

DEPARTMENT OF HOMELAND SECURITY
Office of Inspector General

City of St. Peter, Minnesota

FEMA Disaster Number 1212-DR-MN



Dallas Field Office
Office of Audits

DD-15-04

August 2004



Homeland Security

August 17, 2004

MEMORANDUM FOR: Edward G. Buikema
Regional Director, FEMA Region V

Tonda L. Hadley

FROM: Tonda L. Hadley, Field Office Director

SUBJECT: *City of St. Peter, Minnesota*
FEMA Disaster Number 1212-DR-MN
Public Assistance Identification Number 103-58036
Audit Report Number DD-15-04

The Office of Inspector General (OIG) audited public assistance funds awarded to the City of St. Peter, Minnesota (City). The objective of the audit was to determine whether the City expended and accounted for Federal Emergency Management Agency (FEMA) funds according to applicable federal regulations and FEMA guidelines.

The City received an award of \$9.9 million from the Minnesota Department of Public Safety, Division of Emergency Management (MN DEM), a FEMA grantee, for damages caused by severe storms and tornadoes on March 29, 1998. The award provided 75 percent FEMA funding for 13 large projects and 30 small projects.¹ The audit covered the period April 1, 1998, to June 7, 2000, during which the City claimed \$9.9 million and MN DEM disbursed \$7.3 million in FEMA funds for direct program costs. We examined the costs for four large projects and three small projects totaling \$9.5 million, representing 97 percent of the total award (see Exhibit).

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 City's accounting records, a judgmental sample of project expenditures, and other auditing procedures considered necessary under the circumstances.

RESULTS OF AUDIT

The City did not follow applicable federal procurement standards in contracting for \$8,931,295 in debris removal work. As a result, fair and open competition did not occur and FEMA had no assurance that contract costs claimed were reasonable. Additionally, the City did not expend and account for FEMA funds in accordance with applicable federal regulations and FEMA guidelines.

¹ Federal regulations in effect at the time of the disaster defined a large project as one costing \$47,100 or more and a small project as one costing less than \$47,100.

Consequently, we questioned \$2,032,333 (\$1,524,250 FEMA share) in claimed costs; consisting of unreasonable costs (\$2,007,411), duplicate benefits (\$14,890), and ineligible labor costs (\$10,032).

Finding A: Unallowable Contract Procedures

The City did not follow applicable federal procurement standards in awarding contracts totaling \$8,931,295 for debris removal on project 93905. As a result, fair and open competition did not occur and FEMA had no assurance that contract costs claimed were reasonable. Federal procurement standards, as set forth in 44 CFR 13.36²:

- Require the performance of procurement transactions in a manner providing full and open competition except under certain circumstances. (13.36(c))
- Require that subgrantees maintain records sufficient to detail the significant history of the procurement, including the rationale for the method of procurement, the basis for contractor selection, and basis for the contract price. (13.36(b)(9))
- Require a cost or price analysis in connection with every procurement action including contract modifications. (13.36(f)(1))
- Prohibit the use of time-and-material type contracts unless no other contract is suitable and the contract includes a ceiling price that the contractor exceeds at its own risk. (13.36(b)(10))
- Require negotiation of profits as a separate element for contracts in which there is no price competition and in all cases where cost analysis is performed. (13.36(f)(2))

The City did not solicit competitive bids or proposals or use written contracts for the \$8,931,295 in claimed costs for this project. They simply paid vendor invoices based on time-and-material charges at rates that were not the result of a written contract. With the exception of one minor contractor, the City had no rate sheets that stipulated an agreed-upon rate per unit of measurement. Further, the contractors' inconsistent method of applying billing rates (i.e., both hourly and per-unit for the same physical unit of debris) and their failure to provide source documents to the City to support these billings made the task of determining actual costs per physical unit infeasible. Additionally, in hindsight, there is no way to determine how much contract costs would have been if the City's procurement had provided full and open competition as required.

The City contended that it received telephone quotes from vendors, but provided no documentary evidence to that effect during the audit.³ The City also contended that it based its choice of vendors on availability and on reasonableness, as determined by billings prior to the disaster. We analyzed the prior billings and found little or no basis for direct comparisons between past billings and the

² Code of Federal Regulations, Title 44--Emergency Management And Assistance Chapter I--Federal Emergency Management Agency, Part 13, Uniform Administrative Requirements For Grants And Cooperative Agreements To State And Local Governments, Section 36, Procurement.

³ Under 44 CFR 13.36(d)(1), *Procurement by small purchase procedures*, telephone quotes are an acceptable form of competition for contracts under \$100,000. However, this exception did not apply in this case because the contracts exceeded that amount.

debris project. Therefore, relative to applicable federal procurement standards cited above, the City failed to perform any of the required actions.

Under 44 CFR 13.43(a)(2), 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. Because the City disregarded applicable federal procurement standards, FEMA had the authority to disallow all \$8,931,295 in claimed costs for this project. However, we did not question costs based solely on noncompliance with procurement standards because the City incurred the majority of costs for eligible work. Nevertheless, we determined that the contract costs claimed were unreasonable and questioned \$2,007,411 in Finding B.

Finding B: Unreasonable Costs

Under Project 93905, the City claimed debris removal costs of \$9,024,426, of which \$8,931,295 was for contract costs to remove 124,165 cubic yards plus 27,611 tons of debris. We determined that \$2,007,411 of the contract costs (as shown on the next page) was unreasonable. The Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, Attachment A, paragraph C.1.a., requires that allowable costs under federal awards be both necessary and reasonable. Therefore, we solicited assistance from FEMA Region V to determine reasonable costs for debris removal during this disaster. The Region analyzed debris removal costs claimed by nearby communities for the same disaster and determined that costs ranged from \$20 to \$25 per cubic yard for debris removal and \$15 to \$20 per cubic yard for landfill tipping fees. The Region also advised that, based on FEMA's standard conversion ratio, the estimated cost per ton would range from \$40 to \$50 per ton.

OMB Circular A-87, Attachment A, paragraph C.2., defines a reasonable cost as one that, in nature and amount, does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. The Circular also directs consideration of the following items in determining the reasonableness of a given cost:

- Use of sound business practices; arms length bargaining; federal, state, and other laws and regulations; and terms and conditions of the federal award.
- Market prices for comparable goods or services.
- Whether the individuals acted with prudence.

Based on Finding A and FEMA Region V's cost determination, costs were unreasonable because by not following 44 CFR 13.36, the City also did not follow sound business practices (i.e., competitively bid the work, include a cost ceiling in the contract, perform a cost analysis, and comply with applicable federal standards).

The \$8,931,295 contract costs claimed for debris removal exceeded the OIG's calculation of reasonable costs by \$2,007,411 (see table below). Accordingly, we questioned \$2,007,411 as unreasonable. We calculated reasonable costs of \$6,923,884 by applying the lesser of the actual costs or the high end of the cost range specified by Region V for debris removal and tipping fees and allowing actual costs for long distance (LD) hauling and backhauling when appropriate.

Disposal Site	*Debris (CuYds)	*Debris (Tons)	Debris Per Unit Cost (\$)	LD Haul Cost (\$)	Tipping Fees (\$)	Backhaul Costs (\$)	Total Per Unit Cost (\$)	Reasonable Costs
SMC	108,067		25.00		**11.00		36.00	\$3,890,412
Spruce Ridge		26,104	50.00	**5.90	**39.66		95.56	2,494,498
Timberline		1,435	50.00		40.00		90.00	129,150
Johnson Aggregates	16,098		25.00				25.00	402,450
Lesueur Transfer Facility		72				**102.41	102.41	7,374
TOTALS	124,165	27,611						\$6,923,884

*Actual quantities of debris provided by the City and verified by OIG.

**Actual costs per invoices provided by the City.

Finding C: Duplicate Benefits

The City's claim under project 27754 included \$14,890 in costs for the replacement of damaged restrooms at Gorman Park, a city park facility. As evidenced by a "Statement of Loss" worksheet, these damages were fully covered by insurance and the City was reimbursed for the costs to repair the damage. Section 312 of the Stafford Act, *Duplication of Benefits* (42 U.S.C. § 5155), prohibits any person, business concern, or other entity from receiving assistance that duplicates benefits available for the same purpose from any other source. Therefore, FEMA funding of this work constituted a duplication of benefits and the OIG questioned \$14,890.

Finding D: Ineligible Labor Costs

The City's claim under Projects 93905 and 93906 included \$10,032 (\$8,917 labor plus \$1,115 associated fringe benefits) for bonuses paid to salaried, administrative personnel. According to OMB Circular A-87, Attachment B, paragraph 11.a(1), compensation for employees must conform to the governmental unit's established policies and be applied consistently to federal and non-federal activities. The City Council approved the bonuses, but the City provided no evidence that its standard practice was to award bonuses to salaried personnel.

Additionally, the job titles of the personnel at issue (such as City Administrator and Finance Director) indicate their function was administrative in nature and, therefore, covered by the subgrantee's statutory administrative allowance. According to 44 CFR 206.228(a)(2)(ii), subgrantees receive an administrative allowance to cover the "necessary costs of requesting, obtaining, and administering Federal disaster assistance subgrants." Therefore, we questioned the \$10,032 because the bonuses did not conform to the City's established policies and duplicated costs covered by the statutory administrative allowance.

RECOMMENDATIONS

The Office of Inspector General recommended that the Regional Director:

1. Disallow \$2,032,333 of questionable costs.

2. Require the Minnesota Department of Public Safety, Division of Emergency Management, to develop and implement procedures to ensure that, for all future disasters, subgrantees follow applicable federal regulations and Federal Emergency Management Agency guidelines related to procurement.

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

We discussed the results of the audit with officials from FEMA, MN DEM, and the City on November 5, 2003. City officials disagreed with the findings and recommendations, but deferred comment until later.

Please advise this office by November 15, 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 contact me at (940) 891-8900. Major contributors to this report were Daniel Benbow, DeAnna Fox, and William Lough.

Schedule of Audited Projects
City of St. Peter, Minnesota
FEMA Disaster Number 1212-DR-MN

<u>Project Number</u>	<u>Category</u>	<u>Amount Claimed</u>	<u>Amount Questioned</u>	<u>Finding Reference</u>
Large				
93905	A	\$9,024,426	\$2,008,827	A,B,D
93906	B	243,458	8,616	D
93918	C	70,104	0	
93998	C	<u>135,356</u>	<u>0</u>	
Large Subtotal		\$9,473,344	\$2,017,443	
Small				
27754	G	\$ 22,335	\$ 14,890	C
93916	G	4,191	0	
93992	G	<u>30,208</u>	<u>0</u>	
Small Subtotal		\$ 56,734	\$ 14,890	
TOTAL		<u>\$9,530,078</u>	<u>\$2,032,333</u>	