

# FEMA Should Recover \$4.2 Million of \$142.1 Million in Grant Funds Awarded to the City of Gulfport, Mississippi, for Hurricane Katrina Damages





# DHS OIG HIGHLIGHTS

## *FEMA Should Recover \$4.2 Million of \$142.1 Million in Grant Funds Awarded to the City of Gulfport, Mississippi, for Hurricane Katrina Damages*

September 15, 2015

### Why We Did This

The City received a \$248.3 million grant for 2005 Hurricane Katrina damages. In this third audit of the grant, we reviewed \$142.1 million FEMA approved for 43 permanent repair projects. At the time of our audit, the City had not completed work on all projects and, therefore, had not submitted a final claim for all project expenditures.

### What We Recommend

FEMA should disallow \$4.2 million of unreasonable contract costs and inform Mississippi of its grant management responsibilities.

#### For Further Information:

Contact our Office of Public Affairs at (202) 254-4100, or email us at [DHS-OIG.OfficePublicAffairs@oig.dhs.gov](mailto:DHS-OIG.OfficePublicAffairs@oig.dhs.gov)

### What We Found

For most of the projects in our audit scope, the City of Gulfport, Mississippi, (City) accounted for and expended Federal Emergency Management Agency (FEMA) funds according to Federal regulations and FEMA guidelines. However, the City did not comply with Federal procurement requirements when awarding two contracts for project management services valued at \$10.4 million, of which \$4.2 million was unreasonable.

City officials were not aware that Federal procurement regulations prohibited the use of a qualifications-based contracting method for program management services. However, the grantee (Mississippi) is responsible for ensuring that its subgrantee (the City) is aware of and complies with Federal requirements, as well as for providing technical assistance and monitoring grant activities.

### FEMA Response

FEMA's written response is due within 90 days.

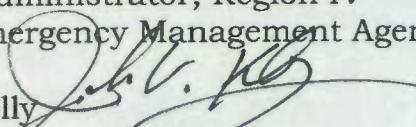


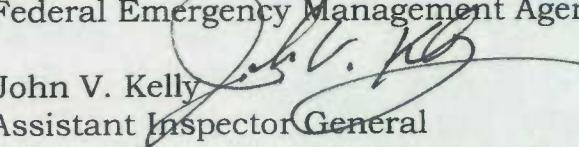
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Department of Homeland Security

Washington, DC 20528 / [www.oig.dhs.gov](http://www.oig.dhs.gov)

SEP 15 2015

MEMORANDUM FOR: Gracia Szczech  
Regional Administrator, Region IV  
Federal Emergency Management Agency  
  
John V. Kelly  
Assistant Inspector General  
Office of Emergency Management Oversight

FROM: 

SUBJECT: *FEMA Should Recover \$4.2 Million of \$142.1 Million in Grant Funds Awarded to the City of Gulfport, Mississippi, for Hurricane Katrina Damages*  
Audit Report Number OIG-15-148-D

We audited Federal Emergency Management Agency (FEMA) Public Assistance grant funds awarded to the City of Gulfport, Mississippi, (City) for Hurricane Katrina damages. In this third audit of the City's grant, we reviewed 43 projects (see appendix B, table 2) totaling \$142.1 million (see appendix A, table 1) for permanent repair projects, or about 57 percent of the \$248.3 million the City received from the Mississippi Emergency Management Agency (Mississippi), a FEMA grantee.<sup>1</sup> The award provided 100 percent FEMA funding. At the time of our audit, the City had not completed work on all projects and, therefore, had not submitted a final claim to Mississippi for all project expenditures.

### Background

On August 29, 2005, Hurricane Katrina struck the City of Gulfport, Mississippi, as a Category 4 hurricane inundating it with salt water from a 28- to 35-foot storm surge from the Gulf of Mexico. The City suffered major damages to piers, buildings, and other facilities, with its water distribution, sewer collection, and storm drainage systems taking a significant hit.

The City owns and maintains the potable water system, sanitary sewer system, and, except for a portion located under or south of U.S. Highway 90 (responsibility of the Mississippi Department of Transportation), the drainage system (referred to as the City's "infrastructure system"). The storm heavily damaged much of this system south of the CSX railroad tracks. FEMA cited an

<sup>1</sup> The first two audits resulted in Audit Report DA-07-02: *Review of Hurricane Katrina Activities, City of Gulfport, Mississippi*, October 19, 2006, and; Audit Report DA-13-10: *FEMA Should Recover \$8.5 Million of Public Assistance Grant Funds Awarded to the City of Gulfport, Mississippi, for Debris Removal and Emergency Protective Measures – Hurricane Katrina*, February 22, 2013.



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Environmental Protection Agency review that identified the necessary replacement of (1) 132,200 linear feet of potable water line, (2) 81,000 linear feet of wastewater line, and (3) 40,900 linear feet of storm water line. As of the start of our audit, the City had claimed \$68.4 million, or about 80 percent of the \$85.4 million FEMA awarded for the four infrastructure system projects.

Hurricane Katrina's storm surge also damaged the four bulkheads and six piers of the City's small craft harbor. Also, the storm blew the City's Uriel Point Lighthouse, a 40-foot metal structure located at the small craft harbor, and Uriel Fishing Pier dedication stone off of their foundations. The storm also lifted and carried the U.S. Merchant Marine Memorial stone into the harbor. As of the start of our audit, the City had completed work on these two projects (small craft harbor and lighthouse/stones) and submitted a final claim of \$20.4 million to Mississippi for project expenditures.

### **Results of Audit**

For most of the projects in our audit scope, the City generally accounted for FEMA funds properly and complied with Federal regulations. However, the City did not comply with Federal procurement standards in awarding two contracts for project management services totaling \$10.4 million. While we do not question the entire contract amounts, we do question \$4.2 million of the \$10.4 million as unreasonable.

These issues occurred primarily because the City misinterpreted Federal procurement requirements. However, the grantee (Mississippi) is responsible for ensuring that its subgrantee (the City) is aware of and complies with these requirements, as well as for providing technical assistance and monitoring grant activities. Therefore; FEMA should also (1) direct Mississippi to inform the City of its requirement to comply with Federal procurement regulations and FEMA guidelines when acquiring goods and services under the FEMA award and (2) inform Mississippi of its grant management responsibilities for ensuring subgrantees follow Federal procurement regulations.

### **Finding A: Contracting Procedures**

The City awarded 25 contracts totaling \$88,777,083 for the 6 projects we reviewed as part of our full audit scope. The City generally followed Federal procurement standards in awarding 23 of the 25 contracts. However, the City awarded two project management contracts totaling \$10,399,059 improperly because the City based its selection on the contractors' qualifications without considering price. These two contracts included \$4,202,857 of unreasonable project management costs.

Federal procurement standards at 44 Code of Federal Regulations (CFR) 13.36, in part, require the City, among other actions, to—



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- conduct all procurement transactions in a manner providing full and open competition (44 CFR 13.36(c)); and
- use competitive proposals for procurement when conditions are not appropriate for sealed bids and make awards to the responsible firm whose proposal is most advantageous to the program, with price and other factors considered (44 CFR 13.36(d)(3)(iv)).

In addition, subgrantees “may use competitive proposal procedures for qualifications-based procurement of architectural/engineering (A/E) professional services whereby competitors’ qualifications are evaluated and the most qualified competitor is selected, subject to negotiation of fair and reasonable compensation.” However, subgrantees cannot use this method, where price is not used as a selection factor, to procure other types of services, even when an A/E firm performs the other services (44 CFR 13.36(d)(3)(v)).

FEMA may grant exceptions to Federal procurement requirements to subgrantees on a case-by-case basis (44 CFR 13.6(c)). In addition, according to Federal cost principles (*Cost Principles for State, Local and Indian Tribal Governments* at 2 CFR 225, Appendix A, Section C.2), costs must be necessary and reasonable for efficient and reasonable performance and administration of the grant to be eligible under a Federal award.

### Contract for Management of Infrastructure Project

The City did not comply with all Federal procurement regulations when it awarded an \$8,248,864 contract to manage water, sewer, and drainage infrastructure projects ultimately valued at \$88,937,734. We determined that \$3,801,977 of the \$8,248,864 project management contract was unreasonable.

Federal procurement standards prohibit using qualifications-based procurements, where price is not an evaluation factor, for non-A/E professional services such as project management. FEMA *Public Assistance Guide* (FEMA 322, October 1999, p. 75) defines A/E work as preliminary engineering analysis, preliminary design, final design, and construction inspection. However, in May 2007, the City used competitive proposal procedures based solely on qualifications to award contract work for project management activities for an infrastructure project initially valued at \$78,336,716. Upon evaluating the proposals the City received from its solicitation, the City selected a construction firm that it believed was best qualified for the work. The City then negotiated an initial contract price with a not-to-exceed amount of \$4,000,000. This amount represented 5.1 percent (\$4,000,000 divided by \$78,336,716) of construction costs. However, change orders increased the construction work from \$78,336,716 to \$88,937,734 (13.5 percent), while the



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Department of Homeland Security

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project management contract ultimately increased from \$4,000,000 to \$8,248,864, an increase of 106.2 percent.

*FEMA Cost Estimating Format (CEF) Instructional Guide for Large Projects*, 11.1(H)(1) and 11.3 (H)(3), allows a total of 4 percent of construction costs for management of the project design (1 percent) and construction phase (3 percent) for construction projects greater than \$5 million. Further, FEMA representatives told us that the agency also typically allows 1 percent of construction costs for a resident project representative for large construction projects.

Using these FEMA cost guidelines for construction services, we concluded that 5 percent of construction costs or \$4,446,887 (\$88,937,734 total construction costs times 5 percent) is fair and reasonable compensation for project management services the firm provided.<sup>2</sup> However, the contract in question, with change orders, totaled \$8,248,864, or 9.3 percent of construction costs—almost twice the amount that FEMA considers reasonable compensation for project management services.

It has been FEMA's practice not to disallow contracting costs based solely on a subgrantee's noncompliance with Federal contracting requirements. FEMA usually determines whether the contracting costs were reasonable under the circumstances, and allows only reasonable costs. Therefore, we are not questioning the entire \$8,248,864 of contract costs for project management activities on the basis of the City's noncompliance with Federal contracting requirements. Instead, we reviewed the contract costs for reasonableness using FEMA construction cost guidelines and question \$3,801,977 of the costs as unreasonable.

City officials were not aware that Federal procurement regulations prohibited the use of a qualifications-based contracting method for non-A/E services. They also said that, while they were aware of the FEMA cost guidelines for project management, during the course of the contract, their focus shifted from the 5 percent guideline to the services required to finish the project.

The City did not concur with our finding. It believes it followed proper procurement regulations and stated that it chose the only two firms that responded to its request for proposals for project management services; one for the infrastructure project and the other for the project management contract for the harbor, lighthouse, and other projects discussed below. The City asserts that the small number of respondents limited its ability to control costs.

City officials also said that multiple agencies at both the State and Federal levels were involved in these projects, which required significant time and



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Department of Homeland Security

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resources on the part of its program manager. They also said that delays by some of these entities and instances of litigation increased program management costs. Finally, the City asserted that its program manager performed duties well beyond the norm, such as overseeing the bidding process for multiple contracts, preparing bid tabulations, reviewing change orders, and coordinating inspections.

We disagree with the City's comments. The City did not follow Federal procurement procedures when it selected the contractor based solely on its qualifications. The initial program management contract price with a not-to-exceed amount of \$4,000,000, which was 5.1 percent of construction costs, was very close to the FEMA cost guidelines for construction services at 5 percent. However, the City did not control program management costs in relation to construction costs, allowing it to almost double to 9.3 percent. All of the duties the City asserts that the program manager performed are normal program management duties; therefore, the 5 percent fee we used in our calculation covers these types of duties. Therefore, our position remains unchanged.

### Contract for Management of Harbor, Lighthouse, and Other Projects

Similar to the finding explained above, in May 2007, the City used competitive proposal procedures based solely on qualifications to award contract work for project management activities for harbor, lighthouse, buildings, and other projects (total of 37 projects) valued at \$34,986,291 (total project cost \$37,136,486 minus project management cost \$2,150,195). Upon selecting a firm it believed was best qualified for the work, the City negotiated a price for the work and paid the firm \$2,150,195 for its services, or approximately 6.1 percent of construction costs.

Again, initially we selected two projects for our audit scope concerning the harbor and lighthouse, but during our review we determined the City's noncompliance with Federal procurement regulations affected additional projects. Therefore, to capture the total costs, we expanded our audit scope to include 35 additional projects that the improper procurement affected. As a result, we question the unreasonable cost of program management services for all 37 projects, totaling \$400,880.

Using FEMA cost guidelines for construction services, we concluded that 5.0 percent of construction costs or \$1,749,315 (\$34,986,291 total construction costs times 5.0 percent) is fair and reasonable compensation for project management services the firm provided. Therefore, we question \$400,880, which is the difference between project management costs the City claimed at 6.1 percent of construction costs and the 5.0 percent that we calculated as reasonable (\$2,150,195 less \$1,749,315).



## OFFICE OF INSPECTOR GENERAL

Department of Homeland Security

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The City did not concur with this finding. Again, City officials were not aware that Federal procurement regulations prohibited the use of a qualifications-based contracting method for non-A/E services. The City essentially asserted most of the same reasons for its disagreement here as it did previously relative to its infrastructure project management.

Again, we disagree with the City's comments. The City did not follow Federal procurement procedures when it procured non-A/E work based solely on qualifications.

### Finding B: Grant Management

Mississippi did not fulfill its grantee responsibility to ensure the City followed applicable Federal procurement regulations. The nature and extent of ineligible costs we identified demonstrate that Mississippi should have more thoroughly reviewed the City's contracting methods. Federal regulations require grantees to (1) ensure that subgrantees are aware of Federal regulations, (2) manage the operations of subgrant activity, and (3) monitor subgrant activity to ensure compliance.<sup>3</sup> Therefore, we recommend that FEMA inform Mississippi of its grant management responsibilities for ensuring subgrtees follow Federal procurement regulations.

FEMA and Mississippi officials withheld comments pending receipt of our final report.

### Recommendations

We recommend that the Regional Administrator, FEMA Region IV:

**Recommendation 1:** Disallow \$4,202,857 of ineligible, unreasonable contract costs for project management that the City did not procure in accordance with Federal requirements, unless FEMA decides to grant an exception for all or part of the costs as 44 CFR 13.6(c) allows and determines that the costs are reasonable (finding A).

**Recommendation 2:** Direct Mississippi to inform the City of its requirement to comply with Federal procurement regulations and FEMA guidelines when acquiring goods and services under the FEMA award (finding A).

**Recommendation 3:** Inform Mississippi of its grant management responsibilities for ensuring that subgrantees follow Federal procurement regulations (finding B).

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<sup>3</sup> 44 CFR 13.37(a)(2) and 44 CFR 13.40(a)



## OFFICE OF INSPECTOR GENERAL

Department of Homeland Security

### **Discussion with Management and Audit Follow-Up**

We discussed the results of our audit with City, Mississippi, and FEMA officials during our audit. We also provided a draft report in advance to these officials and discussed it at the exit conference on May 13, 2015. We included the officials' comments, as applicable, in the body of the report. The City disagreed with finding A, and Mississippi and FEMA officials elected to withhold comments until after we issue our final report.

Within 90 days of the date of this memorandum, please provide our office with a written response that includes your (1) agreement or disagreement, (2) corrective action plan, and (3) target completion date for each recommendation. Also, please include the contact information for responsible parties and any other supporting documentation necessary to inform us about the status of the recommendations. Please email a signed pdf copy of all responses and closeout request to [Larry.Arnold@oig.dhs.gov](mailto:Larry.Arnold@oig.dhs.gov). Until we receive and evaluate your response, we will consider the recommendations as open and unresolved.

The Office of Emergency Management Oversight major contributors to this report are David Kimble, Director; Larry Arnold, Director; John Skrmetti, Acting Audit Manager; Katrina Griffin, Auditor; and Sean Forney, Auditor.

Please call me with any questions at (202) 254-4100, or your staff may contact Larry Arnold, Director, Gulf Coast Regional Office, at (228) 822-0346.



## OFFICE OF INSPECTOR GENERAL

Department of Homeland Security

### Appendix A

#### Objective, Scope and Methodology

We audited FEMA Public Assistance Program grant funds awarded to the City, Public Assistance Identification Number 047-29700-00. Our audit objective was to determine whether the City accounted for and expended FEMA funds according to Federal regulations and FEMA guidelines for FEMA Disaster Number 1604-DR-MS. The City received a Public Assistance grant award of \$248.3 million (\$231.9 million net after reductions for insurance) from the Mississippi Emergency Management Agency (Mississippi), a FEMA grantee, for damages resulting from Hurricane Katrina, which occurred in August 2005.

We audited 31 large and 12 small projects (see table 2) totaling \$142.1 (see table 1) million.<sup>4</sup> Our audit covered the period August 29, 2005, to October 8, 2014, during which the City claimed \$116 million in costs for the 43 projects in our audit scope. For 6 of the 43 projects, we performed a full audit review that included eligibility, procurement, and support; however, we found a procurement issue with 2 contracts which affected 37 additional projects. Therefore, we expanded our scope to include the 37 projects and only reviewed the procurement issue related to those projects. At the time of our audit, the City had not completed work on all projects and, therefore, had not submitted a final claim to Mississippi for all project expenditures.

To accomplish our objective, we interviewed FEMA, Mississippi, and City officials; gained an understanding of the City's method of accounting for disaster-related costs and its procurement policies and procedures; judgmentally selected and reviewed (generally based on dollar values) project costs and procurement transactions for the projects in our audit scope; reviewed applicable Federal regulations and FEMA guidelines; and performed other procedures considered necessary under the circumstances to accomplish our audit objective. As part of standard audit procedures, we also notified the Recovery Accountability and Transparency Board of all contracts the City awarded in excess of \$100,000 under the projects within our full audit scope to determine whether the contractors were debarred or whether there were any indications of other issues related to those contractors that would indicate fraud, waste, or abuse. The Recovery Accountability and Transparency Board determined that none of the contractors were debarred and no other issues

<sup>4</sup> Federal regulations in effect at the time of Hurricane Katrina set the large project threshold at \$55,500.



## OFFICE OF INSPECTOR GENERAL

Department of Homeland Security

### Appendix A (continued)

came to its attention related to those contractors that would indicate fraud, waste, or abuse. We did not perform a detailed assessment of the City's internal controls applicable to its grant activities because it was not necessary to accomplish our audit objective.

Table 1 shows the gross and net award amounts before and after reductions for insurance for all projects and for those in our audit scope.

**Table 1: Gross and Net Award Amounts**

	<b>Gross Award Amount</b>	<b>Insurance Reductions</b>	<b>Net Award Amount</b>
All Projects	\$248,292,509	\$(16,396,726)	\$231,895,783
Full Audit Scope	\$105,737,073	\$( 0)	\$105,737,073
Procurement Scope Only	\$ 36,400,001	\$( 7,813,990)	\$ 28,586,011

Source: FEMA project worksheets

We conducted this performance audit between October 2014 and May 2015 pursuant to the *Inspector General Act of 1978*, as amended, and according to 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 findings and conclusions based upon our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based upon our audit objective. Unless stated otherwise in this report, to conduct this audit, we applied the statutes, regulations, and FEMA policies and guidelines in effect at the time of the disaster.



## OFFICE OF INSPECTOR GENERAL

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### Appendix B

#### Potential Monetary Benefits

**Table 2: Projects Audited and Questioned Costs**

Project Number	FEMA Category of Work <sup>5</sup>	Project Scope	Net Amount Awarded	Amount Claimed	Questioned Costs
<b>Review of Infrastructure Projects:</b>					
<b>Projects Included in Full Scope:</b>					
8692	F	Water, Sewer, Stormwater Repair/Replacement – Area 2	\$25,293,630	\$21,934,418	\$1,523,281 <sup>6</sup>
10970	F	Water, Sewer Repair/Replacement Area 3B	20,813,865	16,323,205	474,984
8708	F	Water, Sewer, Stormwater Repair/Replacement – Area 1	21,316,180	14,861,822	743,234
8702	F	Water, Sewer Repair/Replacement Area 3	17,950,083	15,294,323	744,643
<b>Projects Included in Procurement Review Only:</b>					
11058	F	Water, Sewer Repair/Replacement Area 3A	6,995,526	6,505,423	354,115
11167	F	Water, Sewer, Stormwater Repair/Replacement – Area 3D	4,817,314	4,914,868	(38,280)
<b>Subtotal</b>			<b>\$97,186,598</b>	<b>\$79,834,059</b>	<b>\$3,801,977</b>
<b>Review of Harbor, Lighthouse, and Other Projects:</b>					
<b>Projects Included in Full Scope:</b>					
4722	G	Small Craft Harbor	\$ 20,231,597	\$20,231,597	\$ (253,683)
9851	G	Urie Pt. Lighthouse & Dedication Stones	131,718	131,718	2,160
<b>Projects Included in Procurement Review Only:</b>					
4223	E	Leased Building, Harbor Shop	\$ 357,803	\$ 357,803	\$ 9,218
4234	E	Leased Building, Whitecap Restaurant	1,198,603	1,117,118	(5,491)
4689	E	Municipal Courthouse	1,404,629	1,404,629	244,038
5937	E	Harbor Master Office	1,574,447	1,413,741	25,624
7196	E	Gaston Hewes Recreation Center	2,834,761	2,834,761	4,670
8492	E	Old Allen Plumbing Building	204,326	204,326	12,839
8703	E	Fire Station #7	1,153,620	1,009,512	41,412
8710	E	Centennial Museum and Waiting Station	270,262	0	66,223
8783	E	Joseph T. Jones Building (Water Department)	154,711	154,711	44,988
8813	E	Old Equipment Storage Building	93,040	93,040	14,627
8909	E	Grasslawn Museum Building	485,209	404,740	62,805
8945	G	Artimise Tugge Community Center – Pavilion	27,291	27,291	596
9031	E	Fire Station #12	59,795	59,795	12,816
9266	E	Chuck's Fish Camp Building	154,312	146,597	10,405

<sup>5</sup> FEMA classifies disaster-related work by type: debris removal (Category A), emergency protective measures (Category B), and permanent work (Categories C through G).

<sup>6</sup> The total costs relative to the infrastructure project management contract is \$8,248,864. However, as of audit scope date, FEMA had obligated only \$7,693,662 to specific projects, leaving \$555,202. For administrative purposes, we included this amount under Project 8692. FEMA could assign this amount to projects 8692, 8702, 8708, 10970, 11058, or 11167.



## OFFICE OF INSPECTOR GENERAL

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### Appendix B (continued)

**Table 2: Projects Audited and Questioned Costs (continued)**

Project Number	FEMA Category of Work	Project Scope	Net Amount Awarded	Amount Claimed	Questioned Costs
9267	E	Charles Walker Community Center at West Side Park	1,347,001	1,296,834	84,135
9268	E	Charles Walker Community Center Pavilion at West Side Park	61,994	95,530	(2,350)
9388	E	Handsboro Community Center	184,161	133,755	3,395
9588	E	Courthouse Leisure Services Administration Building	1,161,009	1,161,009	22,097
9761	E	Charles Walker Community Center Storage at West Side Park	67,065	0	(1,672)
9823	E	Sportsplex – Maintenance Warehouse	\$66,134	\$66,134	6,343
9882	E	Grasslawn Support Building	5,529	0	3,375
10046	E	Rice Pavilion, Office/Restrooms/Concessions	1,338,558	1,395,076	(8,817)
10859	G	Bert Jones Harbor	2,450,166	2,450,166	(20,781)
8256	E	Orange Grove Police Substation	3,869	0	2,312
8496	E	North Gulfport Police Resource Center	13,550	0	(405)
8942	E	Fire Station #3 - Sheds	1,262	0	1,213
9156	E	Storage Sheds	1,120	0	585
9178	E	Water Well and Lift Station Building Repair	44,045	0	729
9180	E	Shooting Range Office	4,279	0	257
9460	E	Handsboro Community Center Pavilion	16,811	0	(574)
9468	E	Gaston Point Concession and Pavilion	6,342	0	5,735
9472	E	28 <sup>th</sup> St. Cemetery – Office, Fence, Signs	4,357	0	446
9587	E	28 <sup>th</sup> St. Cemetery – Residence	2,817	0	7,244
9821	E	Sportsplex – Maintenance Warehouse - Trashcan Wash Station	4,081	0	281
9825	G	Permanent Repairs to Pavilions and Press Box Tower	16,212	0	4,085
<b>Subtotal</b>			<b>\$ 37,136,486</b>	<b>\$ 36,189,883</b>	<b>\$ 400,880</b>
<b>Totals</b>			<b>\$134,323,084<sup>7</sup></b>	<b>\$116,023,942</b>	<b>\$4,202,857</b>

Source: Office of Inspector General (OIG) analysis of FEMA project worksheets and City records

<sup>7</sup> The \$134,323,084 is net of \$7,813,990 in insurance reductions shown in table 2; therefore, the total scope obligations before insurance are \$142,137,074.



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### Appendix B (continued)

**Table 3: Summary of Potential Monetary Benefits**

Type of Potential Monetary Benefit	Amounts	Federal Share
Questioned Costs – Ineligible	\$4,202,857	\$4,202,857
Questioned Costs – Unsupported	0	0
Funds Put to Better Use	0	0
<b>Totals</b>	<b>\$4,202,857</b>	<b>\$4,202,857</b>

*Source:* OIG analysis of findings in this report



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### Appendix C

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