



Homeland Security

August 9, 2004

MEMORANDUM FOR: Ron Castleman
Regional Director, FEMA Region VI

FROM: Tonda L. Hadley
Field Office Director

SUBJECT: *Cookson Hills Electric Cooperative, Inc.*
Stigler, Oklahoma
FEMA Disaster Number DR-1355-OK
Public Assistance Identification Number 000-UOT6T-00
Audit Report Number DD-13-04

The Office of Inspector General (OIG) audited public assistance funds awarded to the Cookson Hills Electric Cooperative, Inc. (Co-op), located in Stigler, Oklahoma. The objective of the audit was to determine whether the Co-op expended and accounted for Federal Emergency Management Agency (FEMA) funds according to federal regulations and FEMA guidelines.

The Co-op received an award of \$5.20 million from the Oklahoma Department of Civil Emergency Management (ODCEM), a FEMA grantee, for damages resulting from severe ice storms that occurred December 25, 2000, through, January 10, 2001. The award provided 100 percent FEMA funding for four large projects and 75 percent FEMA funding for one large and one small project.¹ We examined the costs for all six projects (see Exhibit). The audit covered the period December 25, 2000, to May 15, 2001, during which the Co-op claimed \$5.20 million and ODCEM disbursed \$4.53 million in direct program costs.

We performed the audit under the authority of the Inspector General Act of 1978, as amended, and according to generally accepted government auditing standards. The audit included tests of the Co-op's accounting records, a judgmental sample of project expenditures, and other auditing procedures considered necessary under the circumstances.

¹ Federal regulations in effect at the time of the disaster defined a large project as one costing \$50,600 or more and a small project as one costing less than \$50,600.

RESULTS OF AUDIT

The Co-op did not follow federal procurement regulations to contract for \$907,274 in disaster work. As a result, fair and open competition did not occur and FEMA had no assurance that contract costs claimed were reasonable. Further, the Co-op claimed \$255,462 (\$209,231 FEMA share) of costs that the OIG found questionable. The questioned costs consisted of ineligible labor costs (\$176,080), duplicate costs (\$37,974), improperly categorized costs (\$17,122), markups on contract costs (\$15,442), and an accounting error (\$8,844).

Finding A: Unallowable Contracting Procedures

The Co-op did not follow federal regulations in procuring \$907,274 in construction and debris clearance work under five contracts. As a result, fair and open competition did not occur and FEMA had no assurance that contract costs claimed were reasonable. Federal regulations at 44 CFR 13.36:

- State that all procurement transactions will be conducted in a manner providing full and open competition.
- Prohibit the use of time-and-material-type contracts unless a determination is made that no other contract is suitable and provided that the contract include a ceiling price that the contractor exceeds at its own risk.
- Require a cost analysis when adequate price competition is lacking.
- Require profit to be negotiated as a separate element of the price for each contract in which there is no price competition and in all cases where cost analysis is performed.
- Prohibit the use of cost-plus-a-percentage-of-cost method of contracting.

The Co-op did not solicit competitive bids before awarding the five contracts and did not analyze proposed costs or negotiate profit as a separate element of costs. Further, the contracts were time-and-material-type contracts without ceilings; and they contained a cost-plus-a-percentage-of-cost component (see Finding E).

Under 44 CFR 13.43(a)(2), *Remedies for noncompliance*, failure to comply with applicable statutes or regulations can result in the disallowance of all or part of the costs of the activity or action not in compliance. The Co-op did not follow federal procurement regulations; therefore, FEMA had the authority to disallow the \$907,274 claimed for the five contracts. However, except for Finding E, we did not question costs solely based on noncompliance with procurement regulations because the Co-op incurred the costs for eligible work. Further, there is no way to determine how much the costs would have been if the Co-op had provided full and open competition on the five contracts.

Finding B: Ineligible Labor Costs

The Co-op's claim under Project 686 included \$176,080 for force account labor costs not related to the disaster. The Co-op inadvertently claimed all payroll costs posted to its general ledger during the disaster period, including \$176,080 in labor costs and fringe benefits that did not relate to eligible disaster work. According to 44 CFR 206.223(a)(1), to be eligible for financial assistance, an item of work must be required as a result of the major disaster event. Therefore, we questioned \$176,080 claimed for work not related to the disaster.

Finding C: Duplicate Costs

The Co-op claimed \$37,974 for construction (\$36,679) and equipment (\$1,295) costs under Project 986 that were also claimed under Project 686. Therefore, we questioned \$37,974 of duplicate costs.

Finding D: Improperly Categorized Costs

In its claim for Project 986, the Co-op improperly categorized \$68,489 in construction costs as Category A (debris clearance) emergency work. However, the costs should have been categorized as Category F (utilities) permanent work.² For this disaster, FEMA funded emergency work at 100 percent and permanent work at 75 percent. Therefore, we questioned \$17,122, or 25 percent of the \$68,489 improperly categorized as emergency work.

Finding E: Markups on Contract Costs

The Co-op's claim for Projects 986, 2480, 3385, and 3551 included \$15,442 charged by a contractor as a 10 percent markup on costs for lodging and meals. Because there was no evidence additional costs had been incurred, the markups appeared to consist solely of profit. This method of contracting provides a disincentive to reduce costs because the higher the costs, the higher the profit. According to 44 CFR 13.36(f)(4), the cost-plus-a-percentage-of-cost method of contracting shall not be used. Therefore, we questioned \$15,442 in contractor markups.

Finding F: Accounting Error

The Co-op's claim included an \$8,844 credit card cash advance erroneously posted to a disaster expense account. Co-op officials stated that the cash advance should have been posted to its cash account. Therefore, we questioned the \$8,844 posting error.

RECOMMENDATIONS

The Office of Inspector General recommended that the Regional Director:

1. Disallow \$255,462 of questionable costs.
2. Direct the grantee, the Oklahoma Department of Civil Emergency Management, to develop and implement procedures for future disasters to ensure that subgrantees are knowledgeable of and follow federal regulations and FEMA guidelines related to procurement.

² FEMA designates disaster work as either emergency (Categories A and B) or permanent (Categories C through G).

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

On November 19, 2003, we discussed the results of the audit with Co-op officials, who agreed with the findings and recommendations. We discussed the results of the audit with ODCEM on November 19, 2003, and with FEMA on November 24, 2003.

Please advise this office by November 8, 2004, of the actions taken or planned to implement the recommendations, including target completion dates for any planned actions. If you have questions concerning this report, please call me at (940) 891-8900. Major contributors to this report were Stuart Weibel and Rebecca Rodriguez.

Schedule of Projects
Cookson Hills Electric Cooperative, Inc.
FEMA Disaster Number 1355-OK

<u>Project Number</u>	<u>Category Of Work</u>	<u>Amount Claimed</u>	<u>Amount Questioned</u>	<u>Finding Reference</u>
Large				
686	F	\$2,667,912	\$184,924	A, B, F
986	A	616,236	55,124	A, C, D, E
2480	A	1,054,378	8,805	A, E
3385	A	627,478	5,056	A, E
3551	A	<u>209,473</u>	<u>1,553</u>	A, E
Subtotal		<u>\$5,175,477</u>	<u>\$255,462</u>	
Small				
703	B	<u>\$ 26,012</u>	<u>\$ 0</u>	
Total		<u>\$5,201,489</u>	<u>\$ 255,462</u>	