objective.

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Audit Objective:

To assess the effectiveness of DEQ's efforts to accurately report and comply with CMI program reporting requirements.

Audit Conclusion:

DEQ's efforts to accurately report and comply with CMI program reporting requirements were moderately effective. We noted one reportable condition ([Finding 1](#)).

Reportable Condition:

DEQ did not accurately report CMI project activity ([Finding 1](#)).

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Agency Response:

Our audit report contains 1 finding and 1 corresponding recommendation. DEQ's preliminary response indicates that it agrees with the recommendation and will comply.

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AUDITOR GENERAL

November 9, 2012

Mr. Dan Wyant, Director
Department of Environmental Quality
Constitution Hall
Lansing, Michigan

Dear Mr. Wyant:

This is our report on the performance audit of the Clean Michigan Initiative Environmental Protection Programs, administered by the Department of Environmental Quality.

This report is issued pursuant to Section 324.19615 of the *Michigan Compiled Laws*, which states that every two years that State programs are funded with money from Clean Michigan Initiative bond proceeds, the Office of the Auditor General shall conduct a performance audit of the programs. Upon completion of the performance audit, the Office of the Auditor General shall submit a report on the audit to the audited department and the Legislature.

This report contains our report summary; description of programs; audit objectives, scope, and methodology and agency responses; comments, finding, recommendation, and agency preliminary response; summary of appropriations and expenditures, presented as supplemental information; and a glossary of acronyms and terms.

Our comments, finding, and recommendation are organized by audit objective. The agency preliminary response was taken from the agency's response subsequent to our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a plan to comply with the audit recommendation and submit it within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

We appreciate the courtesy and cooperation extended to us during this audit.

Sincerely,


Thomas H. McTavish, C.P.A.
Auditor General

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Description of Programs

Clean Michigan Initiative (CMI)

In November 1998, Michigan voters approved a \$675 million CMI bond for environmental, natural resources, and health protection programs that would clean up and redevelop contaminated sites; protect and improve water quality; prevent pollution; abate lead contamination; reclaim and revitalize community waterfronts; enhance recreational opportunities; and clean up contaminated sediments in lakes, rivers, and streams. The six environmental protection programs administered by the Department of Environmental Quality (DEQ) are the Brownfield* Redevelopment and Environmental Cleanup Program, Waterfront Redevelopment Program, Remediation of Contaminated Lake and River Sediments Program, Nonpoint Source Pollution Prevention and Control Program, Clean Water Fund Program, and Pollution Prevention Program.

The Department of Natural Resources administers the CMI natural resources protection programs. The Department of Community Health administers the health protection program.

Sections 324.19601 - 324.19616 of the *Michigan Compiled Laws* provide for the specific use of CMI bond proceeds as follows:

	Up to
<u>Environmental Protection Programs:</u>	
Response activities* at facilities*	\$335,000,000
Waterfront improvements	50,000,000
Remediation of contaminated lake and river sediments	25,000,000
Nonpoint source pollution prevention and control projects or wellhead protection projects	50,000,000
Water quality monitoring, water resources protection, and pollution control activities	90,000,000
Pollution prevention programs	20,000,000
<u>Natural Resources Protection Programs:</u>	
State park infrastructure improvements	50,000,000
Local recreation projects	50,000,000
<u>Health Protection Program:</u>	
Abatement of lead hazards	5,000,000
Total	\$675,000,000

* See glossary at end of report for definition.

DEQ's environmental protection programs account for \$570 million (84%) of the total \$675 million in CMI bonds. As of September 30, 2011, the State of Michigan had issued nearly \$474 million (83%) in CMI bonds for the environmental protection programs administered by DEQ.

DEQ's CMI Programs

DEQ, through its various divisions, administers the following six CMI programs:

1. Brownfield Redevelopment and Environmental Cleanup Program (up to \$335 million): This Program provides funding to four subprograms:
 - **Redevelopment-Based Cleanup Projects (\$155 million)**
These projects, part of the Cleanup and Redevelopment Program, fund cleanups and/or demolition at sites in order to promote commercial redevelopment, create jobs, and revitalize neighborhoods. This subprogram also can be used to correct leaking underground storage tanks.
 - **Public Health and Environmental Cleanup Projects (\$97 million)**
These projects, also part of the Cleanup and Redevelopment Program, provide State-funded cleanups at contaminated facilities that pose an imminent or substantial endangerment to the public health, safety, or welfare or to the environment.
 - **Brownfield Redevelopment Grants and Loans (\$75 million)**
This subprogram provides grants (\$37.5 million) and loans (\$37.5 million) to local units of government for response activities at known or suspected contaminated properties with redevelopment potential.
 - **Municipal Landfill Cost-Share Grants (\$8 million)**
This subprogram provides grants to local units of government that undertake cleanup actions at municipal solid waste landfills on, or nominated for, the federal Superfund National Priorities List of contaminated sites.
2. Waterfront Redevelopment Program (up to \$50 million): This Program provides grants to local communities for innovative waterfront improvements that contribute significantly to the local unit of government's economy; to the redevelopment or

revitalization of neighborhoods; and to increase public access to the Great Lakes, their connecting waterways, a river, or a lake. Eligible activities include environmental response activities, acquisition of waterfront property, relocation and/or demolition of buildings and facilities, and infrastructure and public facility improvements.

3. Remediation of Contaminated Lake and River Sediments Program (up to \$25 million): This Program expands efforts already underway to remove sediments from lakes and rivers contaminated by toxins, such as polychlorinated biphenyls (PCBs), mercury, and dichlorodiphenyltrichloroethane (DDT).
4. Nonpoint Source Pollution Prevention and Control Program (up to \$50 million): This Program provides grants to nonprofit entities or local units of government to implement physical structures as identified in an approved DEQ watershed management plan to control the runoff of pollutants such as sediment, nutrients, and pesticides into rivers, lakes, and streams. This Program also funds activities to reduce nonpoint source pollution from a specific pollutant source as identified by DEQ, such as the purchase of land or development rights in critical areas of a watershed or fencing and provision of alternative watering systems to eliminate livestock access to lakes or streams.
5. Clean Water Fund Program (up to \$90 million): This Program, which includes the Water Quality Monitoring Program, provides funds to implement a comprehensive water quality monitoring plan to determine water quality trends, evaluate water protection programs, and detect emerging problems. Also, funding is available to implement recommendations in watershed management plans in designated areas of concern or pursuant to lakeside management plans; provide assistance to local units of government to implement the regulations under phase II of the federal Storm Water Permit Program; identify and eliminate illicit connections to storm sewer systems; provide State matching funds required to access a federal grant for the Conservation Reserve Enhancement Program in Michigan; develop a ground water mapping system for the Drinking Water Program; locate and plug abandoned wells; identify and fix failing septic systems that threaten or impair State waters; protect high quality streams and lakes; develop registration and reporting formats for the Water Use and Withdrawal Program; and provide funding to the village of Chesaning to implement a natural river restoration as a solution to a failing dam.

6. Pollution Prevention Program (up to \$20 million): This Program consists of three subprograms:

- Retired Engineers Technical Assistance Program Fund (\$10 million)
This subprogram creates an endowment to provide funding for pollution prevention assessments by retired engineers and scientists for small businesses, municipalities, and public institutions.
- Small Business Pollution Prevention Assistance Revolving Loan Fund (\$5 million)
This subprogram provides funds to establish a revolving loan fund for small businesses to implement pollution prevention improvements.
- Pollution Prevention Activities (\$5 million)
This subprogram will further pollution prevention activities throughout the State, including start-up funding for local governments to operate household hazardous waste collections; grants to public and private organizations to implement regional pollution prevention projects; establishment of the Green Chemistry Support Program to advance research, development, and implementation of green chemistry technologies and practices; and development of an environmental education curriculum for middle schools.

Audit Objectives, Scope, and Methodology and Agency Responses

Audit Objectives

Our performance audit* of the Clean Michigan Initiative (CMI) Environmental Protection Programs, Department of Environmental Quality (DEQ), had the following audit objectives:

1. To assess the effectiveness* of DEQ's efforts to ensure that the use of CMI funds complies with laws, regulations, and contract requirements.
2. To assess the effectiveness of DEQ's efforts to ensure that recipients of CMI funds comply with project outcome requirements.
3. To assess the effectiveness of DEQ's efforts to accurately report and comply with CMI program reporting requirements.

Audit Scope

Our audit scope was to examine the program and other records of the environmental protection programs of the Clean Michigan Initiative. Not included in the scope of this audit were the natural resources protection programs and the health protection program. We selected the following programs and subprograms to include within the scope of our audit: the Cleanup and Redevelopment Program, Brownfield Redevelopment Grant Program, Brownfield Redevelopment Loan Program, Waterfront Redevelopment Grants Program, Remediation of Contaminated Lake and River Sediments Program, Nonpoint Source Pollution Prevention and Control Program, and Water Quality Monitoring Program.

We did not include the following programs and subprograms within the scope of this audit: the Municipal Landfill Grant Program and Abandoned Well Management Grant Program, Water Use and Withdrawal Program, Drinking Water Program, Voluntary Storm Water Permits Grant Program, Failing On-Site Septic Systems, Protecting High Quality Waters, Illicit Storm Sewer Connection Grants, Remedial Action Plan and Lakewide Management Plans Implementation Grants Program, Conservation Reserve

* See glossary at end of report for definition.

Enhancement Program, Village of Chesaning Water Pollution Control Grant, and Pollution Prevention Program. Accordingly, we do not express any conclusions related to these programs and subprograms.

We conducted this performance 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 finding and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objectives. Our audit procedures, conducted from May through September 2012, generally covered the period October 1, 2009 through September 30, 2011.

As part of our audit, we prepared a summary of appropriations and expenditures for the CMI environmental protection programs at DEQ (see supplemental information). Our audit was not directed toward expressing an opinion on this information and, accordingly, we express no opinion on it.

Audit Methodology

We conducted a preliminary review of DEQ's operations related to CMI to formulate a basis for defining the audit objectives and scope of the audit. We interviewed DEQ personnel to obtain an understanding of DEQ's operations as they related to CMI activities. We reviewed applicable laws, regulations, policies, procedures, and other reference materials. We reviewed selected CMI files, records, and reports. We used a risk-based approach to select CMI-funded programs.

To accomplish our first objective, we interviewed DEQ staff to obtain an understanding of CMI processes and procedures for monitoring CMI projects. We reviewed applicable project monitoring criteria included in the *Michigan Compiled Laws*, appropriations act, and *Michigan Administrative Code*. We tested a random and judgmental sample of projects that were in progress during the audit period and assessed DEQ's efforts to ensure that the use of CMI funds complied with laws, regulations, and contract requirements.

To accomplish our second objective, we interviewed DEQ staff to obtain an understanding of the CMI processes and procedures for completing CMI projects. We reviewed applicable project closeout criteria included in the *Michigan Compiled Laws*,

appropriations act, and *Michigan Administrative Code*. We tested a random and judgmental sample of projects that were completed during the audit period and assessed DEQ's efforts to ensure that recipients of CMI funds complied with project outcome requirements.

To accomplish our third objective, we interviewed DEQ staff to obtain an understanding of the CMI processes and procedures for preparing the annual consolidated report. We reviewed applicable reporting criteria included in the annual appropriations act. We tested a random and judgmental sample of projects that were in progress or completed during the audit period. We reviewed selected portions of the annual consolidated reports for fiscal years 2009-10 and 2010-11 to determine whether DEQ accurately reported CMI information and activity to the State Budget Director, the Senate and House Appropriations Subcommittees on Environmental Quality, and the Senate and House Fiscal Agencies.

Agency Responses

Our audit report contains 1 finding and 1 corresponding recommendation. DEQ's preliminary response indicates that it agrees with the recommendation and will comply.

The agency preliminary response that follows the recommendation in our report was taken from the agency's written comments and oral discussion subsequent to our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and the State of Michigan Financial Management Guide (Part VII, Chapter 4, Section 100) require DEQ to develop a plan to comply with the audit recommendation and submit it within 60 days after release of the audit report to the Office of Internal Audit Services, State Budget Office. Within 30 days of receipt, the Office of Internal Audit Services is required to review the plan and either accept the plan as final or contact the agency to take additional steps to finalize the plan.

COMMENTS, FINDING, RECOMMENDATION,
AND AGENCY PRELIMINARY RESPONSE

EFFORTS TO ENSURE USE OF FUNDS COMPLIES WITH LAWS, REGULATIONS, AND CONTRACT REQUIREMENTS

COMMENT

Audit Objective: To assess the effectiveness of the Department of Environmental Quality's (DEQ's) efforts to ensure that the use of Clean Michigan Initiative (CMI) funds complies with laws, regulations, and contract requirements.

Audit Conclusion: **DEQ's efforts to ensure that the use of CMI funds complies with laws, regulations, and contract requirements were effective.** Our audit report does not include any reportable conditions* related to this audit objective.

EFFORTS TO ENSURE RECIPIENTS OF FUNDS COMPLY WITH PROJECT OUTCOME REQUIREMENTS

COMMENT

Background: Project outcome requirements include the final project documentation that is required by DEQ of the CMI grant recipients as well as contractual goals and objectives of a project. Requirements vary between the various programs granting, loaning, or contracting out the CMI funds. Examples of project outcome requirements include improving accessibility to the waterfront, creating permanent jobs, increasing private investment, or improving a specified number of acres.

Audit Objective: To assess the effectiveness of DEQ's efforts to ensure that recipients of CMI funds comply with project outcome requirements.

Audit Conclusion: **DEQ's efforts to ensure that recipients of CMI funds comply with project outcome requirements were effective.** Our audit report does not include any reportable conditions related to this audit objective.

* See glossary at end of report for definition.

EFFORTS TO ACCURATELY REPORT AND COMPLY WITH PROGRAM REPORTING REQUIREMENTS

COMMENT

Audit Objective: To assess the effectiveness of DEQ's efforts to accurately report and comply with CMI program reporting requirements.

Audit Conclusion: **DEQ's efforts to accurately report and comply with CMI program reporting requirements were moderately effective.** Our assessment disclosed one reportable condition related to the annual report (Finding 1).

FINDING

1. Annual Report

DEQ did not accurately report CMI project activity. Without accurate information, the Legislature cannot provide appropriate oversight of the CMI programs.

The annual report presents summary level funding activity at the program and subprogram levels, including detailed project information for each subprogram. Act 118, P.A. 2009, and Act 189, P.A. 2010, require DEQ to annually report CMI project activity, including site information, total funds expended and awaiting expenditure during the fiscal year, and total amount of bonds issued.

Our review of the annual CMI reports for fiscal years 2009-10 and 2010-11 disclosed:

- a. DEQ had not documented the process for preparing the annual report. Preparing the report is a decentralized process with multiple DEQ program staff preparing or reviewing the various sections of the report. We noted inaccuracies in the annual CMI reports for fiscal years 2009-10 and 2010-11. For example, for 13 of 62 projects reviewed, DEQ inaccurately reported project information such as match amount, estimated closure dates, cumulative expenditures, grant amount, loan funds returned, and project activity status. A documented process would provide guidance to program staff to help ensure that they properly prepare and review the report for accuracy.

- b. DEQ did not accurately report the amount of CMI bonds issued. DEQ understated the total bonds issued to date and overstated the remaining bond authorization amount by \$10.0 million in the annual CMI report for fiscal year 2010-11.
- c. DEQ did not accurately report the program funding summary for the Brownfield Redevelopment Loan Program. DEQ understated loan funds returned and available balance for the Brownfield Redevelopment Loan Program by \$107,524 in the annual CMI reports for fiscal years 2009-10 and 2010-11.

RECOMMENDATION

We recommend that DEQ accurately report CMI project activity.

AGENCY PRELIMINARY RESPONSE

DEQ agrees with the recommendation and will comply.

With regard to part a. of the finding, DEQ informed us that many of the DEQ program areas have written instructions for their portion of the report. DEQ indicated that the reporting errors were minor and did not impact the CMI financial transactions, which were accurate. DEQ informed us that the Administration Division has requested instructions from each program area and will compile them and the programs that do not have written instructions will be asked to develop them. DEQ also informed us that the Administration Division will write instructions to coordinate the report and ensure that reporting is consistent across the programs. In addition, DEQ informed us that errors in the report will be corrected and the report will be reposted with the correct information.

With regard to part b. of the finding, DEQ informed us that it reposted the report with the correct total.

With regard to part c. of the finding, DEQ informed us that a loan recipient did not spend the entire loan draw and returned unspent funds to DEQ. DEQ indicated that this is an unusual occurrence and, to ensure that the error does not happen in the future, the checklist used when closing out grants and loans has been modified to include noting whether the entire loan balance was spent and, if not, the amount

returned. DEQ also indicated that the loan or grant balances on the tracking spreadsheets will be reduced by the returned amount. DEQ informed us that the report will be corrected and reposted.

SUPPLEMENTAL INFORMATION

CLEAN MICHIGAN INITIATIVE (CMI) ENVIRONMENTAL PROTECTION PROGRAMS

Department of Environmental Quality (DEQ)
 Summary of Appropriations and Expenditures
As of September 30, 2011

	<u>Appropriations</u>	<u>Expenditures</u>	<u>Difference</u>
Brownfield Redevelopment and Environmental Cleanup Program	\$ 298,671,239	\$ 277,831,512	\$ 20,839,727
Waterfront Redevelopment Program	49,999,671	49,391,486	608,185
Remediation of Contaminated Lake and River Sediments Program	22,243,126	15,544,312	6,698,814
Nonpoint Source Pollution Prevention and Control Program	36,060,129	30,548,415	5,511,714
Clean Water Fund Program	71,303,088	67,872,341	3,430,747
Pollution Prevention Program	18,623,159	18,063,100	560,059
DEQ Administration	17,087,999	17,087,999	0
Total	<u>\$ 513,988,411</u>	<u>\$ 476,339,165</u>	<u>\$ 37,649,246</u>
Portion of total CMI bonds allocated for environmental protection programs	\$ 570,000,000	\$ 570,000,000	
Percent appropriated and expended	90.2%	83.6%	

Source: Department of Environmental Quality Consolidated Report on the Environmental Protection Bond Fund, the Cleanup and Redevelopment Fund, and the Clean Michigan Initiative Bond Fund, Fiscal Year 2010-11.

GLOSSARY

Glossary of Acronyms and Terms

brownfield	Real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant.
CMI	Clean Michigan Initiative.
DEQ	Department of Environmental Quality.
effectiveness	Success in achieving mission and goals.
facility	Any area, place, or property where a hazardous substance in excess of the concentrations that satisfy the cleanup criteria for unrestricted residential use has been released, deposited, disposed of, or otherwise comes to be located. "Facility" does not include any area, place, or property provided for in Section 324.20101r of the <i>Michigan Compiled Laws</i> .
performance audit	An audit that provides findings or conclusions based on an evaluation of sufficient, appropriate evidence against criteria. Performance audits provide objective analysis to assist management and those charged with governance and oversight in using the information to improve program performance and operations, reduce costs, facilitate decision making by parties with responsibility to oversee or initiate corrective action, and contribute to public accountability.
reportable condition	A matter that, in the auditor's judgment, is less severe than a material condition and falls within any of the following categories: an opportunity for improvement within the context of the audit objectives; a deficiency in internal control

that is significant within the context of the audit objectives; all instances of fraud; illegal acts unless they are inconsequential within the context of the audit objectives; significant violations of provisions of contracts or grant agreements; and significant abuse that has occurred or is likely to have occurred.

response activity

The evaluation, interim response activity, remedial action, demolition, or taking of other actions necessary to protect the public health, safety, or welfare; the environment; or the State's natural resources.

