

# **FEMA Can Do More to Improve Public Assistance Grantees' and Subgrantees' Compliance with Federal Procurement Rules**





# DHS OIG HIGHLIGHTS

## ***FEMA Can Do More to Improve Public Assistance Grantees' and Subgrantees' Compliance with Federal Procurement Rules***

**September 2, 2016**

### **Why We Did This Audit**

FEMA grants billions of dollars each year to recipients that contract for services to help communities respond to and recover from disasters. We performed this audit to assess the extent to which FEMA has allowed contract costs we questioned for noncompliance with Federal procurement requirements. We also assessed whether FEMA has granted an exception to procurement requirements for a class of grants, rather than on a case-by-case basis.

### **What We Recommend**

We recommend FEMA (1) better define a disaster's exigent period; (2) explore additional means to enforce Federal procurement regulations; and (3) consider additional training for grantees and subgrantees.

#### **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**

The Federal Emergency Management Agency (FEMA) does not effectively enforce subgrantees' compliance with Federal procurement rules and has allowed the vast majority of procurement costs we questioned in our audits. Over a 6-year period ended September 30, 2014, our audits questioned \$352.3 million in Public Assistance grant costs for noncompliance. FEMA officials subsequently ruled that \$321.7 million, or 91.3 percent, of those costs were eligible.

We questioned these costs because Public Assistance subgrantees (local governments and nonprofit organizations) did not follow Federal rules in awarding contracts. They often failed to conduct full and open competition with contractors to lessen the risks of fraud, waste, and abuse. Many also failed to provide opportunities for disadvantaged firms such as minority firms and women's business enterprises to bid on work funded with Federal dollars as Congress intended.

Without consistent enforcement, FEMA's Public Assistance grantees and subgrantees have little incentive to comply with Federal regulations. And, because we are only able to audit a small fraction of FEMA's multibillion-dollar Public Assistance grant program per year, FEMA's allowance of ineligible contract costs may be much more widespread than our reports show. Although we recognize FEMA has taken positive steps to lessen the risk of noncompliance with procurement requirements, we believe that additional corrective actions will lessen the risks to taxpayer funds invested in disaster relief.

### **FEMA's Response**

FEMA officials provided a written response to a draft of this report. In that response, FEMA officials generally concurred with the findings and recommendations in this report. FEMA's written response also included action plans for implementation of corrective actions.



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Department of Homeland Security

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

September 2, 2016

MEMORANDUM FOR: Elizabeth Zimmerman  
Associate Administrator  
Office of Response and Recovery  
*Thomas M. Salmon*

FROM: Thomas M. Salmon  
Assistant Inspector General  
Office of Emergency Management Oversight

SUBJECT: *FEMA Can Do More to Improve Public Assistance  
Grantees' and Subgrantees' Compliance with Federal  
Procurement Rules*  
Audit Report Number OIG-16-126-D

Attached for your action is our final report, *FEMA Can Do More to Improve Public Assistance Grantees' and Subgrantees' Compliance with Federal Procurement Rules*. We incorporated the formal comments provided by your office.

The report contains three recommendations aimed at improving the Federal Emergency Management Agency Public Assistance program and enhancing the program's overall effectiveness. Your office concurred with all three recommendations and provided corresponding corrective action plans and target completion dates. Based on information provided in your response to the draft report, we consider all three recommendations to be resolved but open. Once your office has fully implemented the recommendations, please submit a formal closeout letter to us within 30 days of implementation so that we may close the recommendations. The memorandum should be accompanied by evidence of completion of agreed-upon corrective actions.

Please email comments or closure requests to [OIGEMOFollowup@oig.dhs.gov](mailto:OIGEMOFollowup@oig.dhs.gov).

Consistent with our responsibility under the *Inspector General Act*, we will provide copies of our report to congressional committees with oversight and appropriation responsibility over the Department of Homeland Security. We will post the report on our website for public dissemination.

Please call me with any questions, or your staff may contact Paige Hamrick, Director Central Regional Office-North, at (214) 436-5200.





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### Background

The *Robert T. Stafford Disaster Relief and Emergency Assistance Act* (*Stafford Act*) authorizes FEMA to provide financial assistance to States, local governments, Indian tribal governments, and certain private nonprofit organizations for debris removal, emergency protective measures, and permanent restoration of infrastructure following a Presidential declaration of an emergency or major disaster.

FEMA has administratively combined these *Stafford Act* authorities under the umbrella of its Public Assistance program, under which FEMA provides financial assistance through grants to a State or Indian tribal government (grantees), which in turn award subgrants to other eligible Public Assistance applicants (subgrantees). Grantees and subgrantees spend billions of dollars in Federal grant funds each year on contractor services to help respond to, and recover from, federally declared disasters. As a condition of receiving this financial assistance, grantees and subgrantees must comply with, among other things, the Federal procurement requirements set forth at 44 Code of Federal Regulations (CFR) 13.36 (for States, local, and Indian tribal governments) and 2 CFR 215.40–48 (for nonprofit organizations).<sup>1</sup> <sup>2</sup> Federal regulations generally have the force of Federal law.

### Results of Audit

FEMA does not use all available remedies to enforce compliance with Federal procurement rules. During the 6 years ended September 30, 2014, FEMA has allowed at least \$321.7 million in ineligible procurement costs we questioned under its Public Assistance grants. In our audit reports for that period, we questioned \$352.3 million for contract costs that did not comply with Federal procurement regulations.<sup>3</sup> Of that amount, FEMA has allowed \$321.7 million, or about 91.3 percent, of the questioned costs in recommendations closed as of July 1, 2015.

Although FEMA has the regulatory authority to enforce grant compliance under 44 CFR 13.43 by disallowing all or part of costs not in compliance, FEMA has

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<sup>1</sup> OMB consolidated the Administrative Requirements, Cost Principles, and Audit Requirements for Federal awards into 2 CFR Part 200, effective December 26, 2014. However, 44 CFR Part 13 and 2 CFR Part 215 remain in effect for disasters declared before that date. All audits in this report include declared disaster dates before the effective date of that change.

<sup>2</sup> When conducting procurements under a grant, State grantees must follow the same policies and procedures used for procurements of non-Federal funds 44 CFR 13.36(a) or 2 CFR 200.317, as applicable. However, Indian tribal grantees must follow the requirements of 44 CFR 13.36(b) through (i) or 2 CFR 200.318 through 200.326, as applicable.

<sup>3</sup> The \$352.3 million does not include \$35 million of questioned cost that remains open and unresolved (also see the next footnote) and does not include an additional \$118,887 recovered in DD-13-07.



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limited authority to grant exceptions on a case-by-case basis under 44 CFR 13.6(c). FEMA's acceptance of nearly all procurement costs we questioned for noncompliance with procurement requirements, has in effect, constituted an exception to an entire class of grants—an express power of the U.S. Office of Management and Budget (OMB), not FEMA, per 44 CFR 13.6(b). By allowing costs that are not compliant with procurement requirements, FEMA has not adequately upheld its responsibility to protect taxpayer funds. Further, this allowance of costs weakens FEMA's ability to enforce good procurement practices. Grantees and subgrantees would be more motivated to comply if FEMA would better enforce procurement requirements and consistently disallow costs that do not comply with Federal procurement requirements. Because we audit only a small fraction of FEMA's multibillion-dollar Public Assistance grant program per year, FEMA's allowance of the majority of ineligible contract costs we questioned indicates the potential for a much larger problem.

When grantees and subgrantees circumvent Federal procurement requirements, especially those that require full and open competition, the effects can be costly and serious. Proper procurement not only serves to hold down costs, but it helps to curb fraud, waste, and abuse. These requirements also promote socioeconomic policies that Congress has legislated and OMB has adopted. For example, subgrantees often do not take the steps required to ensure that small businesses and minorities and women have adequate opportunities to bid on work funded with Federal dollars. FEMA's own regulations and grant agreements with States also require compliance.

FEMA recognized that noncompliance with procurement requirements is a significant problem and has taken action to address it. In April 2014, FEMA's Office of Chief Counsel created the Procurement Disaster Assistance Team concept to deploy staff to disasters with the goal of proactively improving compliance. In December 2014, FEMA also published its *Field Manual – Public Assistance Grantee and Subgrantee Procurement Requirements Under 44 C.F.R. Pt. 13 AND 2 C.F.R. Pt. 215*. In addition, following major disaster declarations, our Emergency Management Oversight Teams periodically deploy to disasters to, among other activities, help FEMA educate subgrantees on procurement compliance.

FEMA officials provided a list of other actions taken over the last 2 years to address procurement-related issues, including—

- implementation in 2016 of a new Public Assistance project work stream in an effort to improve program delivery, including providing better guidance to subrecipients through the project worksheet development and grant processes;
- creation of the Recovery Audits Section by Recovery Directorate to facilitate Recovery audit engagements and improve Recovery programs



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through analysis of audit findings to identify root causes, trends, and areas for improvement based on lessons learned, best practices, and recurring issues;

- consolidation of all Public Assistance policies and guidance in one reference document to provide a more simplified and clear approach to inform recipients and subrecipients on Public Assistance requirements for project eligibility and funding;
- presentation of all frequent audit findings for poor contracting practices noted in OIG-15-100-D, *Audit Tips for Managing Disaster-Related Project Costs*, dated June 8, 2015, in the section and Contracting Requirement;
- Office of Response and Recovery's advisement of FEMA Regional Administrators to request their respective recipients distribute to Public Assistance and Hazard Mitigation Grant Program subrecipients OIG-15-100-D, *Audit Tips for Managing Disaster-Related Project Costs*;
- Recovery Directorate's Public Assistance Appeals and Audits Branch's (PAAB) comparative analysis of OIG audit findings and Public Assistance appeals over the last 3 years to identify trends and best practices;
- presentations to FEMA Regions, recipients, subrecipients, and other stakeholders during FEMA's Public Assistance Workshop in April 2015 on recurring issues and areas for improvement;
- implementation of PAAB's appeals analyst certification training to FEMA Regions, which includes guidance on the relationship between appeals and audits and instructs the Regions to engage OIG if a contemplated appeal determination will reverse a deobligation FEMA had agreed to perform based on an OIG recommendation; and
- FEMA Office of Chief Counsel undertaking a Strategic Legal Priority focused on improving grant management and assessing enforcement methods.

FEMA needs to do more to enforce Federal procurement requirements. Education and outreach are essential, but these efforts fall short unless FEMA enforces Federal regulations with financial consequences for noncompliance. Recovering grant funds places FEMA in the politically unenviable position of taking money back from grantees and subgrantees. We recognize the magnitude of this challenge. However, that should not stop FEMA from (1) developing and clearly communicating tailored options that improve its ability to hold recipients of taxpayer funds accountable for noncompliance and (2) establishing disincentives for noncompliance. Without more accountability and consequences for noncompliance, grantees and subgrantees may have less incentive to comply and may potentially waste taxpayer money on noncompliant procurement.



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### Exceptions for Questioned Costs for Improper Procurement

We questioned \$387.3 million for procurement violations in Public Assistance grants during the 6 years ended September 2014.<sup>4</sup> As of July 1, 2015, FEMA has responded to, and we have resolved and closed, the findings and recommendations for \$352.3 million of the \$387.3 million costs questioned (\$35 million remains unresolved) (see Table 1). Of this \$352.3 million, FEMA granted an exception to procurement requirements and allowed funding for \$321.7 million, or 91.3 percent, of questioned costs.

Prime examples of noncompliance with Federal procurement regulations include failing to use open and free competition and using prohibited contracting methodologies—primarily using cost-plus-a-percentage-of-cost contracts. This can result in high-risk contracts that potentially waste millions of dollars. In addition to helping to provide assurance of reasonable costs, open and free competition helps to discourage favoritism, collusion, fraud, waste, and abuse. It also allows greater opportunity for small businesses, minority firms, and women's enterprises to compete for federally funded work.

Table 1 shows the disposition of closed recommendations as of July 1, 2015, related to noncompliance with procurement regulations for fiscal years 2009–2014. FEMA enforced procurement regulations and therefore deobligated only \$30.7 million, or 8.7 percent, of questioned costs.

**Table 1: Closed Procurement Recommendation Totals for FYs 2009–2014**

Number of Closed Recommendations Per FY		Total Questioned on Closed Recommendations	Amount FEMA Allowed	Percent Allowed	Amount FEMA Disallowed	Percent Disallowed
2009	14	\$30,231,942	\$22,928,149	75.8%	\$7,303,793	24.2%
2010	7	8,897,156	5,704,893	64.1%	3,192,263	35.9%
2011	16	138,651,279	131,412,657	94.8%	7,238,622	5.2%
2012	11	26,413,754	24,322,325	92.1%	2,091,429	7.9%
2013	26	94,367,937	93,181,744	98.6%	1,305,079	1.4%
2014	14	53,762,388	44,128,207	82.1%	9,634,181	17.9%
<b>Total</b>	<b>88</b>	<b>\$352.3million</b>	<b>\$321.7 million</b>	<b>91.3%</b>	<b>\$30.7 million</b>	<b>8.7%</b>

Source: FY 2009–2014 OIG reports and OIG analysis

<sup>4</sup> We questioned a total of \$396,213,451 during the 6 FYs for contracting violations in Public Assistance and Hazard Mitigation Grant Program grants. However, we reduced the \$396,213,451 by \$8,885,502 for costs we questioned and FEMA disallowed for other reasons, such as for unsupported costs to avoid questioning the same costs twice, resulting in the net amount questioned of \$387,327,949.



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FEMA has the authority per 44 CFR 13.43 (for States, local, and Indian tribal governments) and 2 CFR 215.62 (for private nonprofit organizations) to remedy noncompliance with grant terms (to include Federal procurement standards) by suspending payments, disallowing costs, and suspending or terminating current and future grants. In addition, Federal Regulations implemented at 2 CFR 200.338, conveys these remedies for disasters declared after December 26, 2014 (see appendix C).

In addition, regulations at 44 CFR 13.6(c) (States, local, and Indian tribal governments) and 2 CFR 215.4 (private nonprofit organizations) allow Federal awarding agencies to grant exceptions to these uniform administrative grant requirements on a case-by-case basis. However, these regulations do not permit an agency to grant exceptions for classes of grants. The Federal regulations clearly limit the authorization for exceptions for classes of grants to OMB. The rule is the same for disasters declared after December 26, 2014 (2 CFR 200.102) (see appendix C).

Therefore, FEMA has the authority to grant exceptions from the procurement requirements in unusual circumstances on a case-by-case basis, but not for an entire class of grants. However, by consistently allowing ineligible contract costs and not consistently imposing available remedies, FEMA has, in essence, granted an exception for the entire class of Public Assistance grants and disregarded OMB's prerogative.

### **FEMA Has, in Effect, Been Granting an Exception for a Class of Grants**

FEMA's practice has been to allow an exception (under 44 CFR 13.6(c)) for ineligible contract costs. Rather than imposing legally sanctioned remedies for noncompliance, FEMA typically performs a cost analysis for the claimed contract work and allows costs it deems reasonable. However, because FEMA performs these analyses after subgrantees award the contracts and bases the analyses on average prices, historical pricing, cost estimating databases, or FEMA cost codes, the outcomes are inherently subjective and typically result in reasonable costs. In addition, FEMA's method subverts the efficiencies of full and open competition and can result in higher costs. Federal taxpayers eventually pay for those higher costs.

Further, although FEMA's method might be expedient, it is a poor substitute for full and open competition because the goals of proper procurement relate to more than just reasonable cost. FEMA's practice of allowing reasonable costs provides little deterrent to improper procurement. To address this problem, FEMA management needs to explore policies that provide a clear disincentive to grantees and subgrantees that do not comply with procurement regulations.

FEMA does have discretionary authority regarding enforcement of remedies for noncompliance under 44 CFR 13.43 and 2 CFR 215.62. However, we contend





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that FEMA's failure to hold subgrantees accountable or impose any of the legally sanctioned remedies available for noncompliance constitutes, in effect, an exception for a class of grants for noncompliance with Federal procurement requirements under 44 CFR 13.6 and 2 CFR 215.4, which only OMB can grant.

FEMA officials said they do not consider their allowance and funding of improper procurement costs as an exception for a class of grants under 44 CFR 13.6 and 2 CFR 215.4, but rather as part of their discretionary authority to do so under the enforcement remedies under 44 CFR 13.43 and 2 CFR 215.62. As such, FEMA officials do not agree that they are granting an exception for an entire class of grants. Because of this, FEMA officials said they have no desire, nor do they see a need, to request a waiver from OMB to grant exceptions for a class of grants.

In addition, FEMA officials said that it would be unlikely for them to impose any penalties for procurement noncompliance because it is counter to their mission to assist communities in recovering from disaster damages. They argue that disasters and resulting damages are penalty enough, and a punitive fine would not be an effective deterrent to procurement noncompliance.

### **FEMA Needs to Assist Disaster Survivors and Minimize Taxpayer Costs**

We understand the magnitude of FEMA's stated mission, which is to "support our citizens and first responders to ensure that as a nation we work together to build, sustain and improve our capability to prepare for, protect against, respond to, recover from, and mitigate all hazards." However, all missions, no matter how worthy, must function within Federal regulations, policies, and procedures. Inherent in most Federal programs and grants is a fiduciary responsibility to all taxpayers. A Federal agency's responsibility to achieve its mission includes doing so within the confines of Federal regulations and rules and with the well-being of all citizens in mind. The regulations and rules help ensure that FEMA assists disaster survivors without incurring the risk of excess and additional costs to the taxpayer. The enforcement remedies are the vehicle to ensure protection for all taxpayers and Federal missions are accomplished within the programs' rules and regulations. FEMA's lack of consistent enforcement on grants that we audited diminishes the likelihood that subgrantees' compliance will improve. Without accountability or consequences for noncompliance with procurement requirements, taxpayer funds will remain at risk.



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### Competition

Competition is one of the most important Federal procurement requirements. Of the 82 reports containing monetary procurement findings we issued in FYs 2009–2014, 55, or 67.1 percent, contained questioned costs and recommendations related to the lack of full and open competition. Federal regulations provide certain circumstances when Federal agencies can allow procurement by noncompetitive proposals, one of which is when the public exigency or emergency will not permit a delay resulting from competitive solicitations. Generally, we do not question costs for noncompetitive procurements during the public exigency or emergency period. However, once the exigency or emergency period has ended, grantees and subgrantees should stop emergency contracts and competitively solicit the remainder of the work.

Well-defined exigent or emergency circumstances and the time periods these circumstances end directly affect the permissibility of noncompetitive procurements. Therefore, FEMA should be more proactive in requiring grantees to document and conduct timely assessments of the surrounding circumstances to determine the permissibility of noncompetitive procurements. Defining and documenting the specific circumstances and time periods for exigency is critical for grantees and subgrantees to comply with Federal procurement standards. FEMA should coordinate directly with grantee and subgrantee officials to define and document when these circumstances and periods expire for noncompetitive procurements.

We often find that grantees and subgrantees have not defined the exigent or emergency period. Therefore, to determine whether contract actions are compliant, we have had to determine, sometimes years after the disaster event, the exigent or emergency periods. It is critical to define this period during the response to the disaster—when FEMA and the grantees have “boots on the ground” and are actively working with subgrantees to determine the extent of damages. FEMA should consider establishing policies and procedures to coordinate with grantee and subgrantee officials early in the disaster, to clearly define and document the exigent or emergency circumstances for subgrantees.

### Prohibited Contracting Practices

Another important Federal procurement regulation is the prohibition of cost-plus-a-percentage-of-cost contracts. Both 44 CFR 13.36(f)(4) and 2 CFR 215.44(c) prohibit the use of cost-plus-a-percentage-of-cost and percentage-of-construction-cost methods of contracting.<sup>5</sup>

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<sup>5</sup> Federal law applicable to agency contracting also prohibits cost-plus-a-percentage-of-cost contracts. The Federal Acquisition Regulation (FAR) implements this prohibition at 48 C.F.R. § 16.102(c).



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Federal regulations do not prohibit all cost-plus type contracts. For instance, FEMA allows cost-plus-fixed-fee contracts, which are either lump sum or unit price contracts with a fixed contractor fee negotiated and fixed at the inception of the contract and added into the contract price. These contract types are suitable when (1) circumstances do not allow the agency to define its requirements sufficiently to allow for a fixed-price type contract, or (2) uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use any type of fixed-price contract.

However, Federal regulations are specific about the prohibition of cost-plus-a-percentage-of-cost contracts, and in 25 of 82 reports, or 30.5 percent, we noted the use of “cost-plus” contracts and the inclusion of ineligible markups on costs. Federal regulations prohibit cost-plus-a-percentage-of-cost contracts because they provide no incentive for contractors to control costs. In fact, the incentive is to *increase* costs: the more contractors charge, the more profit they make. Because the regulations are specific about cost-plus contracts, when grantees and subgrantees use the prohibited cost-plus-a-percentage-of-cost method of contracting, FEMA should at minimum disallow all or most of the markup portion of the contract. Federal taxpayers should not have to pay more than the minimum for grantees and subgrantees that fail to comply with Federal regulations and FEMA policies on procurement.

### **Impact of Section 705(c) of the *Stafford Act***

*Stafford Act* Section 705, *Disaster Grant Closeout Procedures*, sets forth limits on administrative actions that FEMA can take to recover any payments made to States or local governments for disaster or emergency assistance. FEMA has issued a policy that explains how FEMA will implement Section 705 to ensure consistent application to Public Assistance program funding.<sup>6</sup> Section 705(c) includes criteria for determining whether FEMA is prohibited from seeking reimbursement of assistance payments made for a sub-award.

Section 705 – *Disaster Grant Closeout Procedures* (42 U.S.C. 5205) states:

- 705(c) *Binding Nature of Grant Requirements* – a State or local government shall not be liable for reimbursement or any other penalty for any payment made under this Act if –
- (1) the payment was authorized by an approved agreement specifying the costs;
  - (2) the costs were reasonable; and
  - (3) the purpose of the grant was accomplished.

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<sup>6</sup> On March 16, 2016, FEMA issued FP 205-081-2, *Stafford Act* Section 705, *Disaster Grant Closeout Procedures*.



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This section of the *Stafford Act* is three-fold; and State and local governments must meet all three requirements in order to preclude repayment of grant funding. Additionally, the policy further clarifies that FEMA views compliance with Federal procurement requirements as a critical element for meeting the purpose of disaster grants. One of the key determining factors the policy listed for evaluating whether a grantee or subgrantee accomplished the purpose of the grant hinged on whether the grantee or subgrantee “demonstrates compliance with post-award terms and conditions of the Federal grant award, as described in the obligated PW [Project Worksheet] and the FEMA-State Agreement, including but not limited to applicable requirements: for **federal procurement**,...” (emphasis added).

Therefore, Section 705(c) does not preclude FEMA from recovering costs that are ineligible because of improper procurement methods. These costs are not authorized. Accordingly, FEMA may seek reimbursement even if costs were otherwise reasonable, and the grantee or subgrantee otherwise accomplished the purpose of the grant.

### **FEMA’s Procurement Disaster Assistance Team**

To improve procurement compliance, in April 2014, FEMA developed the Procurement Disaster Assistance Team. The team is comprised of attorneys whose primary mission is to work with grant applicants and FEMA employees to ensure compliance with Federal procurement standards. Also, in December 2014, FEMA published the *Procurement Disaster Assistance Team Field Manual* (Field Manual).<sup>7</sup> It describes and explains the mandatory requirements for grantees and subgrantees when using Public Assistance funding.

This Field Manual also contains information about how FEMA interprets and applies Federal procurement requirements and how a grantee or subgrantee can comply with these requirements. According to the Field Manual, “grantees and subgrantees that use Public Assistance funding must comply with the procurement requirements imposed by Federal law, executive orders, Federal regulations, and terms of the grant award. These requirements control non-Federal authorities (such as State or local rules for contracting) to the extent they conflict with Federal requirements.” Additionally, the Field Manual also states, “it is important to recognize that the purpose of the procurement standards in these regulations is not just to obtain the best value for a particular service or good, but also to further various public policy objectives.” Establishing these assistance teams and issuing the Field Manual are encouraging steps and should assist in improving compliance.

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<sup>7</sup> *Procurement Disaster Assistance Team – Field Manual – Public Assistance Grantee and Subgrantee Procurement Requirements under 44 C.F.R. Pt. 13 and 2 C.F.R. Pt. 215.*





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### Conclusion

FEMA's practice of not imposing legally sanctioned remedies available for procurement noncompliance as authorized in 44 CFR 13.43 and 2 CFR 215.62, constitutes, in effect, an exception for an entire class of grants for Federal requirements, which 44 CFR 13.6 and 2 CFR 215.4 prohibit, a right reserved only to OMB. FEMA has been granting exceptions to Federal procurement regulations for Public Assistance grants and, as a result, has exceeded its regulatory authority by granting an exception to procurement regulations for an entire class of grants. FEMA's policy of allowing these costs without penalty erodes compliance with Federal regulation and increases the risks of fraud, waste, and abuse of Public Assistance grants. It also fails to promote socioeconomic policies that Congress has legislated. FEMA's failure to enforce compliance or consistently impose consequences for noncompliance amounts to granting an exception to Federal procurement regulations for the entire class of Public Assistance grants. FEMA states that where it has allowed procurement costs we have questioned, it has exercised its discretionary enforcement authority because the costs were reasonable and for eligible work. We disagree that cost reasonableness is the only basis for determining eligible work, and FEMA guidance affirms the requirement to abide by the procurement rules specified in its grants. Further, although FEMA recognizes the problem of noncompliance with procurement requirements and has taken steps to educate grantees and subgrantees on proper procurement, education without consequences is not enough.

Therefore, we recommend that FEMA take steps to improve grantee and subgrantee compliance with Federal procurement regulations by enforcing these regulations. FEMA should take proactive steps early in the Public Assistance process to: (1) better communicate that Federal funding is contingent on compliance with Federal regulation and that serious financial consequences could result from noncompliance; and (2) improve compliance with and develop tailored options to enforce Federal regulations early and consistently. Federal agencies like FEMA have a fiduciary responsibility to enforce Federal procurement regulations not just because the regulations have the force of Federal law, but also because they provide an essential framework for ensuring fairness and reasonable prices while helping to prevent fraud, waste, and abuse.



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### Recommendations

We recommend that the Associate Administrator for Response and Recovery, Federal Emergency Management Agency:

**Recommendation 1:** Implement policies and procedures to coordinate with grantee and subgrantee officials in defining and documenting the exigent or emergency circumstances and time periods for declared disasters.

**Recommendation 2:** Undertake a review to assess all legally sanctioned remedies under 2 CFR 200.338 to enforce Federal procurement regulations and to deter noncompliance. Based on the results of the assessment, develop tailored options to address certain forms of procurement noncompliance and the proper method to effect such changes through the issuance of new guidance, policy, or regulations. Such tailored options to include:

- (a) when making cost reasonableness determinations, use the least-cost alternative to determine the allowable amount;
- (b) when grantees and subgrantees use prohibited cost-plus-a-percentage-of-cost contracts, disallow all or most of the markup portion of the contract; and
- (c) establish disincentives for grantees or subgrantees that violate congressionally mandated socioeconomic goals.

**Recommendation 3:** Explore the permissibility and feasibility of: (1) using various funding resources, including using a portion of the amounts disallowed for noncompliance with Federal regulations and FEMA procurement policies, to assist communities affected by future disasters; and (2) expanding FEMA grant management and training programs for Public Assistance that focus on compliance with Federal regulations and FEMA policies on procurement.

### Discussion with FEMA and Audit Follow-up

We discussed the results of our audit with FEMA officials during our audit. We provided a discussion draft report and held an exit conference on March 10, 2016. FEMA officials provided written technical comments. We incorporated those comments, as appropriate, in this report.

FEMA officials provided a written response to a draft of the report on July 13, 2016. FEMA concurred with our recommendations (see appendix B). Based on FEMA's response, we made revisions, as appropriate, to this report. The response indicates that FEMA expects to implement its proposed corrective actions to address all recommendations by June 30, 2017. Therefore, we consider all three recommendations contained in this report to be resolved but



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open. We will evaluate for closure when FEMA provides documentation that it has implemented proposed action plans. Please email closeout documentation and request to [OIGEMOFollowup@oig.dhs.gov](mailto:OIGEMOFollowup@oig.dhs.gov).

In their response, FEMA officials made the observation: "While the OIG's findings are relevant from a historic perspective, they do not adequately consider the effectiveness of initiatives the Agency has undertaken in recent years to reduce noncompliance with procurement requirements." FEMA made this observation while noting that a large percentage of the reports from which we have drawn our report observations are from pre-2009 declared disasters. FEMA's observation about the timing of declared disasters reflected in our database of reports is correct. However, we disagree that our procurement-related findings do not continue to have current relevance. Our work on current declared disasters continues to identify ongoing noncompliance with Federal procurement standards. These procurement audit findings further emphasize the need for FEMA to implement the recommendations in this report.

The Office of Emergency Management Oversight major contributors to this report are Paige Hamrick, Director; John Polledo, Audit Manager; Patti Smith, Auditor-in-Charge; and Heather Hubbard, Auditor.

Please call me with any questions at (202) 254-4100, or your staff may contact Paige Hamrick, Director, Central Regional Office - North, at (214) 436-5200.



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## **Appendix A**

### **Objective, Scope, and Methodology**

Our audit objectives were to compile and summarize procurement findings in our Public Assistance grant and Hazard Mitigation Grant Program audits issued during FYs 2009–2014 and to assess the extent to which FEMA has allowed contract costs OIG questioned for noncompliance with Federal procurement requirements and whether FEMA has granted an exception to Federal procurement requirements for a class of grants, rather than on a case-by-case basis. The objective of all the grant audits was to determine whether the subgrantees accounted for and expended FEMA funds according to Federal regulations and FEMA guidelines. The scope of the audit covered 82 disaster-related audits containing 89 monetary procurement findings and recommendations in reports OIG issued in FYs 2009–2014.

To accomplish our audit objectives, we compiled and summarized 89 monetary procurement findings and recommendations issued during FYs 2009–2014; determined the recommendation amounts FEMA allowed and disallowed; reviewed procurement-related second appeals to FEMA Headquarters; reviewed applicable Federal laws, regulations, and FEMA guidance applicable to the procurement noncompliance we noted in reports; and performed other procedures we considered necessary to accomplish our objectives. We did not assess the adequacy of FEMA’s internal controls because it was not necessary to accomplish our audit objectives.

We conducted this audit between June 2015 and March 2016 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 during this audit and during the 82 performance audits provides a reasonable basis for our findings and conclusions based upon our audit objectives. We conducted these audits according to the statutes, regulations, and FEMA policies and guidelines in effect at the time of the disasters.





## OFFICE OF INSPECTOR GENERAL

Department of Homeland Security

### Appendix B FEMA's Comments to Draft Report


U.S. Department of Homeland Security  
Washington, DC 20472



# FEMA

July 13, 2016

MEMORANDUM FOR: John V. Kelly  
Deputy Inspector General  
Office of Inspector General

FROM:  David Bibb  
Associate Administrator (Acting)  
Office of Policy & Program Analysis

SUBJECT: Management's Response to OIG Draft Report: "FEMA Can Do More to Improve Public Assistance Grantees' and Subgrantees' Compliance with Federal Procurement Rules" (Project No. 15-054-EMO-FEMA)

Thank you for the opportunity to review and comment on this draft report. The U.S. Department of Homeland Security (DHS) appreciates the work of the Office of Inspector General (OIG) in planning and conducting its review and issuing this report.

The Department is pleased to note the OIG's recognition that "FEMA has taken positive steps to lessen the risk of noncompliance with procurement requirements . . ." FEMA recently implemented a number of initiatives the OIG acknowledged, including the establishment of the Procurement Disaster Assistance Team (PDAT), creation of the Recovery Audits Section (RAS), and publication of the *Field Manual on Public Assistance Grantee and Subgrantee Procurement Requirements Under 44 C.F.R. Pt. 13 and 2 C.F.R. Pt. 215*, which are designed to enhance and reinforce on-going agency-wide efforts to be more survivor-centric, effective, and efficient in mission and program delivery. To that end, FEMA will provide to its stakeholders state-specific analytic documents based upon this report to highlight procurement noncompliance trends for purposes of awareness and education, and has already incorporated such information into its PDAT training curriculum.

FEMA remains committed to rapidly providing assistance to reduce the suffering of disaster survivors and doing so in accordance with law. FEMA gives full consideration to all OIG audit findings and exercises its discretionary enforcement authority to resolve them. FEMA applies its discretionary enforcement authority under 44 C.F.R. § 13.43 on a case-by-case basis and has not, in fact or effect, granted an exception to an entire class



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### Appendix B (continued)

of grants. The OIG's report reflects that FEMA has deobligated 8.7 percent of funding for audited projects that involved procurement noncompliance.

In determining how to resolve audit findings, FEMA considers numerous factors including the eligibility of the applicants, the eligibility of the work, the reasonableness of the costs, the extent to which retroactive action to deobligate funds would further harm the community's recovery, and whether a punitive action approach would have deterrent effect on future applicants. FEMA often takes steps to work with applicants to resolve underlying issues associated with OIG recommendations, thereby making a deobligation unnecessary. Based on understanding of FEMA's enforcement authority and consideration of such factors, the OIG ultimately agreed to resolve and close those recommendations even though the Agency did not fully deobligate the questioned costs.<sup>1</sup>

FEMA is working proactively with grantees to reduce procurement noncompliance. Over the last two years, FEMA employed a multi-faceted approach focusing on preventive action, strengthened coordination with the OIG, enhanced education to stakeholders and sub-grantees,<sup>2</sup> and the use of data and trends analysis to improve our sub-grantees' awareness of their risks.<sup>3</sup> Further, and complementary to those efforts, FEMA recently completed a multi-year project to refine the delivery of the Public Assistance Program, which includes providing better guidance to sub-grantees throughout the grant process. FEMA's Office of Chief Counsel is also currently undertaking a Strategic Legal Priority focused on improving grant management, which includes an assessment on enforcement methods.

Greater than 90 percent of the audits reflected in this OIG report involve disasters declared prior to 2009. The average lag time between issuance of the audits considered and when a disaster was declared was 5.9 years. While the OIG's findings are relevant from a historic perspective, they do not adequately consider the effectiveness of initiatives the Agency has undertaken in recent years to reduce noncompliance with procurement requirements.

<sup>1</sup> See U.S. DEP'T OF HOMELAND SEC. OFFICE OF INSPECTOR GEN., OIG-15-146-D, CAPPING REPORT: SUMMARY AND KEY FINDINGS OF FISCAL YEAR 2014 FEMA DISASTER GRANT AND PROGRAM AUDITS, at 31-32 (2015) [hereinafter *FY14 Capping Report*]. The FY14 Capping Report identified a Potential Monetary Benefit (PMB) of \$971.8 million, \$812.2 million of which was for unobligated, not misspent, funds related to one Hazard Mitigation Grant Program recommendation. FEMA quickly addressed and reduced this \$812 million PMB to \$153.2 million (an 81 percent reduction). In addition, of the 84 Public Assistance (PA) grant recommendations with a PMB, FEMA has addressed, and the OIG has agreed to close, 83 of them. The outstanding PMB is \$278,822.

<sup>2</sup> In April 2014 FEMA established PDAT to provide procurement related guidance, training, and tools to recipients and subrecipients. As of May 31, 2016, PDAT had trained 6,140 personnel during a total of 179 disaster and non-disaster related presentations. In addition, PDAT published in May 2016 the *Pricing Guide for Recipients and Subrecipients under the Uniform Rules* (2 C.F.R. pt. 200) to assist FEMA recipients and subrecipients with identifying and executing basic contract cost or price analysis requirements under federal procurement regulations.

<sup>3</sup> FEMA's RAS conducted extensive data analysis of OIG audits to identify trends, best practices, and areas for improvement. This information, including data on procurement issues, was presented to Regional and recipient stakeholders at the annual PA Workshops in 2015 and 2016. On September 30, 2015 FEMA provided the OIG's Audit Tips for Managing Disaster-Related Project Costs (OIG-15-100) to all ten Regional Administrators advising them to request their recipients provide it to every PA and HMGP grant applicant.



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### Appendix B (continued)

In carrying out its mission, FEMA carefully balances its obligations to recovering communities, disaster survivors and federal taxpayers. As the trends reflected in FEMA's response to the FY 2014 Capping Report demonstrate, FEMA has made significant progress in program management and remains committed to continuing to enhance policies and procedures to further improve its effectiveness and efficiency.

The Draft Report contained three recommendations with which FEMA concurs. Please see the attached for our detailed response to each recommendation.

Again, thank you for the opportunity to review and comment on this Draft Report. Technical comments were previously provided under separate cover. Please feel free to contact me if you have any questions. We look forward to working with you in the future.





## OFFICE OF INSPECTOR GENERAL

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### Appendix B (continued)

#### Attachment: DHS Management Response to Recommendations Contained in OIG-15-054-EMO-FEMA

**Recommendation 1:** Implement policies and procedures to coordinate with grantee and subgrantee officials in defining and documenting the exigent or emergency circumstances and time periods for declared disasters.

**Response:** Concur. FEMA agrees with the OIG that greater coordination with grantee and subgrantee officials to define and document exigent or emergency circumstances for declared disasters may improve procurement compliance in using noncompetitive procurement practices. Noting such, federal procurement standards do not prescribe exigent or emergency *periods* that would permit subgrantees to engage in noncompetitive procurements. Instead, the regulations provide that circumstances dictate when procurement by noncompetitive proposals can be allowed. Consequently, the ability to engage in noncompetitive procurement should continue to be determined by contemporaneous documentation and justification of circumstances surrounding individual procurement actions, rather than by an arbitrarily defined time period that would reduce subgrantee flexibility, limit use of the exception, and possibly sanction improper procurement by noncompetitive means based on an arbitrarily defined period.

FEMA's Procurement Disaster Assistance Team (PDAT) has already developed and updated its resources to help grantees and subgrantees document and determine whether the appropriate circumstances exist to justify the use of noncompetitive procurement. PDAT's *Field Manual on Public Assistance Grantee and Subgrantee Procurement Requirements Under 44 C.F.R. Pt. 13 and 2 C.F.R. Pt. 215* (PDAT Field Manual), published in December 2014, provides key considerations in reviewing procurement actions to determine the existence of exigent and emergency circumstances as well as emphasizes the need to document the matter. On June 21, 2016, FEMA issued a supplement to the PDAT Field Manual, which addresses procurement standards under the Uniform Rules found at 2 C.F.R. Part 200 and includes guidance on exigent and emergency circumstances. PDAT has also updated its procurement training to grantees and subgrantees, and is putting together an expanded webinar on the latest guidance with separate applicant specific sections for ease of review and access. These trainings emphasize the exception, when it is appropriate to use, the requirement for documentation, and the importance of planning early to transition promptly to a competitive procurement once the exigent circumstances cease to exist.

To complement PDAT's ongoing efforts, the Public Assistance (PA) Division will develop guidance to support the documentation and justification needed to substantiate the use of noncompetitive procurement due to the existence of exigent or emergency circumstances. This will outline the appropriate documentation needed from the subrecipient and recipient to substantiate the use of the exception.





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### Appendix B (continued)

Interim Milestones	Estimated Completion Dates
1. Issuance of PDAT Field Manual Supplement	Completed
2. PDAT Expanded Webinar and Training Slides	09/30/2016
3. Development of guidance for exigent and emergency circumstances	06/30/2017

Estimated Completion Date (ECD): June 30, 2017

FEMA considers this recommendation **resolved** and **open**.

**Recommendation 2:** Undertake a review to assess all legally sanctioned remedies under 2 CFR 200.338 to enforce Federal procurement regulations and to deter noncompliance. Based on the results of the assessment, develop tailored options to address certain forms of procurement noncompliance and the proper method to effect such changes through the issuance of new guidance, policy, or regulations. Such tailored options to include:

- (a) when making cost reasonableness determinations, use the least-cost alternative to determine the allowable amount;
- (b) when grantees and subgrantees use prohibited cost-plus-a-percentage-of-cost contracts, disallow all or most of the markup portion of the contract; and
- (c) establish disincentives for grantees or subgrantees that violate congressionally mandated socio-economic goals.

**Response:** Concur. While the awarding of reasonable costs is often an effective method of addressing noncompliance with cost-specific requirements, FEMA recognizes such enforcement actions do not necessarily address noncompliance with non-cost-specific requirements. Consequently, FEMA will develop more tailored enforcement options to address different types of procurement noncompliance. Determining appropriate enforcement methods, including those to address non-cost-related forms of procurement noncompliance, requires careful review, consideration of options, and possibly rulemaking before implementing Agency-wide. Accordingly, FEMA will look to review (1) the effects of recent FEMA initiatives taken over the last two years to improve procurement compliance, and (2) other potential enforcement options, including those suggested in the OIG's recommendations. The initial phase of this review will leverage the ongoing Office of Chief Counsel Strategic Legal Priority (SLP) to develop Agency-wide grants management guidance, which includes consideration of enforcement remedies. Building upon that study FEMA will assess options and then take action through policy and, if necessary, regulation to provide a greater level of specificity with regard to tailored enforcement actions to address various forms of procurement noncompliance.



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### Appendix B (continued)

Interim Milestones	Estimated Completion Dates
1. Conduct SLP survey of enforcement options	Completed
2. Complete SLP assessment	09/30/2016
3. Finalize white paper with recommendations for options and implementation	12/31/2016
4. Present options to FEMA Senior Leadership	03/31/2017
5. Depending on option(s) selected, initiate the policy and/or rulemaking process needed to implement.	06/30/2017

ECD: June 30, 2017

FEMA considers this recommendation **resolved** and **open**.

**Recommendation 3:** Explore the permissibility and feasibility of: (1) using various funding resources, including using a portion of the amounts disallowed for noncompliance with Federal regulations and FEMA procurement policies, to assist communities affected by future disasters; and (2) expanding FEMA grant management and training programs for PA that focus on compliance with Federal regulations and FEMA policies on procurement.

**Response:** Concur. The Disaster Relief Fund (DRF) is available to provide financial assistance for communities impacted by future disasters only following a declaration by the President of a major disaster emergency. Disaster relief funds disallowed from a particular grantee are returned to the DRF and thus available to provide assistance to future declared events. FEMA will explore its current grant management and training programs and develop an issues and options paper that provides recommendations on whether these programs may be expanded to focus on compliance with Federal regulations and FEMA policies on procurement.

ECD: December 31, 2016.

FEMA considers this recommendation **resolved** and **open**.



## OFFICE OF INSPECTOR GENERAL

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### Appendix C Criteria

Federal regulations regarding enforcement/remedies for noncompliance include:

For States, local, and Indian tribal governments:

#### **44 CFR 13.43 Enforcement.**

(a) *Remedies for noncompliance.* If a grantee or subgrantee materially fails to comply with any term of an award, whether stated in a Federal statute or regulation, an assurance, in a State plan or application, a notice of award, or elsewhere, the awarding agency may take one or more of the following actions, as appropriate in the circumstances:

- (1) Temporarily withhold cash payments pending correction of the deficiency by the grantee or subgrantee or more severe enforcement action by the awarding agency,
- (2) Disallow (that is, deny both use of funds and matching credit for) all or part of the cost of the activity or action not in compliance,
- (3) Wholly or partly suspend or terminate the current award for the grantee's or subgrantee's program,
- (4) Withhold further awards for the program, or
- (5) Take other remedies that may be legally available.

Similarly, for institutions of higher education, hospitals, and other nonprofit organizations (pre-2015):

#### **2 CFR 215.62 Enforcement.**

(a) *Remedies for noncompliance.* If a recipient materially fails to comply with the terms and conditions of an award, whether stated in a Federal statute, regulation, assurance, application, or notice of award, the Federal awarding agency may, in addition to imposing any of the special conditions outlined in § 215.14, take one or more of the following actions, as appropriate in the circumstances.

- (1) Temporarily withhold cash payments pending correction of the deficiency by the recipient or more severe enforcement action by the Federal awarding agency.
- (2) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.
- (3) Wholly or partly suspend or terminate the current award.
- (4) Withhold further awards for the project or program.
- (5) Take other remedies that may be legally available.



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### Appendix C (continued)

Federal Regulations implemented at 2 CFR 200, effective for disasters declared after December 26, 2014:

#### **2 CFR 200.338 Remedies for noncompliance.**

If a non-Federal entity fails to comply with Federal statutes, regulations or the terms and conditions of a Federal award, the Federal awarding agency or pass-through entity may impose additional conditions, as described in § 200.207 Specific conditions. If the Federal awarding agency or pass-through entity determines that noncompliance cannot be remedied by imposing additional conditions, the Federal awarding agency or pass-through entity may take one or more of the following actions, as appropriate in the circumstances:

- (a) Temporarily withhold cash payments pending correction of the deficiency by the non-Federal entity or more severe enforcement action by the Federal awarding agency or pass-through entity.
- (b) Disallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.
- (c) Wholly or partly suspend or terminate the Federal award.
- (d) Initiate suspension or debarment proceedings as authorized under 2 CFR part 180 and Federal awarding agency regulations (or in the case of a pass-through entity, recommend such a proceeding be initiated by a Federal awarding agency).
- (e) Withhold further Federal awards for the project or program.
- (f) Take other remedies that may be legally available.

Federal regulations regarding case-by-case exceptions and exceptions for a class of grants include:

#### **44 CFR 13.6 Additions and exceptions.**

- (a) For classes of grants and grantees subject to this part, Federal agencies may not impose additional administrative requirements except in codified regulations published in the FEDERAL REGISTER.
- (b) Exceptions for classes of grants or grantees may be authorized only by OMB.
- (c) Exceptions on a case-by-case basis and for subgrantees may be authorized by the affected Federal agencies.





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### Appendix C (continued)

#### **2 CFR 215.4 Deviations.**

The Office of Management and Budget (OMB) may grant exceptions for classes of grants or recipients subject to the requirements of this part when exceptions are not prohibited by statute. However, in the interest of maximum uniformity, exceptions from the requirements of this part shall be permitted only in unusual circumstances. Federal awarding agencies may apply more restrictive requirements to a class of recipients when approved by OMB. Federal awarding agencies may apply less restrictive requirements when awarding small awards, except for those requirements which are statutory. Exceptions on a case-by-case basis may also be made by Federal awarding agencies.

Federal Regulations implemented at 2 CFR 200, effective for disasters declared after December 26, 2014, state (in part):

#### **2 CFR 200.102 Exceptions.**

- (a) With the exception of Subpart F—Audit Requirements of this part, OMB may allow exceptions for classes of Federal awards or non-Federal entities subject to the requirements of this part when exceptions are not prohibited by statute. However, in the interest of maximum uniformity, exceptions from the requirements of this part will be permitted only in unusual circumstances. Exceptions for classes of Federal awards or non-Federal entities will be published on the OMB Web site at [www.whitehouse.gov/omb](http://www.whitehouse.gov/omb).
- (b) Exceptions on a case-by-case basis for individual non-Federal entities may be authorized by the Federal awarding agency or cognizant agency for indirect costs, except where otherwise required by law or where OMB or other approval is expressly required by this part.
- (c) The Federal awarding agency may apply more restrictive requirements to a class of Federal awards or non-Federal entities when approved by OMB, or when, required by Federal statutes or regulations, except for the requirements in Subpart F—Audit Requirements of this part. A Federal awarding agency may apply less restrictive requirements when making fixed amount awards as defined in Subpart A—Acronyms and Definitions of this part, except for those requirements imposed by statute or in Subpart F—Audit Requirements of this part.
- (d) [omitted]



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