



Homeland Security

AUDIT TIPS FOR MANAGING DISASTER-RELATED PROJECT COSTS

Department of Homeland Security
Office of Inspector General

I. Introduction

The Department of Homeland Security (DHS), Office of Inspector General (OIG), prepared this guide. It is for recipients of FEMA public assistance and hazard mitigation funds. Using it will help you to:

- Document and account for disaster-related costs,
- Minimize the loss of FEMA disaster assistance program funds,
- Maximize financial recovery, and
- Prevent fraud, waste, and abuse of disaster funds.

This pamphlet has five parts:

- (1) This introduction.
- (2) A brief overview of the OIG (Part II).
- (3) Applicable Federal regulations that govern the management of FEMA disaster assistance grants (Part III).
- (4) Information about the audit process and frequent audit findings (Part IV). This part responds to frequently asked questions about common problems found during our audits of disaster projects.
- (5) Key points to remember when administering FEMA grants (Part V).

II. Overview of the Office of Inspector General

The Homeland Security Act of 2002 provided for the establishment of an OIG in DHS by amendment to the Inspector General Act of 1978 (P.L.-95-452). The OIG serves as an independent unit to promote economy, efficiency, and effectiveness; to prevent

waste, fraud, and abuse; and to keep Congress and the Secretary of DHS fully informed of problems in DHS programs and operations. The principal functions of the OIG are to:

- Perform or oversee all audit functions relating to programs and operations of DHS;
- Inspect department activities to identify actual or potential fraud, waste, abuse, or mismanagement, and to develop recommendations for corrective action; and
- Investigate allegations of illegal, unethical, or other activities that may lead to civil or criminal liability on the part of DHS or its employees, contractors, or program participants.

III. Applicable Federal Regulations and FEMA Guidelines

Many directives are available to you as a public assistance applicant. Some help in responding to and recovering from a disaster. Others help in getting and managing Federal funds. The most important is Title 44 of the Code of Federal Regulations (44 CFR), which contains policies and procedures for implementing the Robert T. Stafford Disaster Relief and Emergency Assistance Act, as amended (Stafford Act). These basic policies and procedures govern disaster relief operations. Title 44 CFR is available at the following website:

www.access.gpo.gov/su_docs/index.html.

Pay particular attention to Part 13 (44 CFR 13) that sets forth administrative requirements for grants, and to Part 206 (44 CFR 206) that sets forth the disaster assistance rules applicable to major disasters and emergencies declared by the President.

Other important directives, issued by the Office of Management and Budget (OMB), establish administrative requirements and cost principles applicable to public

assistance and hazard mitigation applicants.

OMB Circulars are available online at: www.whitehouse.gov/omb/circulars/index.html

The table below references other Federal rules that may apply to your organization. To be certain that you are aware of all applicable requirements, we strongly urge you to contact your State’s disaster management officer or the Disaster Field Office (DFO).

	State and Local Governments	Public and Private Institutions of Higher Education	Hospitals Affiliated With Institutions of Higher Education	Quasi-Public And Private Nonprofits	Public and Private Hospitals
Administration of Grants	44 CFR 13 OMB Circular A-102	OMB Circular A-110	OMB Circular A-110	OMB Circular A-110	OMB Circular A-110
Cost Principles	OMB Circular A-87	OMB Circular A-21	OMB Circular A-21	OMB Circular A-87	OMB Circular A-87
Audits	OMB Circular A-133	OMB Circular A-133	OMB Circular A-133	OMB Circular A-133	OMB Circular A-133

IV. The Audit Process and Frequent Audit Findings

The OIG reviews several factors to determine which activities to audit. These factors include:

- Statutory and regulatory requirements;
- Current or potential dollar magnitude;
- Requests from congressional, FEMA, or State officials;
- Reports/allegations of impropriety or problems in implementing the FEMA programs.

The OIG tries to cover the full range of FEMA-funded disaster activities (temporary housing, public assistance, mitigation, etc.), and organizations that receive funds for conducting those activities.

Generally, the OIG schedules audits within 3 years after the grantee or subgrantee reports that all work has been completed and the final expenditure report has been submitted. The audits are conducted mainly to determine whether the grantee and subgrantees expended and accounted for FEMA funds according to federal regulations and FEMA guidelines.

Frequent Audit Findings (examples)

A. Poor Project Accounting

Criteria: Federal regulations (44 CFR 13.20 and 206.205) require each subgrantee to maintain a system that accounts for FEMA funds on a project-by-project basis. The system must disclose the financial results for all FEMA-funded activities accurately, currently, and completely. It must identify funds received and disbursed and reference source documentation (i.e., cancelled

checks, invoices, payroll, time and attendance records, contracts, etc.).

Finding 1: The subgrantee did not account separately for the costs of each project. The subgrantee had five distinct FEMA-funded projects but accounted for project expenditures under one cost center. As a result, the subgrantee's claim could not be verified by project.

Finding 2: The subgrantee's journal of project expenditures did not contain references to payroll or daily activity reports that supported the payroll expenditures charged to the FEMA project. Therefore, expenditures for labor could not be systematically traced to supporting documents and the costs claimed could not be readily verified.

B. Unsupported Costs

Criteria: Federal regulations (OMB Circular A-87 and 44 CFR 13.20) require that costs claimed under Federal programs must be adequately supported by source documentation such as cancelled checks, payrolls, contracts, etc.

Finding 1. The subgrantee claimed \$150,000 for contract labor but had invoices and cancelled checks to support only \$100,000. The OIG questioned the unsupported difference of \$50,000.

Finding 2. The subgrantee's claim included \$300,000 for force account labor. However, the subgrantee had time sheets and payroll registers to support only \$275,000. The OIG questioned the unsupported difference of \$25,000.

Finding 3. The subgrantee claimed \$1 million for materials withdrawn from its existing inventory to repair its electrical distribution system. The subgrantee had a listing of material items reportedly used for

repairs and a listing of the value of such items. However, records reflecting the withdrawal of items from the existing inventory did not support the listing. Accordingly, the OIG questioned the \$1 million claim.

C. Duplication of Benefits

Criteria: Government policy (Stafford Act and 44 CFR 206.191) prohibits duplication of benefits. In other words, a subgrantee cannot receive disaster funding for activities covered by insurance benefits, other Federal programs, or any other source.

Finding 1. The subgrantee claimed and received \$200,000 to repair a fence, replace dirt, and construct a retaining wall at a baseball park facility. However, the subgrantee had insurance coverage that was never acknowledged to FEMA, and received \$220,000 from its insurance carrier for the same damages. Thus, the subgrantee was not eligible for the \$200,000 of FEMA funding.

Finding 2. The subgrantee received \$100,000 of FEMA funds to repair its fire station. This amount and \$300,000 of anticipated insurance proceeds accounted for the \$400,000 needed for disaster-related repairs. However, the subgrantee had actual insurance recoveries of \$350,000. Under this scenario, the subgrantee should refund the \$50,000 of excess FEMA funding.

Finding 3. Under a FEMA project, the subgrantee had losses of \$1 million. The losses were fully covered by insurance. However, the subgrantee only pursued and received insurance recoveries of \$500,000. Thus, the remaining losses of \$500,000 were improperly funded under the FEMA project.

Finding 4. The subgrantee claimed and received \$100,000 of FEMA funds for road repairs and to replace a chain link fence at a Head Start facility. However, the

subgrantee also received funds from the U.S. Department of Housing and Urban Development and the U.S. Department of Health and Human Services to carry out the same activities. Therefore, the \$100,000 of FEMA funds duplicated the funds received from the other Federal programs.

D. Excessive Equipment Charges.

Criteria: Federal regulations (44 CFR 206.228) require that subgrantees use the FEMA schedule of equipment rates or their local rates -- whichever are lower. Applicants that do not have local established rates must use the FEMA equipment rates when claiming costs under a FEMA project.

Finding 1. The subgrantee's claim included \$78,348 for the use of bucket trucks. The claim was calculated using the FEMA rate of \$24 per hour (3,264.5 hours x \$24 per hour). However, the subgrantee's equipment rate for bucket trucks was \$16 per hour, or \$8 less than the FEMA rate. Therefore, the OIG questioned \$26,116 (3,264.5 hours x \$8) of excess charges.

E. Excessive Labor and Fringe Benefit Charges.

Criteria: According to OMB Circular A-87, allowable costs must be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities of the governmental unit. According to 44 CFR 206.228, straight or regular-time salaries and benefits of permanent employees engaged in emergency service work are not eligible for FEMA assistance.

Finding 1. The subgrantee's \$50,000 claim for overtime fringe benefits was overstated by \$30,000. The claim was based on a fringe benefit rate of 23.55 percent. However, the rate included the cost of workmen's compensation, which is not

applicable to overtime. The claim should have been based on a rate of 10 percent, resulting in charges of \$20,000. Thus, the subgrantee received \$30,000 of FEMA funds to which it was not entitled.

Finding 2. The subgrantee claimed \$10,000 for fringe benefits for personnel supplied by a temporary personnel agency. However, the subgrantee did not provide fringe benefits to the workers or pay the personnel agency for the costs claimed. Therefore, the charges were inappropriate.

Finding 3. The subgrantee charged a debris-removal project \$250,000 for regular time (\$150,000) and overtime (\$100,000) labor costs of permanent employees. The \$150,000 for regular-time labor was not eligible for FEMA funding and the charge was disallowed.

F. Unrelated Project Charges

Criteria: According to OMB Circular A-87, charges to Federal grants must be necessary and reasonable to fulfill the objective of the grant program.

Finding 1. FEMA funds were awarded to repair a local electrical distribution system. However, the subgrantee's claim under the project included charges of \$10,000 for meals provided to the subgrantee's vice presidents, car washes, and a VCR. The OIG questioned these costs because they did not benefit the project.

Finding 2. The subgrantee claimed and received \$500,000 to repair Road XYZ. However, the subgrantee's claim included \$250,000 for heavy equipment and material charges for Road ABC. The OIG questioned the \$250,000 for Road ABC because the road was not included under the approved project.

G. Unapplied Credits

Criteria: According to OMB Circular A-87, grants must be reduced by credits that offset or reduce expenses allocable to Federal awards.

Finding 1. FEMA awarded funds for repairs to the subgrantee's electrical distribution system. The subgrantee sold scrap material related to the FEMA project. However, the subgrantee did not credit the FEMA project with the sale proceeds of \$15,000. Thus, the OIG questioned \$15,000 of the subgrantee's final claim.

Finding 2. The City received two credit discounts totaling \$7,000 under a FEMA project for early payments to a contractor. However, the \$7,000 was not reflected in the City's claim under the project. Accordingly, FEMA reduced its final payment to the subgrantee by \$7,000.

H. Excessive Administrative Charges

Criteria. Under the Stafford Act, the subgrantee is entitled to an administrative allowance based on a statutory formula to cover the costs associated with requesting, obtaining, and administering FEMA awards. Federal regulation (44 CFR 206.228) limits funding for administrative costs to that allowance.

Finding. A subgrantee claimed \$50,000 for overtime labor charges of administrative personnel (engineers, claims adjusters, and budget supervisors) who performed surveys and damage assessments. These charges were administrative in nature, as defined under 44 CFR 206.228. Therefore, we questioned the charges because such costs are covered under the administrative allowance.

I. Poor Contracting Practices

Criteria. Federal regulations contain procurement standards with which a subgrantee must comply under FEMA-sponsored projects. According to 44 CFR 13.36:

- The subgrantee must maintain records in sufficient detail to reflect the significant history of the procurement, including the rationale for the method of procurement, the basis for the contractor selection, and the basis for the contract price;
- The subgrantee is prohibited from using time-and-material-type contracts unless a determination is made that no other contract is suitable, and provided that the contract includes a ceiling price that the contractor exceeds at its own risk; and
- The subgrantee is prohibited from using a "cost plus a percentage of cost" contract arrangement.

Finding. The subgrantee entered into 3 contracts for renovating 19 vacant buildings to be used as temporary emergency shelters. However, the subgrantee did not document the basis for the contractor selection or the basis for the contract price. Further, although payments under the contracts were based on "time and materials," the subgrantee did not determine the availability of other contractual arrangements with more suitable pricing terms and, contrary to regulation, did not establish a ceiling price under the contracts. The subgrantee accepted and paid the contractors' bills without question.

The OIG also noted that payments under the three contracts were made on a "cost plus a percentage of cost" basis. The contractors were reimbursed for time and materials and were also given an overhead and profit allowance of 25 percent of actual costs.

Under this type of contract, the greater the labor costs, the greater the overhead and profit. This payment arrangement is prohibited because there is a disincentive to reduce costs.

At the time of our review, the subgrantee had paid \$789,255 in profit and overhead. Due to the improper contracting practices and related weak cost control measures, we questioned the reasonableness of the \$789,255 claimed for profit and overhead.

V. Key Points to Remember When Administering FEMA Grants

1. Designate a person to coordinate the accumulation of records.
2. Establish a separate and distinct account for recording revenue and expenditures, and a separate subsidy account for each distinct project awarded funds by FEMA.
3. Ensure that the final claim made for each project is supported by amounts recorded in the accounting system.
4. Ensure that each expenditure is recorded in the accounting books and references supporting source documentation (checks, invoices, etc.) that can be readily retrieved.
5. Research insurance coverage and seek reimbursement for the maximum amount. Credit the appropriate FEMA project with that amount.
6. Check with your Federal Grant Program Coordinator about the availability of funding under other Federal programs (i.e., Federal Highway, Housing and Urban Development, etc.) and ensure that the final project claim does not include costs that were funded or should be funded by another Federal agency.

7. Ensure that inventory withdrawal and usage records document materials taken from existing inventories for use under FEMA projects.
8. Do not charge the regular salary of permanent employees or seasonal employees (whose salaries are contained in annual appropriations) to FEMA debris removal and emergency service projects.
9. Do not claim costs for items or activities for which you did not have a cash outlay.
10. Ensure that claims for overtime fringe benefits are based on cost items (i.e., F.I.C.A., worker's compensation, etc.) that accrue as a result of overtime. Items such as health benefits and leave are not eligible as overtime fringe benefits.
11. Ensure that expenditures claimed under the FEMA project are reasonable and necessary, are authorized under the scope of work, and directly benefit the project.
12. Ensure that you document pertinent actions for contracts let under FEMA projects, including the rationale for the method of procurement, the basis for contractor selection, and the basis for the contract price. Remember that Federal regulations prohibit "cost plus a percentage of cost" contracts.

OIG FRAUD HOTLINE

1-800-323-8603

The DHS OIG not only conducts audits, but also aggressively investigates allegations of fraud, waste, and abuse. Below are a few of the more common allegations reported through our Hotline.

- ❑ Disaster assistance applicants use false names and/or fictitious addresses.
- ❑ Disaster assistance applicants claim losses that they did not incur or were not entitled to claim.
- ❑ Private individuals claim to be FEMA employees.
- ❑ Disaster fund recipients are victimized by contractors who inflate repair fees and/or fail to properly complete repairs.
- ❑ Disaster fund recipients damage their own properties to receive disaster assistance.
- ❑ Subgrantees do not use FEMA funds for the purpose intended.

*To report fraud, waste, or abuse, call the OIG Hotline at 1-800-323-8603; write to DHS OIG Hotline, 245 Murray Drive, S.W., Building 410, Washington, DC 20528; or send an electronic message to DHSOIGHOTLINE@dhs.gov. **OIG protects the identity of each caller and writer.***