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Homeland
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March 2, 2011

MEMORANDUM FOR: Nancy Ward, Regional Administrator
FEMA Region IX

FROM: 
Humberto U. Melara, Director
Western Regional Office

SUBJECT: *California Department of Forestry and Fire Protection*
Sacramento, California
Public Assistance Identification Number 000-UYUB9-00
FEMA Disaster Number 1731-DR-CA
Audit Report Number DS-11-06

We audited public assistance funds awarded to the California Department of Forestry and Fire Protection, Sacramento, California (Department). The objective of the audit was to determine whether the Department expended and accounted for Federal Emergency Management Agency (FEMA) funds according to federal regulations and FEMA guidelines.

The Department received a public assistance award of \$122 million from the California Emergency Management Agency (Cal EMA),¹ a FEMA grantee, to provide emergency protective measures for Southern California wildfires that occurred in October 2007. The award provided 75% FEMA funding for one large project. We reviewed cost categories that included: labor, non-rental equipment, fringe benefits, and administrative charges with a total claimed amount of about \$80 million. The remaining claim of about \$42 million that was not covered in our audit scope included a multitude of cost categories, such as per diem, food, water, office expense, and rental equipment. The audit covered the period October 21, 2007, to October 2, 2009,² and included a review of selected invoices totaling \$33 million, or 41% of the cost claimed for the categories of costs we reviewed.

¹ At the time of the disaster, the grantee's name was the California Office of Emergency Services, which became a part of Cal EMA on January 1, 2009.

² In a letter dated November 10, 2010 FEMA management advised Cal EMA that they had approved an additional \$80,848,965 to the initial \$41,234,041 award amount for the large project, resulting in a total award of \$122,083,006. See Finding D of this report.

We conducted this performance audit under the authority of 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 on our audit objective. We believe that the evidence obtained during the audit provides a reasonable basis for our findings and conclusions based on our audit objective.

We interviewed FEMA, Cal EMA, and Department officials; reviewed judgmentally selected samples (generally based on dollar value) of documentation to support project costs; and performed other procedures considered necessary to accomplish our objective. We did not assess the adequacy of the Department’s internal controls applicable to grant activities because it was not necessary to accomplish our audit objective. We did, however, gain an understanding of the Department’s method of accounting for disaster-related costs.

RESULTS OF AUDIT

Of the \$80,398,408 the Department claimed for the cost categories selected for audit, \$12,676,128, or 16%, was not in compliance with applicable federal requirements. The Department also did not properly request additional funding for a cost overrun exceeding \$80 million. The table below lists our findings and the associated costs we question in this report.

Finding	Subject	Amount Questioned
A	Eligibility of Labor, Equipment, and Related Costs	\$ 7,823,339
B	Support for Labor, Equipment, and Related Costs	1,832,746
C	Support for Mutual Aid Administrative Surcharges	3,020,043
D	Unauthorized Cost Overrun	0
Total		\$12,676,128

In addition, based on the results of our testing, we estimate that an additional \$19 million would be questioned if a 100% review of the categories of costs we sampled were performed. (See the “Other Matters” section of this report for further details of this determination).

The principal criteria used in determining the eligibility or supportability of the costs we question in Findings A and B are listed below.

- Title 2, *Code of Federal Regulations* (CFR), Part 225, Appendix A, Sections C.1.a and C.1.j, provide that to be allowable under federal awards, costs must be necessary and reasonable for proper and efficient performance and administration of federal awards, and be adequately documented [Findings A and B].
- FEMA Recovery Policy 9525.7, *Labor Costs - Emergency Work*, Section VII.H, provides that FEMA reimbursement for employees is limited to actual time worked, even when the applicant is contractually obligated to pay for 24 hour shifts. The policy further states that it is not reasonable for a person to work more than 48 hours continuously without an extended rest period. Therefore, FEMA will reimburse up to 24 hours for each of the first 2 days, and up to 16 hours for each of the following days for emergency work. All requested hours must

be for actual time worked, and standby time is not eligible under the Public Assistance Program or Fire Management Assistance Grant Program [Findings A and B].

- FEMA Disaster Assistance Policy 9523.6, *Mutual Aid Agreements for Public Assistance and Fire Management Assistance*, Section VII.B.1, provides in part that, to be eligible for reimbursement by FEMA, the costs must be reasonable. Section VII.H.1 of this policy also provides that requesting and providing entities must keep detailed records of the services requested and received and provide these as part of the supporting documentation for a reimbursement request [Finding B].
- According to 44 CFR 13.20(a)(2), a state must have fiscal controls and accounting procedures sufficient to permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes [Finding B].
- According to 44 CFR 206.228, FEMA has published a Schedule of Equipment Rates for use in determining allowable hourly rates for applicant-owned equipment. This schedule of rates provides that equipment must be in actual operation and performing eligible work to be eligible [Finding B].

Finding A: Eligibility of Labor, Equipment, and Related Costs

The Department claimed labor hours that exceeded the maximum claimable under FEMA's policy regarding the reimbursement for labor costs associated with emergency work. As a result, the Department's eligible labor costs and related equipment charges and workers' compensation costs were overstated. (See listing of applicable federal criteria in the preceding paragraph.) The following table identifies the type of costs and ineligible amounts.

Description	Ineligible Amounts
Labor	\$6,652,458
Equipment	834,485
Workers' Compensation	336,396
Total	\$7,823,339

Labor. The Department claimed \$6,652,458 for ineligible labor costs that exceeded the maximum hours allowable under FEMA criteria. These costs consisted of \$1,888,227 for force account labor and \$4,764,231 for mutual aid contract labor (first responders from a multitude of local and state governmental jurisdictions in California and Nevada). Generally, the claim for labor included 24 hours daily based on a portal-to-portal concept that considered, while on deployment for wildfire response away from the home station, the responders were on call even for those hours when they were "off-shift." The Department contended the responders should be compensated for all deployment hours, including sleep and other off-shift periods. This practice resulted in claiming costs that were not necessary or reasonable for the proper and efficient performance and administration of the grant. Likewise, the practice was contrary to FEMA's policy of only allowing actual time worked up to 16 hours per day after the first continuous 48 hours of an emergency or disaster.

Based on the activity records submitted, the Department claimed costs for labor hours not actually worked. For the costs to be eligible for FEMA reimbursement, they must not exceed the actual hours worked and be within the maximum hours allowable. Therefore, we question \$6,652,458 claimed for costs that did not meet the stated criteria.

Equipment. The Department claimed \$834,485 for equipment costs that were ineligible. The claim included 16 hours daily for equipment use, including the days in which the assigned crew members, according to the activity records, were off-shift. The claim for equipment hours during non-operating periods does not conform to applicable federal criteria, including FEMA's Schedule of Equipment Rates, that require eligibility to be based on actual operating hours. We identified the number of equipment hours claimed for which the crew members were off-shift, and determined that the \$834,485 was claimed for non-operating hours and was therefore ineligible.

Workers' Compensation. The Department claimed workers' compensation costs by applying the applicable percentage of each mutual aid entity to the base labor rate claimed. Because we questioned ineligible mutual aid contract labor costs, the related workers' compensation costs of \$336,396 were also ineligible.

FEMA officials stated that, subject to verification of our calculations, they agreed with the portion of our questioned costs (\$5,703,540) that was based on hours claimed in excess of the maximum 16 hours per day. They did not agree with our adjustment to actual hours worked below 16, regardless of the actual hours reported on the activity records. Cal EMA and Department officials did not agree with any of the questioned costs because they did not agree with the FEMA policy on maximum daily hours eligible for reimbursement.

Finding B: Documentary Support for Labor, Equipment, and Related Costs

The Department claimed mutual aid contract labor and equipment hours that were not properly supported with source documentation. In addition, related workers' compensation and other charges were also unsupported. The following table identifies the types of costs and unsupported amounts.

Description	Unsupported Amounts
Labor	\$1,478,409
Equipment	239,180
Workers' Compensation	93,122
Other Charges	22,035
Total	\$1,832,746

Labor. The Department claimed \$1,478,409 for mutual aid contract labor that was not supported by records of actual hours worked. Multiple local governmental entities in California and Nevada provided mutual aid response to the wildfires and generally claimed compensation from the Department based on a portal-to-portal basis that considered the employees should be paid continuously during the deployment period regardless of actual hours worked. This procedure did not conform to applicable federal criteria that require eligible costs to be: (1) necessary and reasonable; (2) based on actual hours worked; and (3) supported by detailed records.

Many of the mutual aid entities complied with the detailed records requirement in FEMA Policy 9523.6 by submitting activity records that detailed the actual time worked versus off-shift periods for each employee. In those cases, we questioned ineligible costs (as shown in Finding A) for hours that were claimed in excess of actual hours worked. However, other entities did not meet the records requirement because the activity records did not always show daily hours worked. Instead, they reported the overall deployment period and claimed all hours during this period without recording actual hours worked (i.e., on-shift vs. off-shift). We questioned unsupported costs of \$1,478,409 that were not documented as actual hours worked.

Equipment. The Department claimed \$239,180 for equipment costs that were unsupported by activity records that showed actual hours of operation. The claim for undocumented equipment hours did not conform to applicable federal criteria, including FEMA's Schedule of Equipment Rates, that require documentation to show the actual equipment operating hours. Therefore, we question the \$239,180 of unsupported equipment costs claimed.

Workers' Compensation. The Department claimed workers' compensation costs by applying the applicable percentage of each mutual aid entity to the base labor rate claimed. Because we question unsupported mutual aid contract labor costs, we also question the related workers' compensation costs of \$93,122 that was claimed by the Department.

Other Charges. The Department claimed \$22,035 in unemployment insurance and vehicle charges that are related to the unsupported mutual aid contract labor costs that we question in this finding. Thus, we question the \$22,035 as unsupported.

FEMA officials did not agree that unsupported hours below 16 hours daily should be questioned. Cal EMA and Department officials did not agree with any of the questioned costs because they did not agree with FEMA's policy on the maximum daily hours eligible for reimbursement.

Finding C: Documentary Support for Mutual Aid Administrative Surcharges

The Department claimed unsupported administrative surcharges of \$3,020,043 billed by mutual aid entities based on percentages applied to all labor, equipment, and fringe benefits charges. This method of charging indirect costs did not meet federal requirements because it was based on neither actual costs nor a cost allocation plan that assigned costs relative to the benefits received.

According to 2 CFR, Part 225, Appendix A, costs must be adequately documented (Section C.1.j), reasonable (Sections C.1.a and C.2), and must be assignable to a project according to relative benefits received (Section C.3.a). Section G pertains to interagency services and provides that "[t]he cost of services provided by one agency to another within the government unit may include allowable direct costs of the service plus a pro rate share of indirect costs. A standard indirect cost allowance equal to 10% of the direct salary and wage cost of providing the service (excluding overtime, shift premiums and fringe benefits) may be used in lieu of determining the actual indirect costs of the service..." However, these services do not include centralized services included in central service cost allocation plans as described in Appendix C. Appendix C provides that indirect costs (departmental and central services) may be pooled and distributed to different programs on bases that will produce a reasonable and consistent result in consideration of relative benefits derived, through the development of a cost allocation plan and an indirect cost rate.

In billing for administrative costs, state agencies applied a 28% surcharge to their invoiced costs and the local jurisdictions applied a 16.14% surcharge to their invoiced costs. Cal EMA officials said these percentages were pursuant to their pre-disaster agreement for mutual aid services, but were not based on cost documentation of the providing entities. The invoice costs to which the percentages were applied included all labor, overtime, fringe benefits, and equipment charges. This methodology was not established under a cost allocation plan, was not reasonable, and did not assure that indirect costs were allocated according to relative benefits received as required by federal regulations.

The Department did not provide any documentation to support the 28% rate claimed for state agencies or the 16.14% rate claimed by local governmental entities. As such, for state agencies, we applied the 10% standard indirect cost allowance (prescribed in criteria cited above) to the eligible regular salaries and wages of the state agencies and determined that state agencies claimed unsupported administrative costs of \$303,090. For the local entities, we consider the total claimed amount of \$2,716,953 to be unsupported because the 16.14% rate was not supported by actual administrative cost documentation or cost allocation plans. Therefore, for all mutual aid entities, we question \$3,020,043 in total for unsupported administrative charges.

FEMA officials agreed that documentation of administrative costs is needed to determine eligibility of claimed costs. Cal EMA and Department officials did not agree with any of the questioned costs.

Finding D: Unauthorized Cost Overrun

In October 2009, about 2 years after incurring the costs, the Department submitted its claim to Cal EMA for \$122,083,006, or \$80,848,965, more than the \$41,234,041 FEMA had approved for the project at that time. Cal EMA forwarded the claim and its recommendation for approval to FEMA in July 2010. In November 2010, FEMA officials notified Cal EMA that they had approved the additional \$80,848,965.³

According to 44 CFR 206.204(e), subgrantees may find during project execution that actual project costs exceed approved project worksheet estimates. The subgrantee must evaluate each cost overrun and, when justified, submit a request for additional funding through the grantee (in this case, Cal EMA) to the Regional Administrator (here, FEMA Region IX) for a final determination. Also, FEMA *Public Assistance Guide* (FEMA 322, dated June 2007, pp. 139-140) provides that an applicant should notify the grantee as soon as possible when a need for additional funding is discovered. It states that the applicant should not assume that the excess costs can be reported at the end of the project and that the additional funds will be approved automatically. The request for additional funding should contain justification for the eligibility of the additional costs. The grantee will forward the request to FEMA with a written recommendation. FEMA will render a decision and notify the grantee with an amended project worksheet for additional funding or a written denial of the request.

The Department did not request supplemental funding during the course of performing the approved work or subsequent to its completion as stipulated in the FEMA guidance. As a result, FEMA and the grantee did not promptly review the excess costs nor advise the applicant of ineligible or unsupported costs that it had incurred. Thus, the ineligible and unsupported costs identified in Findings A, B, and C, as well as the additional ineligible and unsupported costs that we estimated

³ Because FEMA's notification occurred after our fieldwork ended, we did not verify whether FEMA had reviewed the claimed costs or obligated the additional funds.

(Other Matters below) may have been disclosed earlier and corrected if FEMA guidance had been followed. Similarly, the \$42 million not included in our audit scope may also include ineligible and unsupported costs that a timely review would have disclosed.

In July 2010, we discussed the cost overrun with FEMA officials who said they were aware that additional costs were incurred but they would not approve supplemental funding until they reviewed the supporting documentation. In August 2010, Cal EMA and Department officials said they agreed with FEMA’s policy of reviewing supporting documentation before approving supplemental funding.

Other Matters

Based on the results of our audit tests, we estimate that an additional \$19 million would be questioned if a 100% review were performed of the cost categories we sampled. Although we did not use statistical sampling, our samples were large (41% of the \$80 million claimed for mutual aid and force account labor and equipment) and costs reviewed were generally selected based on dollar values, rather than the likelihood of negative results. As such, there is a high probability that the exception rates for eligibility and supportability of costs reviewed would be similar for costs not reviewed.

As shown in the table below, the exception rates for costs reviewed were 50% for the mutual aid local entities, 34% for the mutual aid state agencies, and 23% for force account labor (the Department’s regular employees). Based on these results, we estimate that an additional \$19,491,989, comprised of the same categories of ineligible and unsupported costs, would be questionable if a 100 percent review were performed.

Description	Cost Universe for Categories Audited	Exception Rate	Projected Additional Unallowable Costs
Mutual aid-local entities	\$52,632,169	50%	\$26,277,575
Mutual aid-state agencies	9,433,217	34%	3,245,917
Force account labor	11,562,929	23%	2,644,625
Force account equipment	6,770,093	0%	0
Total	\$80,398,408		\$32,168,117
		Less questioned costs - Findings A, B, & C	-12,676,128
		Projected Additional Unallowable Costs	\$19,491,989

RECOMMENDATIONS

We recommend that the Regional Administrator, FEMA Region IX, in coordination with the California Emergency Management Agency:

Recommendation #1: Disallow ineligible labor and related costs of \$7,823,339 (Finding A).

Recommendation #2: Disallow unsupported labor, equipment, and related costs of \$1,832,746 (Finding B).

Recommendation #3: Disallow unsupported administrative surcharges of \$3,020,043 (Finding C).

Recommendation #4: Advise the Department on the proper procedures for requesting additional funding for project cost overruns (Finding D).

Recommendation #5: Require the Department to review its costs incurred and submit a revised claim based on supporting documentation and applicable federal criteria (Other Matters).

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

We discussed the results of our audit with Department, Cal EMA, and FEMA officials during our audit and included their comments in this report as appropriate. We also provided written summaries of our findings and recommendations to these officials in January 2011; and they declined to request an exit conference because they had previously discussed the issues with us. As noted within the report findings, the Department and Cal EMA officials did not concur with Findings A, B, and C. FEMA officials concurred with Finding C and parts of Findings A and B.

Please advise this office by May 31, 2011, of the actions planned or taken to implement the recommendations, including target completion dates for any planned actions. To promote transparency, this final report and your response to this report, including your corrective actions planned, will be posted to our website, with exception of sensitive information identified by your office.

Significant contributors to this assignment were Jack Lankford, Tony Fajardo, Connie Tan, Gloria Conner, Montul Long, and Renee Gradin. Should you have questions concerning this report, please contact me at (510) 637-1463, or your staff may contact Jack Lankford, Audit Manager, at (510) 637-1462.

cc: Audit Liaison, FEMA Region IX
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