



Homeland Security

AUDIT TIPS FOR MANAGING DISASTER-RELATED PROJECT COSTS

Department of Homeland Security
Office of Inspector General
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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 and FEMA guidelines 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 established the 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 and 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:

<http://ecfr.gpoaccess.gov>

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.

In addition to 44 CFR, FEMA has several policy documents that will assist you in understanding all aspects of the Public Assistance Program. The website below will give you access to a number of FEMA resources including the following:

- FEMA 321, *Public Assistance Digest* (October 2001)
- FEMA 322, *Public Assistance: Public Assistance Guide* (June 2007)
- FEMA 323, *Public Assistance: Applicant Handbook* (September 1999)
- FEMA 325, *Public Assistance: Debris Management Guide* (June 2007)
- FEMA Disaster Assistance Policy (9500 series policy statements)

<http://www.fema.gov/government/grant/pa/policy.shtm>.

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 the following website:

www.whitehouse.gov/omb/circulars/index.html.

The table below references 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 Joint Field Office (JFO).

| | 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 |
|-----------------------------|--------------------------------|---|--|-------------------------------------|------------------------------|
| Grant Administration | 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; and
- 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 no later than 3 years after the grantee or subgrantee reports that all work has been completed and the final expenditure report has been submitted. However, audits may be done after a majority of the work has been completed and before a grant or subgrant recipient submits its final expenditure report. 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 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 inventory did not support the listing. Therefore, the OIG questioned the \$1 million claim.

C. Duplication of Benefits

Criteria: Government laws and regulations (Stafford Act and 44 CFR 206.191) prohibit 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. Therefore, the OIG questioned the \$200,000 of FEMA funding received for damages covered by insurance.

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. Therefore, the OIG questioned the \$50,000 of excess FEMA funding.

Finding 3: Under a FEMA project, the subgrantee had losses of \$1 million that were fully covered by insurance. However, the subgrantee only pursued and received insurance recoveries of \$500,000. Therefore, the OIG questioned the \$500,000 of FEMA funding received for damages covered by insurance.

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 OIG questioned the \$100,000 of FEMA funds received for activities covered by 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: The subgrantee claimed \$78,348 for the use of bucket trucks based on the FEMA rate of \$24 per hour (3,264.5 hours x \$24 per hour). However, the subgrantee's local 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 claimed \$50,000 for overtime fringe benefits based on a fringe benefit rate of 23.55 percent. However, the rate included the cost of worker's compensation, which is not applicable to overtime. The claim should have been based on a rate of 10 percent, which would have resulted in charges of \$20,000. Therefore, the OIG questioned \$30,000 received by the subgrantee for 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 OIG questioned the inappropriate charges of \$10,000.

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. However, as a general rule, the regular-time salaries and benefits of a subgrantee's permanent employees engaged in debris removal work are not eligible for FEMA assistance. Therefore, the OIG questioned the \$150,000 claimed for regular-time labor.

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: The subgrantee's claim for repairs to its local electrical distribution system 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 were for activities that did not benefit the project.

Finding 2: The subgrantee claimed and received \$500,000 under a FEMA project 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 project's approved scope of work.

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 received \$15,000 of proceeds from the sale of scrap material related to the FEMA project. However, the subgrantee did not credit the FEMA project with the sale proceeds. Therefore, 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 City did not credit the FEMA project for the discounts. Therefore, the OIG questioned \$7,000 of costs under the project.

H. Poor Contracting Practices

Criteria. According to federal regulations (44 CFR 13.36), a subgrantee must comply with the following procurement standards:

- 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 OIG also noted that payments under the three contracts were 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 to the contractor. Due to the improper contracting practices and related weak cost control measures, the OIG 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 account for each distinct FEMA project.
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 is referenced to 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 materials taken from existing inventories for use under FEMA projects are documented by inventory withdrawal and usage records.
8. Do not charge the regular time salary of permanent employees or seasonal employees (whose salaries are contained in annual appropriations) to FEMA debris removal and emergency protective services 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 awarded 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.

Reader Response Sheet

The OIG is interested in the comments and suggestions of those using *Audit Tips for Managing Disaster-Related Project Costs*.

Please take a few minutes to complete this sheet and send it to:

**DHS OIG
Murray Drive, S.E., Building 410
Washington, DC 20528
Attn: ADIG EMO**

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1. The things I liked most about the document were:
 2. The things I liked least about the document were:
 3. In the next update, the things I would like to see added or changed are:
 4. Other comments, suggestions and corrections:

Respondent's Name, Title, Phone Number (optional):

Date of Response _____

Disaster Fraud Hotline

1-866-720-5721

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.

If you have knowledge of fraud, waste, or abuse, or allegations of mismanagement involving disaster relief operations, you can:

- Call the Disaster Fraud Hotline at 1-866-720-5721
- Fax the Disaster Fraud Hotline at 1-225-334-4707
- Email: disaster@leo.gov
- Or write: National Center for Disaster Fraud
Baton Rouge, LA 70821-4909

***Calls can be made anonymously and
confidentially***