



Homeland
Security

September 1, 2005

MEMORANDUM FOR: Gary Jones
Acting Regional Director, FEMA Region VI

Tonda L. Hadley

FROM: Tonda L. Hadley
Field Office Director

SUBJECT: *Western Farmers Electric Cooperative, Anadarko, Oklahoma*
FEMA Disaster Number DR-1355-OK
Public Assistance Identification Number 000-U05EF-00
Audit Report Number DD-09-05

The Office of Inspector General (OIG) audited public assistance funds awarded to Western Farmers Electric Cooperative (WFEC), Anadarko, Oklahoma. The objective of the audit was to determine whether WFEC expended and accounted for Federal Emergency Management Agency (FEMA) funds according to federal regulations and FEMA guidelines.

WFEC received an award of \$2.05 million from the Oklahoma Department of Emergency Management (OEM), a FEMA grantee, for damages resulting from a severe ice storm beginning on December 25, 2000, and ending January 10, 2001. The award provided funding for three large projects¹, (one project for emergency work funded at 100 percent and two projects for permanent work funded at 75 percent). The OIG examined all projects under the award (see Exhibit). The audit covered the period December 25, 2000, to December 2, 2002, during which WFEC claimed \$2.05 million and OEM disbursed \$1.6 million in direct program costs.

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 WFEC's accounting records, judgmental samples of project expenditures generally based on dollar amount or category of cost, and other auditing procedures considered necessary under the circumstances.

¹ Federal regulations in effect at the time of the disaster set the large project threshold at \$50,600.

RESULTS OF AUDIT

WFEC did not expend and account for all FEMA funds according to federal regulations and FEMA guidelines. WFEC did not comply with federal procurement standards or FEMA guidelines in awarding \$592,643 of contracted utility and debris removal work. Further, WFEC's claim included \$259,851 (\$245,901 FEMA share) of costs that the OIG found questionable. The questioned costs included ineligible damages to private property (\$204,049), overstated fringe benefits (\$34,098), duplicate labor costs (\$15,984), and unsupported costs (\$5,720).

Finding A: Improper Contracting

WFEC did not comply with federal procurement standards or FEMA guidelines in awarding \$592,643 for contracted utility and debris removal work. As a result, fair and open competition did not occur and FEMA has no assurance that contract costs were reasonable. Paraphrased, federal regulations at 44 Code of Federal Regulations (CFR), section 13.36:

- Require the performance of procurement transactions in a manner providing full and open competition except under certain circumstances. (44 CFR 13.36(c)). One acceptable circumstance is when public exigency or emergency for the requirement will not permit a delay for competitive solicitation. (44 CFR 13.36(d)(4)(i))
- Require that subgrantees maintain records sufficient to detail the significant history of the procurement, including the rationale for the method of procurement, the basis for contractor selection, and basis for the contract price. (44 CFR 13.36(b)(9))
- Require subgrantees to maintain a contract administration system that ensures contractors perform in accordance with the terms, conditions, and specifications of their contracts or purchase orders. (44 CFR 13.36(b)(2))
- Require a cost or price analysis in connection with every procurement action, including contract modifications. (44 CFR 13.36(f)(1))
- Prohibit the use of time and material type contracts unless no other contract is suitable and provided that the contract include a ceiling price that the contractor exceeds at its own risk. (44 CFR 13.36(b)(10))
- Require profit to be negotiated as a separate element of the price for each contract in which there is no price competition and in all cases where cost analysis is performed. (44 CFR 13.36(f)(2))

Rather than competitively bidding contract work for utility line repair and debris removal, WFEC selected contractors based on past work history or from referrals by other electric cooperatives. The selected contractors provided rate sheets; and WFEC awarded the work using time-and-material purchase orders without cost ceilings. Further, WFEC did not analyze the proposed contractor costs for reasonableness nor did they negotiate contractor profits as a separate element of costs. WFEC officials stated that they considered the cost of work reasonable if it was \$200,000 or less per mile of utility line.

In addition, WFEC did not adequately monitor the work of contractor crews. WFEC stated that they did monitor how many miles the crews advanced on a daily basis. However, they did not maintain logs or reports that documented contractor activities to compare to contractor invoices. Without proper documentation, WFEC could not verify charges for labor and equipment. FEMA Public

Assistance Guide (FEMA 322, October 1999, page 40) states that applicants should avoid time-and-material contracts, but if they are used, applicants must carefully monitor and document contractor expenses and include a cost ceiling provision in the contract.

According to 44 CFR 13.43(a)(2), failure to comply with applicable statutes or regulations can result in the disallowance of the costs of the activity or action not in compliance. However, we did not question the contract costs because WFEC incurred these costs under exigent circumstances, which sometimes justify the use of non-competitive, time-and-material contracts. We considered the period December 25, 2000, when the ice storm occurred, through February 16, 2001, when WFEC fully restored power to all its customers, to be an “emergency period” that constituted exigency because life and property were at stake.

Both WFEC and OEM should be aware that, while exigent circumstances may justify the use of non-competitive, time-and-material contracts, they do not justify not following other procurement standards imposed to ensure the reasonableness of contract costs. WFEC should have performed a cost analysis, negotiated profit as a separate element of costs, set a realistic ceiling price, and monitored contract performance using daily activity logs.

According to 44 CFR 13.37(a)(2), grantees are responsible for ensuring that subgrantees are aware of requirements imposed upon them by federal statute and regulation. WFEC officials stated that OEM did not instruct them on proper federal procurement standards and told them that they could follow their normal procurement procedures. While the regulations do state that subgrantees will use their own procurement procedures, the regulations also state that those procedures must conform to applicable federal law and standards identified in 44 CFR 13.36.

Further, 44 CFR 13.40(a) states that “[g]rantees are responsible for managing the day-to-day operations of grant and subgrant supported activities.” Grantees must monitor grant and subgrant activities to ensure compliance with applicable federal requirements and the achievement of performance goals. WFEC’s lack of compliance with federal procurement standards clearly demonstrates that OEM did not adequately monitor WFEC’s subgrant activities.

WFEC is aware of its improper contracting procedures and, in response to a Single Audit Office of Management and Budget (OMB) Circular A-133 (June 27, 2003) conducted for the year-ended December 31, 2002, has implemented procedures to assure that bids or quotes are received for disaster work. However, even though WFEC has documented new procedures, we noted that these procedures did not include all federal requirements for contracting.

Recommendation:

The OIG recommended that the Regional Director, FEMA Region VI:

1. Require the Oklahoma Department of Emergency Management to develop, document, and implement procedures for future disasters to (a) provide subgrantees guidance on federal regulations, standards, and guidelines related to procurement and (b) monitor subgrantees to ensure compliance with those federal regulations, standards, and guidelines.

Finding B: Ineligible Damages to Private Property

WFEC claimed \$204,049 under Project 3540 for damages to private property. However, the entire amount is ineligible because the damages did not pose a threat to public health or safety. FEMA's Public Assistance Policy Digest (FEMA Publication 321, October 1998, page 85) states that repairs to private property are not eligible unless the damages result in a health or safety risk. WFEC paid the \$204,049 to landowners or to contractors who made repairs for the landowners for damages resulting from WFEC's access to right of ways to repair electrical transmission lines. Accordingly, we questioned the entire \$204,049 as ineligible damages to private property.

In addition to being ineligible, the costs for repairs to private property were also unsupported. According to 44 CFR 13.20(a)(2), subgrantees' accounting for grant funds must permit the tracing of funds to a level of expenditures adequate to establish that the subgrantee uses grant funds in an applicable manner. WFEC based its payments for damages to private property on estimates rather than actual costs. Therefore, we could not determine whether property owners spent the funds for their intended purpose. The estimates also included costs for items that were otherwise ineligible such as seeding and fertilizing pasturelands, lost production, and \$54,350 of costs that did not have adequate descriptions of the work performed.

Further, OEM funded Project 3540 at 100 percent for emergency debris removal, rather than 75 percent for permanent work. However, only a small portion of the claimed costs was for debris removal. Therefore, even if these costs had been eligible and supported the error in categorization would have resulted in \$51,012 of questioned costs (\$204,049 X 25%).

Recommendation:

The OIG recommended that the Regional Director, FEMA Region VI:

2. Disallow \$204,049 claimed for ineligible damages to private property.

Finding C: Overstated Fringe Benefit Costs

WFEC's claim included \$34,098 that we questioned as overstated fringe benefits. WFEC erroneously applied a fringe benefit rate to labor costs that was higher than its normal rate. OMB Circular A-122, Att. B, section 7(f)(2), states that fringe benefits are allowable, but will be distributed to particular awards and other activities in a manner consistent with the pattern of benefits accruing to the individuals or groups of employees whose salaries and wages are chargeable to such awards and other activities. Therefore, we questioned the \$34,098 of overstated fringe benefits.

Recommendation:

The OIG recommended that the Regional Director, FEMA Region VI:

3. Disallow \$34,098 of overstated fringe benefit costs.

Finding D: Duplicate Labor Costs

WFEC's claim included \$15,984 for labor that we questioned as duplicate costs. The duplicate costs included labor for administrative and management personnel (\$15,508) and labor for mechanics (\$476). The costs for administrative and management personnel were covered under the statutory administrative allowance. These personnel were not engaged in disaster-related field activities, but were managing facilities or performing administrative and secretarial-type duties. According to 44 CFR 206.228(a)(2)(ii), the administrative allowance covers the subgrantee's necessary costs of requesting, obtaining, and administering federal disaster assistance subgrants. Similarly, the costs for mechanics to work on equipment were duplicate costs because these costs were included in the equipment rates. WFEC claimed equipment costs at the FEMA rate, which includes the cost of operation, insurance, depreciation, and maintenance (FEMA Public Assistance Policy Digest, October 1998). Accordingly, we questioned \$15,984 (\$15,508 + \$476) as duplicate labor costs.

Recommendation:

The OIG recommended that the Regional Director, FEMA Region VI:

4. Disallow \$15,984 of duplicate labor costs.

Finding E: Unsupported Costs

WFEC's claim included \$5,720 for force account and contract costs that we questioned because WFEC did not provide adequate source documentation. The unsupported costs included:

- Equipment costs of \$2,799 that WFEC did not support with proper timesheets or vehicle operating records.
- Labor costs totaling \$1,879 that WFEC did not support with time and attendance records documenting that employees were engaged in disaster-related activities.
- Contract costs totaling \$1,042 less than invoice amounts.

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 list of adequate source documentation including cancelled checks, paid bills, payrolls, time and attendance records, and contract award documents that are acceptable accounting records. No records were provided to document the above-referenced costs. Accordingly, we questioned the \$5,720 as unsupported costs.

Recommendation:

The OIG recommended that the Regional Director, FEMA Region VI:

5. Disallow \$5,720 of unsupported costs.

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

We discussed the results of the audit with WFEC officials on July 19, 2005. WFEC officials agreed with the findings and recommendations. The OIG discussed the results of the audit with OEM on June 28, 2005, and with FEMA Region VI on June 28, 2005.

Please advise this office by November 30, 2005, of the actions taken or planned to implement the recommendations, including target completion dates for any planned actions. If you have questions concerning this report, please call me at (940) 891-8900. Major contributors to this report were Paige Hamrick, Charles Riley, and Jerry Prem.

EXHIBIT

**Schedule of Audited Projects
Western Farmers Electric Cooperative, Anadarko, Oklahoma
FEMA Disaster Number DR-1355-OK**

| <u>Project Number</u> | <u>Category</u> | <u>Percent of Federal Funding</u> | <u>Amount Claimed</u> | <u>Questioned Costs</u> | <u>Finding Reference</u> |
|---------------------------|-----------------|---------------------------------------|---------------------------|-----------------------------|------------------------------|
| 3540 | A | 100 | \$ 204,049 | \$204,049 | B |
| 3221 | F | 75 | 1,782,789 | 53,674 | A, C, D, E |
| 3222 | F | <u>75</u> | <u>59,372</u> | <u>2,228</u> | C, D |
| Totals | | | <u>\$2,046,210</u> | <u>\$259,851</u> | |