




# Homeland Security

August 19, 2011

MEMORANDUM FOR: Major P. (Phil) May  
Regional Administrator, Region IV  
Federal Emergency Management Agency

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

SUBJECT: *FEMA Public Assistance Grant Funds Awarded to  
Memorial Hospital at Gulfport, Mississippi*  
FIPS Code 047-UHJ7Y-00  
FEMA Disaster Number 1604-DR-MS  
Audit Report Number DA-11-21

We audited public assistance grant funds awarded to Memorial Hospital at Gulfport (Hospital) in Gulfport, Mississippi. The objective of the audit was to determine whether the Hospital accounted for and expended Federal Emergency Management Agency (FEMA) funds according to federal regulations and FEMA guidelines.

As of September 2, 2010, the Hospital had received a public assistance award of \$8.3 million from the Mississippi Emergency Management Agency (MEMA), a FEMA grantee, for damages related to Hurricane Katrina, which occurred in August 2005. The award provided 100% FEMA funding for debris removal, emergency protective measures, and repair of buildings and equipment damaged as a result of the disaster. The award included nine large projects and four small projects.<sup>1</sup>

We focused our audit on \$7.7 million awarded under five large projects (see Exhibit, Schedule of Projects Reviewed). We also performed a limited review of several other projects for potential duplicate funding as a result of insurance settlement allocation issues we identified during the audit. The audit covered the period of August 29, 2005, to September 2, 2010, during which the Hospital claimed \$2.4 million under the five large projects. At the time of our audit, the Hospital had completed work on all projects, but had not submitted a final claim to MEMA for project expenditures.

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<sup>1</sup> Federal regulations in effect at the time of Hurricane Katrina set the large project threshold at \$55,500.

We conducted this performance audit pursuant to 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 upon our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based upon our audit objective. We conducted this audit according to the statutes, regulations, and FEMA policies and guidelines in effect at the time of the disaster.

We reviewed judgmentally selected samples of project costs (generally based on dollar value); interviewed Hospital, MEMA, and FEMA personnel; reviewed the Hospital's procurement policies and procedures; reviewed applicable federal regulations and FEMA guidelines; and performed other procedures considered necessary to accomplish our audit objective. We did not assess the adequacy of the Hospital's internal controls applicable to its grant activities because it was not necessary to accomplish our audit objective. We did, however, gain an understanding of the Hospital's method of accounting for disaster-related costs and its policies and procedures for administering activities provided for under the FEMA award.

## **BACKGROUND**

Memorial Hospital at Gulfport is an acute-care hospital providing inpatient, outpatient, rehabilitation, and emergency care services primarily to residents of Harrison County, Mississippi, and the surrounding area. The Hospital is a joint venture of the City of Gulfport and the Gulfport-West Harrison County Hospital District. The Hospital operates in the form of a governmental authority, governed by a board of trustees.

## **RESULTS OF AUDIT**

The Hospital did not account for expenditures on a project-by-project basis, as required by federal regulations. We also determined that the Hospital's allocation of insurance recoveries among FEMA eligible and ineligible damages may have resulted in a disproportionate share being allocated to reduce FEMA project costs.

### **Finding A: Project Accounting**

The Hospital's accounting system did not provide an accurate accounting of costs by project. The Hospital set up a single expense account and a single work order account to record all disaster expenses (FEMA and non-FEMA) and capital expenditures, respectively. As a result, the Hospital did not separately account for project expenditures and commingled them with non-FEMA related expenditures. According to 2 CFR 215.21(b), recipients' financial management systems shall provide accurate, current, and complete disclosure of the financial results of each federally sponsored project. Further, 44 CFR 206.205(b) requires large project expenditures to be accounted for on a project-by-project basis.

To conduct the audit, we obtained and reconciled various expenditure and receipt documents, schedules, and spreadsheets from MEMA to determine expenditures and receipts by project.

**Finding B: Allocation of Insurance Proceeds**

Section 312 of the *Robert T. Stafford Disaster Relief and Emergency Assistance Act*, as amended, prohibits the receipt of public assistance funds with respect to any part of such loss for which it received assistance from insurance. Also, federal regulation 44 CFR 206.250(c) states that actual and anticipated insurance recoveries shall be deducted from otherwise eligible costs.

The Hospital’s insurance policy provided coverage of \$25 million per occurrence for general property losses, business interruption, expenses to reduce loss, extra expenses, and other items. The insurance policy covered FEMA-eligible and ineligible damages without specifying limits for each type of loss. The Hospital received insurance proceeds totaling \$17.7 million under the policy and applied \$6.9 million to building damages under Project 10068 and \$10.8 million to business interruption losses, which are ineligible for FEMA reimbursement. The Hospital based the allocations on insurance settlement information provided by its insurance carrier, as shown in table 1.

<b>Table 1: Insurance Settlement Information</b>			
Coverage	Damages	Deductible	Payment
Buildings	\$ 9,783,763	(\$2,914,666)	\$ 6,869,097
Contents	532,982	(463,816)	69,166
Loss of Income	14,683,255	(3,901,340)	10,781,915
Total	\$25,000,000	(\$7,279,822)	\$17,720,178

FEMA’s Disaster Assistance Fact Sheet Number 9580.3, *Insurance Considerations for Applicants*, provides guidance to disaster applicants for allocating insurance recoveries among FEMA-eligible and ineligible damages. It notes that if the insurance policy covers eligible and ineligible damages (for example, property damage and business interruption losses, respectively) without specifying limits for each type of loss, the proceeds will be apportioned based on the ratio of the applicant’s eligible-to-ineligible damage. However, as discussed below, the Hospital’s allocation may not have been consistent with this policy, resulting in a disproportionate share being allocated to reduce FEMA project costs.

- FEMA authorized approximately \$5.1 million<sup>2</sup> under several project worksheets for emergency protective measures. Costs claimed on these projects included air conditioning and elevator repairs, boarding of broken windows, dehumidification, and monitoring of air quality for mold during the emergency period. These costs appeared to be covered by the Hospital’s insurance policy under “Expenses to Reduce Loss” and “Extra Expenses.”<sup>3</sup> However, the Hospital did not claim such expenses to its insurance

<sup>2</sup> Of the \$5.1 million, the Hospital claimed \$2.8 million, and \$2.3 million remained obligated.

<sup>3</sup> The Hospital’s insurance policy defined “Expenses to Reduce Loss” as expenses that are necessarily incurred for the purpose of reducing any loss due to business interruption. The policy defined “Extra Expenses” as excess costs necessarily incurred to continue the operation of the insured’s business or facility that would not have been incurred had there been no loss.

carrier. Had the Hospital claimed the expenses, the amount of proceeds allocable to business losses might have been less, thus providing additional proceeds to reduce FEMA project costs.

- The Hospital's insurance carrier calculated the deductible for Loss of Income (business interruption) to be \$3.9 million. However, this calculation was inconsistent with the insurance policy provisions. Per the policy, the deductible for such loss is calculated at 2% of the loss or \$1 million, whichever is greater. In this case, \$1 million would have been the greater amount, indicating that the insurance carrier underpaid the Hospital by \$2.9 million. As a result, the insurance carrier may owe the Hospital additional proceeds, which should be applied to reduce FEMA project costs as appropriate.

## RECOMMENDATIONS

We recommend that the Regional Administrator, FEMA Region IV:

**Recommendation #1:** Instruct the Hospital to separately account for project costs, as required by federal regulations (Finding A).

**Recommendation #2:** Evaluate the Hospital's allocation of insurance proceeds for consistency with FEMA guidelines and reduce FEMA project costs, as appropriate (Finding B).

## DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOWUP

We discussed the audit results with the Hospital, MEMA, and FEMA officials during our audit. We also provided a written summary of our findings and recommendations in advance to these officials and discussed them at the exit conference held on April 7, 2011. Hospital officials agreed with Finding A and the related recommendation, but disagreed with Finding B. They said that the insurance company had allocated all of the insurance proceeds. However, the allocation appeared to be inconsistent with FEMA policy, and the Hospital did not provide details on how its insurance carrier determined the insurance settlement, although we requested such information several times during our fieldwork.

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 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 David Kimble, Larry Arnold, and James Miller.

Should you have questions concerning this report, please contact me at (202) 254-4100 or David Kimble at (404) 832-6702.

cc: Administrator, FEMA  
Audit Liaison, FEMA Mississippi Recovery Office  
Audit Liaison, FEMA Region IV  
Audit Liaison, FEMA  
Audit Liaison, DHS

**Schedule of Audited Projects**  
**August 29, 2005 through September 2, 2010**  
**Memorial Hospital at Gulfport, Mississippi**  
**FEMA Disaster No. 1604-DR-MS**

<b>Project</b>	<b>Amount Awarded</b>	<b>Amount Claimed</b>
Original Scope:		
6793	\$ 166,805	\$ 166,805
9473	4,411,148	2,119,786
9938	149,400	149,400
10068	2,088,833	0
10131	853,347	0
<b>Subtotal</b>	<b>\$7,669,533</b>	<b>\$2,435,991</b>
Projects related to Finding B:		
10064	\$ 95,499	\$ 95,499
8125	30,328	30,328
9261	118,088	88,566
10000	279,361	279,361
10003	73,862	73,862
10161	13,343	13,343
<b>Subtotal</b>	<b>\$ 610,481</b>	<b>\$ 580,959</b>
<b>Total</b>	<b>\$8,280,014</b>	<b>\$3,016,950</b>