



Homeland Security

July 22, 2011

MEMORANDUM FOR: Nancy Ward
Regional Administrator
FEMA Region IX

FROM: Matt Jadacki 
Assistant Inspector General
Office of Emergency Management Oversight

SUBJECT: *Reclamation District 768, Arcata, California*
FEMA Disaster Number 1628-DR-CA
Public Assistance Identification Number 023-UZ2H7-00
Audit Report DS-11-09

We audited public assistance (PA) funds awarded to Reclamation District 768 in Arcata, California (District). Our audit objective was to determine whether the District accounted for and expended Federal Emergency Management Agency (FEMA) funds according to federal regulations and FEMA guidelines.

The District received a PA award of \$10 million from the California Emergency Management Agency (Cal EMA),¹ a FEMA grantee, for emergency protective measures and permanent repairs to facilities damaged by severe storms beginning on December 17, 2005. The award provided 75% FEMA funding for one large project and three small projects.² The audit covered the period from December 17, 2005, to March 23, 2011. We audited the one large project (Project 2076), with a total award of \$9.9 million, or 99% of the total award. As of June 2011, the District has completed all of the projects.

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 and appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. The evidence obtained during the audit fulfilled those requirements.

We discussed issues related to this audit with FEMA, Cal EMA, and District officials; reviewed judgmentally selected samples of cost documentation (generally based on dollar value); and performed other procedures considered necessary to accomplish our objective. We did not assess the adequacy of the District'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

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 At the time of the disaster, the large project threshold was \$57,500.

District's method of accounting for disaster-related costs and its procurement policies and procedures.

RESULTS OF AUDIT

District officials did not comply with federal regulations and FEMA guidelines when procuring professional services and disaster repairs totaling \$2,087,966 (\$1,565,975 federal share). This amount includes \$844,893 for excessive and unreasonable professional services costs. Further, after completing all disaster-related projects, the District had a remaining unused award amount of \$1,894,342 (\$1,420,757 federal share) that should be deobligated and put to better use.

Finding A – Contracting Procedures

District officials did not follow federal procurement regulations and FEMA guidelines for two contracts totaling \$2,087,966. Specifically, the District did not obtain competitive bids or proposals; perform cost analyses; or take affirmative steps to ensure that small and minority firms, women's business enterprises, and labor surplus area firms were used when possible.

Therefore, we question the following ineligible contract costs:

- \$1,385,512 paid to a local firm for professional services (engineering, design services, and project management). We refer to these services as architectural and engineering (A&E).³
- \$702,454 of additional repair work incorporated into an existing contract by way of a change order that should have been opened for competition. The District added the repair work to an existing contract 30 days after it was executed. The initial contract (identified by the District as Project A) was awarded based on the low bid of \$964,312. The contract did not include the extra repair work (identified by the District as Project B) totaling \$702,454. In addition, the District did not perform a cost analysis as required by procurement regulations to ensure that the additional costs were reasonable.

Federal procurement regulations at 44 CFR 13.36, Procurement, require, among other things—

- Performing procurement transactions in a manner providing full and open competition except under certain circumstances. One allowable circumstance is when there is a public exigency or emergency for the requirement that will not permit a delay resulting from competitive solicitation. (13.36(c)(1) and (d)(4)(i)(B))
- Performing a cost or price analysis in connection with every procurement action, including contract modifications. (13.36(f)(1))
- Taking affirmative steps to ensure that small and minority firms, women's business enterprises, and labor enterprise surplus area firms are used when possible. 13.36(e)

³ The \$1.4 million of A&E costs include \$844,893 that is also questioned as ineligible in Finding B because it was excessive and unreasonable.

FEMA procurement guidelines (*Public Assistance Guide*, FEMA 322; October 1999; pp. 39–40) specify that contracts must be of reasonable cost; generally must be competitively bid; and must comply with federal, state, and local procurement standards.

The District did not use competitive procurement methods and could not reasonably justify sole-sourcing for the \$2,087,966 (\$1,385,512 plus \$702,454) of A&E services and repair work. Full and open competition increases the opportunity for obtaining reasonable pricing from the most qualified contractors. Competitive contracting also allows the opportunity for small and minority firms, women’s business enterprises, and labor enterprise surplus area firms to participate in federally funded work. In addition, full and open competition helps discourage and prevent favoritism, collusion, fraud, waste, and abuse. District officials justified their procurement practices by stating that—

- They were comfortable with pre-disaster work the local consultant had completed for the District and therefore other firms were not considered, and
- Awarding additional repair work under an existing contract was cost-effective. The District did not provide documentation to support this assertion.

Because the District did not comply with federal procurement regulations and FEMA guidelines, we question \$2,087,966 of ineligible A&E services and repair work. This amount includes \$844,893 in A&E costs that are also questioned as ineligible in Finding B because they were excessive and unreasonable. To avoid duplicate questioned costs, the net amount recommended for disallowance for this finding is \$1,243,073.

Finding B – Professional Services

District officials charged \$844,893 in excessive and unreasonable engineering, design services, and project management (A&E) costs. FEMA officials estimated A&E costs at 8.2% of total construction cost; however, the District charged 21%. The District’s records did not include documentation explaining the nature of the excessive charges.

Federal regulations and FEMA guidelines 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 must be adequately documented. (2 CFR, Part 225, Appendix A, Sections C.1.a and C.1.j)
- Basic engineering and design services for disaster projects of average complexity are funded based on a percentage of construction cost identified in FEMA engineering and design services cost curve B. In addition, special services not included in the curve B percentage allowance are eligible for reimbursement separately. (FEMA 322; October 2007; pp. 56–61)

The District did not comply with this requirement. The scope of work for the project consisted of various repairs within a 4.9-mile levee area, and FEMA determined these repairs were of

average complexity. The repairs generally included removing broken concrete and placing riprap rock, as illustrated in figure 1.



Figure 1. Levee Riprap Slope Repair
Source: E&D consulting firm records for Project 2076

FEMA estimated A&E costs for the project using curve B and selected 8.2% as the applicable percentage of eligible construction costs. When the 8.2% is applied to the final construction costs of \$6,592,917, the allowable A&E charges total \$540,619. The District's 21% of A&E costs totaled \$1,385,512, or \$844,893 above the eligible costs. District records did not include justification for these excessive charges and did not identify charges for special services not included in the allowable percentage. Therefore, we question \$844,893 in A&E costs as excessive and unreasonable.

Finding C – Funds Not Used

FEMA estimated and approved Project 2076 for \$9,890,208. The District incurred actual project costs of \$7,995,866. Therefore, FEMA should deobligate the difference of \$1,894,342 (\$1,420,757 federal share) and put those funds to better use.

RECOMMENDATIONS

We recommend that the FEMA Region IX Administrator, in coordination with Cal EMA:

Recommendation #1: Disallow \$1,243,073 (federal share \$932,305) of ineligible contract costs incurred without compliance with federal procurement regulations and FEMA guidelines (Finding A). This amount is net of the \$844,893 recommended for disallowance in Recommendation #2 below.

Recommendation #2: Disallow \$844,893 (federal share \$633,670) of engineering, design, and project management costs that were ineligible as excessive and unreasonable (Finding B) and incurred without compliance with federal procurement regulations and FEMA guidelines (Finding A).

Recommendation #3: Deobligate \$1,894,342 (federal share \$1,420,757) and put those funds to better use (Finding C).

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

We discussed the results of this audit with District, 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 in advance to Cal EMA on June 10, 2011, to the District on June 14, 2011, and to FEMA on June 8, 2011. District officials disagreed with Findings A and B and did not comment on Finding C. FEMA and Cal EMA officials withheld further comment until after we issue our final report.

Within 90 days of the date of this memorandum, please provide our office with a written response that includes your (1) agreement or disagreement, (2) corrective action plan, and (3) target completion date for each recommendation. Also, please include names of responsible parties and any other supporting documentation necessary to inform us about the current status of the recommendation. Until your response is received and evaluated, the recommendations will be considered open and unresolved.

Consistent with our responsibility under the *Inspector General Act*, we are providing copies of our report to appropriate congressional committees with oversight and appropriation responsibility over the Department of Homeland Security. To promote transparency, this report will be posted to our website, with the exception of sensitive information identified by your office. Significant contributors to this report were Humberto Melara, Louis Ochoa, Renee Gradin, and Arona Maiava.

Should you have questions concerning this report, please contact me at (202) 254-4100 or Humberto Melara at (510) 637-1463.

cc: Audit Liaison, FEMA Region IX
Audit Liaison, FEMA (Job Code: G-11-013-EMO-FEMA)
Audit Liaison, DHS