



DEPARTMENT OF HOMELAND SECURITY

Office of Inspector General
Dallas Field Office - Audit Division
3900 Karina Street, Room 224
Denton, Texas 76208

October 29, 2003

MEMORANDUM

TO: Richard Hainje, Regional Director
FEMA Region VII
Tonda L. Hadley

FROM: Tonda L. Hadley, Field Office Director

SUBJECT: City of Hoisington, Kansas
FEMA Disaster Number 1366-DR-KS
Public Assistance Identification Number 009-32550-00
Audit Report Number DD-02-04

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

The City received an award of \$2.26 million from the Kansas Division of Emergency Management (KDEM), a FEMA grantee, for damages resulting from severe storms, hail, flooding, and tornadoes beginning on April 21, 2001, and continuing. The award provided 75 percent FEMA funding for all categories of work A through G. The award consisted of 8 large projects and 18 small projects.¹ The audit covered the period April 21, 2001, to November 7, 2002, during which the City claimed \$2.26 million and KDEM disbursed \$1.86 million in direct program costs. The OIG examined the costs for four large projects and two small projects totaling \$1.72 million, representing 76 percent of the total award (see Exhibit).

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 tests of the City's accounting records, a judgmental sample of project

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

expenditures, and other auditing procedures considered necessary under the circumstances.

RESULTS OF AUDIT

The City did not expend and account for FEMA funds according to federal regulations and FEMA guidelines. The City's claim contained \$262,015 in questioned costs (\$196,511 FEMA share) for unsupported and ineligible volunteer credits (\$120,534), excessive and unreasonable costs (\$47,880), unsupported contractor labor costs (\$42,933), work not related to the disaster (\$34,910), unallowable markups on contract costs (\$6,148), unsupported contractor equipment costs (\$3,908), unsupported force account labor (\$2,740), duplicate benefits (\$1,782), and unsupported force account equipment and material (\$1,180).

In addition, the City did not follow federal procurement regulations to contract for \$779,269 in construction services. As a result, fair and open competition did not occur and FEMA had no assurance that contract costs were reasonable.

Finding A: Unsupported and Ineligible Volunteer Credits

The City's claim included \$120,534 in unsupported (\$93,195) and ineligible (\$27,339) volunteer credits. FEMA Donated Resources Regulation 9525.2, paragraph 7.A.1, states that donated resources must be documented by a local public official or designate. Further, the documentation must include a record of hours worked, the work site, a description of work for each volunteer, and equivalent information for equipment and materials. The City failed to consistently record the required information at the time of the disaster and failed to provide supplemental documentary evidence to support \$93,195 of volunteer credits. Further, the City claimed \$27,339 for work performed outside its area of legal responsibility and, therefore, outside the scope of the project. Accordingly, the OIG questioned \$120,534 in unsupported and ineligible volunteer credits.

Finding B: Excessive and Unreasonable Costs

The City's claim included \$47,880 in excessive and unreasonable costs for transportation of hazardous waste from Kansas to Utah. These excessive and unreasonable costs resulted from a \$3.00 per round-trip mile rate, when KDEM had approved a \$3.00 per one-way mile rate. Additionally, the OIG contacted four transportation companies who all stated that a reasonable rate would be \$3.00 or less per one-way mile. The Office of Management and Budget (OMB) Circular A-87, Attachment A, paragraph C.2., defines a reasonable cost as one that, in nature and amount, does not exceed that which would be incurred by a prudent person. Further, the Circular states that, in determining the reasonableness of a given cost, consideration should be given to, among other things, market prices for comparable goods or services. The \$3.00 per round-trip mile charge

was twice the approved rate and twice the market price for comparable services. Therefore, the OIG questioned \$47,880 as excessive and unreasonable.

Finding C: Unsupported Contractor Labor Costs

The City's claim included \$42,933 in unsupported contractor labor costs. According to 44 CFR 13.20(b)(2), a subgrantee must maintain accounting records that adequately identify the source and application of federal funds. Additionally, 44 CFR 13.20(b)(6) provides a specific list of source documentation, including cancelled checks, paid bills, payrolls, time and attendance records, and contracts that are acceptable as supporting documents for the accounting records. Because the City was unable to provide acceptable source documentation, such as timesheets, to support the labor costs, the OIG questioned these costs.

Finding D: Work Not Related to the Disaster

The City's claim included \$34,910 for work not related to the disaster:

- \$20,194 for Force Account Labor. Documentation for the force account labor did not substantiate that the workers performed disaster work related to the electric utility reconstruction. The disaster site was located across town from the utility plant and approved work required the installation of poles, wire, and transformers. Force account labor that appeared to be disaster-related occurred in the 5 months immediately after the disaster and was traceable to claimed equipment usage and transportation charges to and from the work site. However, the 986 hours of questioned force account labor occurred in October and November, 6 and 7 months after the disaster. Contrary to the previous months, during these months, the City claimed no related charges for equipment or transportation. Repair of downed utility lines without using utility equipment is not feasible, with the possible exception of salvage reclamation, but no salvage credit was claimed. Because equipment was necessary for the type of work approved and transportation was necessary to travel to the disaster work site, these labor hours did not appear related to the disaster.
- \$9,135 for Contract Labor. Documentation for contract labor did not substantiate that the workers performed disaster work related to the electric utility reconstruction. The questioned contract labor occurred on a Saturday. The contractor employees worked the previous Friday and the following Sunday with utility equipment; however, they used no equipment on the Saturday in question. Utility repairs require equipment usage. Therefore, the contract labor appeared to be idle, standby time, which is unallowable and not disaster related.

- \$2,758 for Work Prior to the Disaster. This work consisted of force account labor overtime carried forward from the period prior to the disaster.
- \$1,625 for Equipment. These costs consisted of freight and equipment that the City did not provide documentary evidence to substantiate a direct disaster relationship.
- \$1,198 for Repairs to Private Property. These repairs were documented as the result of damage caused by a power surge during utility repair work and, therefore, did not result from the disaster.

According to 44 CFR 206.223(a)(1), an item of work must be required because of the disaster event to be eligible for financial assistance. Because the City did not substantiate that these charges were related to the disaster event, the OIG questioned \$34,910 for work not related to the disaster.

Finding E: Unallowable Markups

The City’s claim included \$6,148 in unallowable markups ranging from 10 to 20 percent applied to pass-through subcontractor material and labor invoices for time-and-materials contracts that were not bid, contained no price ceilings, and on which a cost analysis was not performed. According to 44 CFR 13.36(f)(4), the cost-plus-a-percentage-of-cost method of contracting shall not be used. Further, 44 CFR 13.36(f)(1) and (2) require a cost analysis and separately negotiated profit when adequate price competition is lacking. The City did not provide documentary evidence that it performed the requisite cost analysis, described in 44 CFR 13.36(d)(4)(ii) as verifying the proposed cost data, the projections of the data, and the evaluation of the specific elements of costs and profits. The City did not negotiate profit as a separate element of its contracts; and the City’s contractors were unable or unwilling to provide the OIG with factual data detailing the amount of overhead and profit included in their rates. Therefore, the OIG questioned the \$6,148 in markups because the cost-plus-a-percentage-of-cost method of contracting is prohibited and because the City failed to demonstrate that the markups were a component of reasonable profit.

Finding F: Unsupported Contractor Equipment Costs

The City’s claim included \$3,908 in contractor equipment costs unsupported by source documents. According to 44 CFR 13.20(b)(2), a subgrantee must maintain accounting records that adequately identify the source and application of federal funds. Additionally, 44 CFR 13.20(b)(6) provides a specific list of source documentation, including cancelled checks, paid bills, payrolls, and contracts that are acceptable as supporting documents for the accounting records. Because the City was unable to provide acceptable source

documentation, such as equipment usage logs tied to operator hours, to support the \$3,908 in equipment costs, the OIG questioned these costs.

Finding G: Unsupported Force Account Labor

The City's claim included \$2,740 in unsupported force account labor costs. According to 44 CFR 13.20(b)(2), a subgrantee must maintain accounting records that adequately identify the source and application of federal funds. Additionally, 44 CFR 13.20(b)(6) provides a specific list of source documentation, including cancelled checks, paid bills, payrolls, time and attendance records, and contracts that are acceptable as supporting documents for the accounting records. Because the City was unable to provide acceptable source documentation, such as timesheets, to support the \$2,740 in labor costs, the OIG questioned these costs.

Finding H: Duplicate Benefits

The City's claim included \$1,782 for the replacement of insured audio equipment owned by the local school board, a separate legal entity. The school board collected insurance for these items and replaced them at no cost to the City. Section 312 of the Stafford Act specifically prohibits an entity from receiving assistance that duplicates benefits available from another source for the same purpose. Accordingly, the OIG questioned \$1,782 as duplicate benefits.

Finding I: Unsupported Force Account Equipment and Material

The City's claim included \$1,180 in force account equipment and material costs unsupported by source documents. According to 44 CFR 13.20(b)(2), a subgrantee must maintain accounting records that adequately identify the source and application of federal funds. Additionally, 44 CFR 13.20(b)(6) provides a specific list of source documentation, including cancelled checks, paid bills, payrolls, and contracts that are acceptable as supporting documents for the accounting records. Because the City was unable to provide acceptable source documentation, such as equipment usage logs tied to operator hours and paid bills for materials to support the \$1,180 claimed, the OIG questioned these costs.

Finding J: Unallowable Contract Procedures

The City did not follow federal procurement regulations to contract for \$779,269 in construction services. As a result, fair and open competition did not occur and FEMA had no assurance that contract costs claimed were reasonable.

Under 44 CFR 13.36, procurements must provide for (1) competitive bids, unless an allowable exception is met; (2) reasonable costs; (3) a cost or price analysis; and (4) negotiation of profit as a separate element of the price when competition is lacking. Further, these regulations prohibit the use of a cost-plus-a-percentage-of-cost contract, limit the use of T&M contracts to situations where no other contract is suitable, and mandate the inclusion of a ceiling price that the contractor exceeds at its own risk for T&M contracts.

The City violated material elements of these regulations on every procurement action examined by the OIG. Under 44 CFR 13.43(a)(2), failure to comply with applicable statutes or regulations can result in the disallowance of all or part of the costs of the activity or action not in compliance. Because the City disregarded federal procurement regulations and FEMA guidelines, FEMA had the authority to disallow all \$779,269 claimed for contractor costs. However, the OIG did not question costs solely based on noncompliance with procurement regulations because the City incurred the majority of costs for eligible work. Further, there was no way to quantify the impact of the City's noncompliance with federal regulations and FEMA guidelines related to procurement.

On February 26, 2001, the OIG issued *Dawson County Public Power District, Lexington, Nebraska*, (Audit Report Number W-11-01) that recommended the Regional Director of Region VII require the Nebraska Emergency Management Agency to provide guidance to subgrantees on federal regulations and FEMA guidelines related to contracting. On November 30, 2001, the OIG issued *City of Wichita, Kansas*, (Audit Report Number C-02-02) that recommended the Regional Director of Region VII, in coordination with the Kansas Division of Emergency Management, ensure that, for future disasters, subgrantees are provided guidance on federal regulations and FEMA guidelines related to contracting.

On April 22, 2002, the Region VII Director, Richard Hainje, responded to the OIG recommendation in audit report number W-11-01 with the following action plan:

- All states within the region now provide potential applicants with a *Debris Removal and Contract Information Fact Sheet* at the applicants briefing.
- During the region's most recent disasters, FEMA in conjunction with Kansas and Missouri developed a strategy for educating applicants about contracts and debris operations. During future disaster operations, Region VII and the states will maintain the same oversight as exemplified in the two current operations.
- Once disaster activity subsides, Region VII will develop workshops or other training on contracting issues and offer it to federal, state, and local employees involved in the contracting process. Implementation is expected during the first quarter of fiscal year 2003.

On April 24, 2002, the Region VII Director responded to the OIG recommendation in audit report number C-02-02 with additional details on the plan described in his April 22, 2002 response to report W-11-01. These details included a discussion of adding a contracting appendix to state administrative plans; formal training on applicable sections of the Stafford Act, 44 CFR Part 13, and FEMA guidelines; and additional state workshops on contracting issues.

Based on the Region VII action plan described in these memorandums, the OIG closed these recommendations. Because this disaster occurred before Region VII implemented the described action plan, the OIG made no recommendation to address this finding. However, the OIG will continue to examine Region VII subgrantee procurement procedures to ensure compliance with applicable federal regulations and FEMA guidelines.

RECOMMENDATION

The Office of Inspector General recommended that the Regional Director of FEMA Region VII, in coordination with the Kansas State Division of Emergency Management, disallow \$262,015 of questioned costs.

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

The OIG discussed the results of this audit with officials from the City, KDEM, and FEMA Region VII on August 21, 2003. City officials disagreed with the findings and recommendations, stating that they would gather additional documentation and work with KDEM and FEMA to resolve the findings. The OIG responded that it had delayed audit fieldwork at least 3 months because the City had not responded to OIG requests for documentation related to unsupported costs; and, therefore, the OIG would review any additional documentation the City provided after the audit report was issued.

Please advise this office by November 28, 2003, of the actions taken or planned to implement the recommendation. If you have questions concerning this report, please contact me at (940) 891-8900. Major contributors to this report were Daniel Benbow, Rita Dear, Patti Smith, and William Lough.

Schedule of Audited Projects
City of Hoisington, Kansas
FEMA Disaster Number 1366-DR-KS

<u>Project Number</u>	<u>Amount Claimed</u>	<u>Amount Questioned</u>	<u>Finding Reference</u>
Large			
25	\$ 407,277	\$ 0	J
51	418,849	102,034	B,C,D,E,F,J
58	671,190	37,665	B,E,F,G,I,J
63	<u>157,216</u>	<u>120,534</u>	A
Large Subtotal	\$1,654,532	\$260,233	
Small			
32	\$ 20,826	\$ 0	
35	<u>47,126</u>	<u>1,782</u>	H
Small Subtotal	\$ 67,952	\$ 1,782	
TOTAL	<u>\$1,722,484</u>	<u>\$262,015</u>	