



# DEPARTMENT OF HOMELAND SECURITY

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January 16, 2004

## MEMORANDUM

TO: Jeff Griffin  
Regional Director  
FEMA Region IX

*Robert J. Lastrico*

FROM: Robert J. Lastrico  
Field Office Director

SUBJECT: Newhall County Water District  
Santa Clarita, California  
Public Assistance Identification Number 037-91125  
FEMA Disaster Number 1008-DR-CA  
Audit Report Number DS-05-04

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The Office of Inspector General (OIG) audited public assistance funds awarded to the Newhall County Water District, Santa Clarita, California (District). The objective of the audit was to determine whether the District expended and accounted for Federal Emergency Management Agency (FEMA) funds according to federal regulations and FEMA guidelines.

The District received an award of \$4.3 million from the California Office of Emergency Services (OES), a FEMA grantee, for emergency repairs and replacement of water tanks damaged as a result of the Northridge earthquake in January 1994. The award provided 90 percent FEMA funding for 17 small projects and 14 large projects.<sup>1</sup> The audit covered the period January 17, 1994, to November 27, 2000, and included the review of three small projects and seven large projects with a total award of \$3.1 million (see Exhibit).

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<sup>1</sup> Federal regulations in effect at the time of the disaster set the large project threshold at \$42,400.

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The OIG 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 a review of FEMA, OES, and District records, a judgmental sample of project expenditures, and other auditing procedures considered necessary under the circumstances.

## RESULTS OF AUDIT

The District had sufficient documentation to support accomplishment of the work for the three small projects reviewed. However, the District's claim for four large projects contained \$1.9 million in questionable costs (FEMA's share \$1.7 million) that related to the replacement of three water storage tanks and the construction of a new tank that was non-existent before the disaster. Projects 82247, 82410, 82490, and 82280 provided funding for the repair or replacement of Tanks 2, 3, 4, and 5 respectively. Contrary to federal regulations, Tanks 2, 3, and 4 were replaced with tanks of a greater capacity. While Tank 5 was repaired to pre-disaster condition, a new tank (Tank 9) was constructed under the same project (project 82280) to provide the District with additional water storage capacity.

*Tank 9 on the left has a capacity of 1,428,000 gallons, and Tank 5 on the right has a capacity of 750,000 gallons.*



DHS OIG photograph

Section 406 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act (Stafford Act) authorizes federal assistance for repair, restoration, reconstruction, or replacement of certain public and private nonprofit facilities damaged or destroyed by a major disaster (Public Assistance). Title 44 of the Code of Federal Regulations, Section 206.226<sup>2</sup> (44 CFR 206.226) allows federal assistance “. . . to restore eligible facilities on the basis of the design of such facilities as they existed immediately prior to the disaster . . .” This section, among other things, provides: (1) that eligible work can include upgrades (based on building codes and standards) that change the pre-disaster construction of the facility as long as the upgrades are appropriate to the pre-disaster use of the facility; and (2)

<sup>2</sup> Unless otherwise noted, the October 1993 version of the Code of Federal Regulations is referenced here and throughout the remainder of this report.

that those building codes and standards be uniformly applied and enforced during the time they are in effect.

On March 2, 1994, FEMA and OES executed a Memorandum of Understanding (MOU) specific to the Northridge earthquake. One key provision of the MOU was that when the estimated cost of structural repair work did not exceed 10 percent of the replacement cost of the facility, the damaged portion(s) should be restored to its/their pre-disaster condition. The OIG noted that for Tanks 2, 3, and 4, the estimated costs of repair exceeded the replacement cost (based on actual contractor bid schedules) for each tank. Therefore, replacement of these tanks to their pre-disaster condition was appropriate. However, as noted in the table below, the District replaced Tanks 2, 3, and 4 with tanks whose capacities far exceeded the capacity at the time of the disaster. In addition, while Tank 5 was repaired to its pre-disaster condition because the estimated cost of structural repair work did not exceed 10 percent of the replacement cost, the District built, and FEMA paid for the construction of Tank 9 to provide additional storage capacity required by the District as a result of population growth.

Project	Tank No.	Capacity*		Difference
		Pre-Disaster	Post-Disaster	
82247	2	300	635	335
82410	3	300	593	293
82490	4	300	635	335
82280	5	750	750	0
82280 <sup>3</sup>	9	0	1,428	1,428

\* Thousands of gallons

The District's replacement of the three water tanks with those of greater capacity increased project costs by \$415,944 over the estimated costs to bring the tanks to their pre-disaster condition and capacity. In addition, constructing Tank 9 added \$1,519,287 to project costs.

Project	Tank No.	Estimated	Actual	Excess Costs
		Replacement Costs	Replacement Costs	
82247	2	\$216,000	\$ 339,482	\$ 123,482
82410	3	211,000	345,498	134,498
82490	4	<u>211,000</u>	<u>368,964</u>	<u>157,964</u>
	Subtotal	\$638,000	\$1,053,944	\$ 415,944
82280	9	<u>0</u>	<u>1,519,287</u>	<u>1,519,287</u>
	Total	<u>\$638,000</u>	<u>\$2,573,231</u>	<u>\$1,935,231</u>

<sup>3</sup> Damage Survey Report (DSR) 82280 was the master DSR supplemented by DSR 21681 (repair of Tank 5), DSR 78313 (construction of Tank 9) and DSR 98493 (large project closeout).

Regarding Tank 9, the District claimed that the repairs to Tank 5 were temporary and therefore, new construction was appropriate. However, project documents showed that as early as February 1991, nearly 3 years prior to the disaster, the District planned to build the new tank to satisfy current (1991) reserve and fire flow requirements, but delayed construction due to a lack of funds. Further, Tank 5, with a pre-disaster capacity of 750,000 gallons, was repaired with FEMA funding of \$32,094. Project documentation prepared after completion of the work noted that the tank had been repaired to pre-disaster condition and that there was no need for replacement. Because Tank 5 remained, and still remains, in operation, the construction of Tank 9 was ineligible work funded by FEMA.

The MOU between FEMA and OES also addressed the DSR process and the use of “triggers” for the application of current building codes and standards. The MOU specified that the only applicable standard for repair or replacement of eligible facilities was the 1991 or 1994 Uniform Building Code depending on what version of the Code was in force at the time plans were submitted to the Building Official for review. The codes and standards cited by the District as relevant to its water storage requirements (daily use, reserve, and fire flow requirements) were not addressed in the Uniform Building Code. Nonetheless, the District claimed that replacing the four tanks would bring the District in compliance with the usage, reserve, and fire flow requirements. However, review of project records showed that this did not occur and that the District remained in violation of the requirements for the areas served by the four tanks and for other tanks operated by the District even after disaster repairs and tank replacements had been completed.

- Tanks 2 and 5 provided storage for the base zone of the Newhall System, with a required storage capacity of 7.3 million gallons to meet daily use, reserve, and fire flow requirements. However, after tanks 2 and 9 were constructed (tank 5 continued in operation), the system had a capacity of 2.8 million gallons. Accordingly, the District remained deficient by 4.5 million gallons (7.3 million - 2.8 million).
- Tanks 3 and 4 remained deficient by 247,000 gallons and 715,000 gallons, respectively.
- Tanks 6 and 8 were replaced by FEMA to pre-disaster capacity, but still were not in compliance with use, reserve, and fire flow requirements by at least 238,750 and 200,000 gallons, respectively.

Thus, the District had not uniformly applied and enforced the daily use, reserve, and fire flow requirements that it used to justify replacement of its tanks.

During project execution, FEMA denied increased funding for the additional storage capacity requested by the District on the grounds that it represented improvements beyond those required to restore the tanks to their pre-disaster condition/capacity. On August 17, 1995, the District appealed the determination arguing that larger tanks were needed to meet capacity

guidelines of the California Department of Health Services and Los Angeles County Fire Department for storage and fire flow requirements. The OES letter transmitting the District's appeal also noted that eligible work included work to restore eligible facilities in conformance with current and applicable codes and standards. On January 19, 1996, FEMA denied the District's 1<sup>st</sup> appeal on the basis that the additional storage capacity was triggered by population growth and the regulations only allow restoration of facilities to their pre-disaster condition/capacity.

On April 2, 1996, the District submitted a 2<sup>nd</sup> appeal to OES. In addition to citing reserve and fire flow requirements, the District noted that the tank replacements met the conditions of the Stafford Act for hazard mitigation. Although this appeal was forwarded by the District to OES, there was no record that OES forwarded the appeal to FEMA.<sup>4</sup> Therefore, there was no 2<sup>nd</sup> appeal before FEMA.

On July 29, 1996, FEMA reversed its 1<sup>st</sup> appeal decision and approved the increased costs without citing statutory or regulatory provisions to justify the award. Discussions with both FEMA Headquarters and Regional officials<sup>5</sup> indicated that it was not uncommon for a Region to "re-consider" and reverse a 1<sup>st</sup> appeal decision based on compelling additional information provided by the subgrantee. However, the Code of Federal Regulations does not give FEMA regional offices the authority to reconsider earlier 1<sup>st</sup> appeal decisions. Further, FEMA's re-evaluation of project eligibility neither discussed the applicability or relevance of capacity standards for the tanks replaced or constructed after the disaster, nor did FEMA substantiate the eligibility of the work as a hazard mitigation effort authorized under Section 404 (Hazard Mitigation Grant Program) or Section 406 (Public Assistance funding of mitigation measures for damaged public facilities). In fact, no hazard mitigation proposal was suggested or offered by OES or by FEMA.

The records available from FEMA, OES, and the District provided insufficient support to justify increasing the capacity of Tanks 2, 3, and 4 or for constructing Tank 9 since it did not even exist prior to the disaster. The OIG concurs with FEMA's 1<sup>st</sup> appeal determination that the added costs for replacing tanks with greater capacities than existed before the disaster (including construction of Tank 9) was triggered by population growth and therefore not eligible for funding above the original damage estimate. Since there was no 2<sup>nd</sup> appeal before FEMA and the Region had no authority (based on the Code of Federal Regulations) to reverse its 1<sup>st</sup> appeal determination, the projects should have been viewed as improved projects with funding limited to the costs of restoring the District's water storage capacity to the pre-disaster level. The following paragraphs discuss improved projects and the related environmental review requirements as they pertain to the work accomplished by the District.

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<sup>4</sup> 44 CFR 206.206(d)(1) [October 1995] states that if the Regional Director denies the first appeal, the subgrantee may submit a second appeal to FEMA Headquarters. Such appeals were to be made in writing through grantee and the Regional Director.

<sup>5</sup> See DHS OIG Audit Report DO-18-03 issued August 15, 2003.

- According to 44 CFR 206.203(d)(1), if a subgrantee desires to make improvements, but still restore the pre-disaster function of a damaged facility, the grantee's approval must be obtained and federal funding will be limited to the federal share of the approved estimate of eligible costs. The approval of Tanks 2, 3, and 4 as improved projects would have been consistent with the regulations but, neither FEMA nor OES had any documentation indicating that the District requested that these projects be approved as improved projects (Tank 9 was a new construction project and therefore was not eligible for FEMA funding under any circumstance).
- Because the work performed by the District restored (or provided) facilities substantially beyond that which existed prior to the disaster, it was FEMA's responsibility under the National Environmental Policy Act (NEPA) to ensure that environmental reviews were performed. The criteria for categorically excluding disaster recovery efforts from detailed NEPA environmental review requirements were delineated in 44 CFR 10.8(c) [October 1993]. However, the "unapproved" improved projects performed by the District were not covered by the regulations and therefore, could not be categorically excluded. In fact, FEMA Environmental Memorandum #3 of May 3, 1996, clarified federal regulations and stated that facilities restored to their pre-disaster condition do not require NEPA documentation, implying that projects that go beyond that do require NEPA documentation. Further, that memorandum stated that it is FEMA's policy that actions initiated and/or completed without fulfilling the specific documentation and procedural requirements of NEPA may not be considered for funding.
- On October 28, 1997, FEMA's Executive Associate Director, Response and Recovery Directorate, issued a memorandum to the Regional Directors addressing unapproved improved projects. That memorandum discussed situations in which subgrantees perform work well beyond approved scopes of work and make substantial improvements without obtaining grantee and FEMA approval. By doing so, the subgrantees deny FEMA the opportunity to comply with NEPA. The Executive Associate Director requested that regional public assistance officials notify subgrantees that they must receive approval from the grantees prior to initiating improved projects. Further, approval by the grantees is contingent upon notifying FEMA and obtaining NEPA clearance in order to prevent possible deobligation of all project funding.
- On July 23, 1997, OES forwarded the District's June 4, 1997 request for the status of environmental reviews required for the District's projects. OES asked that FEMA expeditiously provide the status for all outstanding reviews. On July 29, 1998, a FEMA Environmental Officer essentially waived NEPA requirements and recommended that the District be allowed to retain all project funding "... because of a lapse of communication or process on the part of FEMA ..." The Environmental Officer's Special Consideration of Completed Projects Not Meeting Environmental Policy Memorandum #3 indicated that there was a disagreement between OES and FEMA as to whether or not the

District's projects could be categorically excluded from detailed environmental reviews but this disagreement was never communicated to the District. The District proceeded with construction believing that action had been taken to categorically exclude the projects from the reviews. The Environmental Officer indicated that the District was later told that there could be an environmental review problem although the OIG found no documentation to confirm this statement from the Environmental Officer.

- The Environmental Officer's documentation of special NEPA consideration for the District's projects identified steps taken to ensure that similar procedural failures did not occur. Among other things, the Environmental Officer indicated that proper processes were initiated to inform subgrantees of their NEPA responsibilities and a July 23, 1998 internal memorandum was issued defining the requirement for all improved or alternative projects to receive environmental reviews. The Environmental Officer's comments recognize the District projects as improved projects. Further, the then current version of the Code of Federal Regulations, the May 1996 Environmental Policy Memorandum #3, and the October 1997 memorandum on unapproved improved projects provided more than sufficient regulatory and policy guidance on the treatment of and funding for improved projects. The regulatory and policy guidance available to FEMA, at minimum, allowed FEMA to limit funding to the federal share of the approved estimate of eligible costs, and at a maximum, allowed FEMA to deny all funding since NEPA requirements were never met. The OIG did not find, and FEMA did not provide any other authority that would allow FEMA to act in a manner other than that prescribed in regulation and in its own policy. Based on the foregoing, the OIG asserts that the Environmental Officer did not have the authority to waive NEPA requirements or make funding decisions as related to NEPA compliance.

The OIG has several concerns regarding the award of FEMA funding for the replacement of Tanks 2, 3, and 4 with tanks of greater capacity and the construction of Tank 9:

1. In December 1994, FEMA and OES agreed that the District's request for increased capacities should be approved but specific tanks and sites were not mentioned. In February 1995, FEMA notified OES and the District that FEMA's responsibility was to fund repair or replacement of damaged structures to current building codes and standards applicable to the structures and not on the basis of storage capacities. Nonetheless, FEMA and OES allowed the District to proceed with construction and re-construction although the question of codes and standards upgrades had not been resolved.
2. In August 1995, the District appealed FEMA's February 1995 decision to limit funding. Although the 1<sup>st</sup> appeal was denied in January 1996, FEMA reversed its 1<sup>st</sup> appeal decision in July 1996 without regulatory authority to do so.

3. FEMA funded permanent repairs to Tank 5 while at the same time funding Tank 9 as a replacement to Tank 5 (Tank 9 had nearly twice the storage capacity of Tank 5 and was planned by the District for construction as early as 1991).
4. FEMA did not ensure that environmental reviews under NEPA were performed consistent with 44 CFR 10.8. Further, and more importantly, FEMA did not have the authority to waive NEPA requirements or allow the District to retain all project funding. While recognizing District projects as upgrades and improvements, the Headquarters Environmental Officer failed to consider the improved project funding option specified in 44 CFR 206.203(d)(1) or the Headquarters Response and Recovery Directorate policy statement on unapproved improved projects. Further, because the District's projects could not be statutorily or categorically excluded from NEPA requirements, the Environmental Officer, in consultation with the Regional Director and the President's Council on Environmental Quality should have determined if District actions completed prior to NEPA review had actual significant impact not previously mitigated and whether or not those impacts can be mitigated.<sup>6</sup>
5. OIG review of documentation at FEMA, OES, and the District appears to support an argument that the increased capacity was required to meet various State and local reserve and fire flow requirements. However, the OIG does not concur with this argument since the District remained in violation of reserve and fire flow standards after construction was completed.

As a result of these concerns, the OIG questions the excess costs over the FEMA approved estimates associated with replacing Tanks 2, 3, and 4 (\$415,944), and the total cost of constructing Tank 9 (\$1,519,287).

## RECOMMENDATIONS

The OIG recommends that the Regional Director, FEMA Region IX, in coordination with OES, disallow \$1,935,231 of questionable costs.

The OIG also recommends that the Environmental Officer, in consultation with the Regional Director and the President's Council on Environmental Quality determine if District actions completed prior to NEPA review had actual significant impact not previously mitigated and whether or not those impacts can be mitigated in accordance with Environmental Policy Memorandum #3.

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<sup>6</sup> See Environmental Policy Memorandum # 3.

## DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

The OIG discussed the results of this audit with the District and OES officials on October 16, 2003. Those officials did not agree with the finding and recommendation. The OIG also notified FEMA Region IX officials of the audit results on October 17, 2003.

Please advise this office by March 16, 2004, of the actions taken to implement the recommendation in this report. Should you have any questions concerning this report, please contact me at (510) 627-7011. Key contributors to this assignment were Humberto Melara and Renee Brescia.

Schedule of Audited Projects  
 Newhall County Water District  
 Santa Clarita, California  
 Public Assistance Identification Number 037-91125  
 FEMA Disaster Number 1008-DR-CA

Project Number	Amount Awarded	Questioned Costs
<u>Large projects</u>		
82247	\$ 339,482	\$ 123,482
82410	345,498	134,498
82490	368,964	157,964
37109	196,339	0
21684	58,365	0
73319	138,117	0
82280	<u>1,551,381</u>	<u>1,519,287</u>
Subtotal	\$2,998,146	\$1,935,231
<u>Small projects</u>		
44323	\$ 31,427	\$ 0
05788	40,549	0
73322	<u>30,375</u>	<u>0</u>
Subtotal	\$ 102,351	\$ 0
Totals	<u>\$3,100,497</u>	<u>\$1,935,231</u>