

# Department of Homeland Security **Office of Inspector General**

**FEMA Should Recover \$5.3 Million of the \$52.1 Million  
of Public Assistance Grant Funds Awarded to the Bay  
St. Louis Waveland School District in  
Mississippi—Hurricane Katrina**





## OFFICE OF INSPECTOR GENERAL

Department of Homeland Security

Washington, DC 20528 / www.oig.dhs.gov

FEB 25 2014

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

FROM: John V. Kelly  
Assistant Inspector General  
Office of Emergency Management Oversight

SUBJECT: *FEMA Should Recover \$5.3 Million of the \$52.1 Million of Public Assistance Grant Funds Awarded to the Bay St. Louis Waveland School District in Mississippi—Hurricane Katrina*  
FEMA Disaster Number 1604-DR-MS  
Audit Report Number OIG-14-44-D

We audited Public Assistance funds awarded to the Bay St. Louis Waveland School District, Mississippi (District) (FIPS Code 045-00E4A-00). 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 Public Assistance grant award of \$52.1 million from the Mississippi Emergency Management Agency (State), a FEMA grantee, for damages resulting from Hurricane Katrina, which occurred in August 2005. The award provided 100 percent FEMA funding for debris removal activities, emergency protective measures, and permanent repairs to buildings and facilities. The award consisted of 72 large projects and 10 small projects.<sup>1</sup>

We audited 36 projects with awards totaling \$43.8 million. This included a full scope audit of the costs claimed for seven large projects with awards totaling \$27.0 million. We also performed a limited review of 29 additional projects totaling \$16.8 million to determine whether the District (1) completed the projects (3 small projects), (2) followed Federal procurement standards when using contractors to complete work (21 large projects), and (3) received duplicate benefits for some projects from another funding source (5 large projects). See Exhibit, Schedule of Projects Audited and Questioned Costs. The audit covered the period of August 29, 2005, to February 6, 2013, during which the District claimed \$42.0 million in FEMA funds for the 36 projects. At the time of our audit, the District had not completed work on all projects and, therefore, had not submitted a final claim to the State for all project expenditures.

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



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We conducted this performance audit between February 2013 and October 2013 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. To conduct this audit, we applied the statutes, regulations, and FEMA policies and guidelines in effect at the time of the disaster.

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

### RESULTS OF AUDIT

FEMA should recover \$5.3 million of the \$52.1 million in grant funds awarded to the District. Although the District properly accounted for FEMA funds, it did not always expend those funds according to Federal regulations and FEMA guidelines. The District's claim included \$5,333,797 of questionable costs, as follows:

- \$4,405,625 for ineligible contract costs;
- \$746,554 of ineligible project costs; and
- \$181,618 of duplicate benefits.

#### **Finding A: Contracting Procedures**

The District did not comply with Federal procurement requirements when awarding two contracts totaling \$18,837,190:

- \$17,334,772—The District awarded this contract under exigent circumstances using a prohibited cost-plus-percentage-of-costs method of contracting and did not perform a cost or price analysis. We are not questioning the entire contract amount because the work was critical to re-opening the District's schools. However, we do question \$2,903,207 in improper markups on costs.



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- \$1,502,418—The District awarded this contract for nonexigent work without competition and did not take the required affirmative steps to ensure the use of minority firms, women’s business enterprises, and labor surplus area firms when possible. Therefore, we question the \$1,502,418 as ineligible contract costs.

Federal procurement regulations at 44 Code of Federal Regulations (CFR) 13.36 required the District, among other things, to—

- Avoid using prohibited cost-plus-a-percentage-of-cost and percentage-of-construction-cost methods of contracting. (44 CFR 13.36(f)(4))
- Conduct all procurement transactions in a manner providing full and open competition. Noncompetitive procurement is allowable under certain circumstances, one of which is when the public exigency or emergency will not permit a delay resulting from competitive solicitation. (44 CFR 13.36(c)(1) and 44 CFR 13.36(d)(4)(i)(B))
- Take all necessary affirmative steps to ensure the use of minority firms, women’s business enterprises, and labor surplus area firms when possible. (44 CFR 13.36(e))
- Perform a cost or price analysis in connection with every procurement action, including contract modifications, to determine the reasonableness of the proposed contract price. Applicants must perform a cost analysis when adequate price competition is lacking. (44 CFR 13.36(f)(1))

In addition, FEMA’s *Public Assistance Guide* (FEMA 322, October 1999, p. 39) specifies, “Contracts must be of reasonable cost, generally must be competitively bid, and must comply with Federal, State, and local procurement standards.”

Finally, U. S. Federal Acquisition Regulations (FAR Section 16.102) specifically prohibits the use of cost-plus-percentage-of-cost type contracts by U.S. Government agencies.

FEMA may grant exceptions to Federal procurement requirements to subgrantees on a case-by-case basis (44 CFR 13.6(c)).

#### *Cost-Plus-Percentage-of-Cost Contract and Cost Analysis*

The District awarded a prime contractor a prohibited cost-plus-percentage-of-cost contract for work totaling \$17,334,772 under 13 projects. The noncompetitive contract largely included work the District started in September 2005 to expedite opening its schools for the 2005–06 school year. The work included mold remediation; replacement of canopies, exterior windows, doors, and frames; repairs to roofing and flooring; and other various repair items. The



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emergency requirement to get schools opened as quickly as possible after the disaster justified the District's use of a noncompetitive contract. However, Federal regulations prohibit cost-plus-percentage-of-cost contracts because they provide no incentive for contractors to control costs—the more contractors charge, the more profit they make. Under the contract in question, the primary contractor added markups of 10 percent each for overhead and profit on time-and-materials billings for its own employees and on pass-through costs of its subcontractors. The subcontractors performed approximately 68 percent of the contract work.

Additionally, the District could not provide evidence that it conducted a cost or price analysis to determine the reasonableness of the contractor's proposed price. Federal regulation 44 CFR 13.36(f)(1) requires a cost or price analysis be performed in connection with every procurement action. A cost or price analysis decreases the likelihood of unreasonably high or low prices, contractor misinterpretations, and errors in pricing relative to the scope of work.

Because the contract work expedited the opening of the District's schools, we are not questioning the entire contract amount. However, we question the markups for overhead and profit, which totaled about \$2,903,207 because (1) Federal procurement regulations prohibit cost-plus-percentage-of-cost contracts, and (2) FEMA has no assurance that the District paid a fair and reasonable price for the contract work.

*District Response.* District officials disagreed with our finding, saying that no contract types other than cost-plus-percentage-of cost were available to the District because specific scopes of work were impossible to determine as the damage was so extensive. They also said that it was not the District's intention or practice to obtain anything but the most competitive prices for the work needed to recover from the unprecedented disaster.

*Office of Inspector General (OIG) Response.* We disagree with District officials that no other contracting method was available. FEMA's *Public Assistance Guide* (FEMA 322, October 1999, p. 40) states that, when applicants cannot readily develop clear scopes of work, they may use a time-and-materials contract with a not-to-exceed provision. Finally, Federal regulation prohibits cost-plus-percentage-of-cost contracting methods.

#### *Full and Open Competition*

The District did not solicit competitive bids for architectural and engineering (A/E) services valued at \$1,502,418 for permanent repair work under 16 projects. Full and open competition increases the probability of reasonable pricing from the most qualified contractors and helps discourage and prevent favoritism, collusion, fraud, waste, and abuse. District officials also did not take affirmative steps to ensure the use of minority firms, women's business enterprises, and labor surplus area firms when possible. These affirmative steps should include using the services and assistance of the Small Business Administration and the Minority Business Development Agency of the Department of Commerce, and requiring the prime contractor, if



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using subcontracts, to take the affirmative steps listed in Federal regulations 44 CFR 13.36(e)(2)(i) through (v). The District did not give these types of firms the opportunity to bid on the A/E contract.

Instead of seeking competitive bids for the A/E work, the District hired an A/E firm it used before Hurricane Katrina. District officials said they were familiar with the contractor's work and that other A/E firms did not have the capacity to meet their requirements. However, District officials did not provide any evidence to support their assertion that no other qualified A/E firms were available for the project work. Also, the noncompetitive A/E contract did not support work to expedite the opening of the District's schools for the 2005–06 school year. Therefore, we question the \$1,502,418 the District claimed for A/E contract work it awarded under a noncompetitive process (see Exhibit, Schedule of Projects Audited and Questioned Costs).

*District Response.* District officials disagreed with our finding, saying that they entered into the contract under exigent circumstances and that they complied with all applicable procurement procedures.

*OIG Response.* We disagree with District officials that exigent circumstances warranted the use of the no-bid contract. The A/E services were for permanent repair work that began in January 2007, approximately 17 months after the disaster.

#### **Finding B: Ineligible Project Costs**

The District's claim for mold remediation services under Project 8422 included \$746,554 of excessive contract costs. Federal cost principles at 2 CFR 225, Appendix A, Section C.1.a., state that costs under Federal awards must be both reasonable and necessary.<sup>2</sup>

In September 2005, shortly after the disaster, the District awarded a noncompetitive contract for emergency mold remediation for several damaged schools. Exigent circumstances justified the District's use of a noncompetitive contract because the work was to protect the schools from further damage and to get the schools opened as quickly as possible after the disaster. The District initially used a time-and-materials contract because it could not readily determine a clear scope of work required to bring the schools back to their predisaster condition. At FEMA's recommendation, the District later renegotiated the time-and-materials contract into three lump-sum contracts totaling \$7,680,455. The District paid the contractor, and claimed \$7,680,455 for the contract work. FEMA analyzed the \$7,680,455 of costs for reasonableness

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<sup>2</sup> OMB Circular A-87 was moved to 2 CFR 225 effective August 31, 2005.



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using construction cost data and, after disallowing \$48,600 of ineligible costs, awarded the District \$7,631,855 for the contract work.<sup>3</sup>

However, subsequent to FEMA analysis, the contractor submitted a corrected invoice to the District that reduced final costs for the mold remediation work to \$6,885,301, or \$746,554 less than the amount that FEMA awarded the District for the contract work. The contractor corrected the billings because of calculation errors it had made in documenting recovery costs, labor costs, and several other cost elements of the contract. Although FEMA acknowledged the corrected invoice in a narrative included in the project worksheet, it inadvertently used the contractor's original billings to calculate eligible project costs during project closeout. Therefore, we question the \$746,554 as ineligible because that is the difference in amount of FEMA funds that the District received for the mold remediation and what it paid for the mold remediation services.

*District Response.* District officials disagreed with our finding, saying that FEMA was accurate in its review of the contract and invoices and that FEMA awarded the proper costs for the work. They also said that the District has no information to support that the costs were excessive and that they believe the costs are reasonable.

*OIG Response.* We disagree that District officials did not have information to support that the costs were excessive. As previously discussed, the District's contractor submitted a revised invoice to the District in May 2006 that reduced final contracts by \$746,554. Therefore, the District should have been aware that the amount of funding FEMA awarded the District under the project exceeded the total costs the contractor billed the District for project work.

**Finding C: Duplicate Benefits**

The District received \$181,618 of duplicate benefits for the replacement of damaged equipment and books. Section 312 of the *Robert T. Stafford Disaster Relief and Emergency Assistance Act*, as amended, states that no entity will receive assistance for any loss for which it has already received financial assistance from any other program, from insurance, or from any other source.

The District received \$181,618 of FEMA funding under several projects to replace damaged books and equipment. However, the District replaced the damaged books and equipment using donations it received from various third parties. The value of these donations totaled \$181,618; \$164,400 in cash and books, and equipment valued at \$17,218. For example, under Projects 7802 and 8058 (Waveland Elementary and North Bay Elementary schools), FEMA awarded the

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<sup>3</sup> FEMA calculated reasonable costs using RSMeans. RS Means, a product line of Reed Construction Data, is a supplier of construction cost information for North America. RSMeans provides accurate and up-to-date cost information used to project the cost of building construction and renovation projects.



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District \$36,429 for damaged refrigerators and kitchen warmers. However, the District received two refrigerators and two warmers valued at \$17,218 from private donors, which replaced the damaged equipment. Therefore, we question the \$181,618 of duplicate benefits as table 1 identifies.

**Table 1. Questioned Costs for Duplicate Benefits**

Project Number	School	Donated Item	Value of Donation	Amount Questioned
7802	Waveland Elementary	Refrigerator and warmer	\$ 8,377	\$ 8,377
8058	North Bay Elementary	Refrigerator and warmer	8,841	8,841
8347	Bay High School	Cash to replace books	75,000	75,000
8350	Waveland Elementary	Cash to replace books	60,000	60,000
8350	Waveland Elementary	Library books	17,000	17,000
8373	North Bay Elementary	Cash to replace books	12,400	12,400
<b>Totals</b>			<b>\$181,618</b>	<b>\$181,618</b>

*District Response.* District officials disagreed with our finding, saying that they were not aware of any private donations to replace damaged items that FEMA funded.

*OIG Response.* We disagree with District officials. As explained in the finding, we specifically identified several items totaling \$181,618 that FEMA funded for which the District replaced with cash and other items it received from private donors.

**Finding D: Grant Management**

The nature and extent of ineligible costs we identified demonstrate that the State should have done a better job of reviewing the District’s contracting methods and project costs. Federal regulations require grantees to (1) ensure that subgrantees are aware of Federal regulations, (2) manage the day-to-day operations of subgrant activity, and (3) monitor subgrant activity to ensure compliance.<sup>4</sup> Therefore, we recommend that FEMA remind the State of its grant management responsibilities for monitoring and reviewing costs that subgrantees claim.

**RECOMMENDATIONS**

We recommend that the Regional Administrator, FEMA Region IV:

**Recommendation #1:** Disallow \$4,405,625 of ineligible costs the District claimed for contracts that it did not procure in accordance with Federal requirements, unless FEMA decides to grant an exception for all or part of the costs as provided for in 44 CFR 13.6(c) and Section 705(c) of

<sup>4</sup> 44 CFR 13.37(a)(2) and 44 CFR 13.40(a).





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the *Robert T. Stafford Disaster Relief and Emergency Assistance Act*, as amended, and determines the costs are reasonable (finding A).

**Recommendation #2:** Instruct the State to remind subgrantees of their responsibility to comply with Federal procurement regulations and FEMA guidelines when acquiring goods and services under the FEMA award (finding A).

**Recommendation #3:** Disallow \$746,554 for ineligible contract costs the District received for mold remediation services under Project 8422 (finding B).

**Recommendation #4:** Disallow \$181,618 of duplicate benefits the District received from third-party donors for damaged items (finding C).

**Recommendation #5:** Reemphasize to the State and FEMA Region IV Public Assistance personnel their responsibility to adequately review costs subgrantees claim for compliance with Federal regulations and FEMA guidelines (finding D).

### DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOWUP

We discussed the results of our audit with the District, State, and FEMA officials during our audit. We also provided a draft report in advance to these officials and discussed it at the exit conference held on October 1, 2013. District officials disagreed with our findings and recommendations. We incorporated their comments, as appropriate, into the body of this 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 the contact information for responsible parties and any other supporting documentation necessary to inform us about the current status of the recommendation. Until we receive and evaluate your response, we will consider the recommendations open and unresolved.

Consistent with our responsibility under the *Inspector General Act*, we will provide copies of our report to appropriate congressional committees with oversight and appropriation responsibility over the Department of Homeland Security. We will post the report on our website for public dissemination.

Major contributors to this report are David Kimble, Director; Larry Arnold, Audit Manager; Katrina Griffin, Auditor-in-Charge; Alicia Lewis, Auditor; and Sharonda Toney, Auditor.



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Please call me with any questions at (202) 254-4100, or your staff may contact David Kimble, Director, Eastern Regional Office, at (404) 832-6702.



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Exhibit

**Schedule of Projects Audited and Questioned Costs**

Project	Project Amount Awarded	Amount Claimed	Questioned Cost				Total Amount Questioned
			Cost Plus Percentage of Cost Contract and Cost Analysis (Finding A)	Full and Open Competition (Finding A)	Ineligible Project Cost (Finding B)	Duplicate Benefits (Finding C)	
<b>Projects Included in Full Scope:</b>							
930	\$ 5,789,716	\$ 6,596,590	\$1,211,159	\$ 108,700	\$ 0	\$ 0	\$1,319,859
932	900,669	900,669	0	0	0	0	0
6185	4,466,343	4,466,343	0	3,928	0	0	3,928
7480	1,774,933	1,774,933	0	1,991	0	0	1,991
8422	7,631,855	7,631,855	0	0	746,554	0	746,554
9470	2,748,340	199,304	0	0	0	0	0
11157	3,652,145	3,652,145	0	0	0	0	0
<b>Subtotal</b>	<b>\$26,964,001</b>	<b>\$25,221,839</b>	<b>\$1,211,159</b>	<b>\$ 114,619</b>	<b>\$746,554</b>	<b>\$ 0</b>	<b>\$2,072,332</b>
<b>Projects Reviewed for Work Completion:</b>							
8651	\$18,632	\$15,471	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
9083	18,653	18,653	0	0	0	0	0
9303	17,602	28,000	0	0	0	0	0
<b>Subtotal</b>	<b>\$ 54,887</b>	<b>\$ 62,124</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Projects Reviewed for Federal Contracting Requirements:</b>							
5886	\$165,072	\$971,060	\$141,862	\$12,219	\$ 0	\$ 0	\$154,081
5913	237,810	237,810	37,031	3,670	0	0	40,701
7483	1,057,147	1,057,147	0	869	0	0	869
7493	1,560,739	1,560,739	0	1,493	0	0	1,493
7495	1,488,131	1,488,131	0	1,646	0	0	1,646
7563	1,363,967	1,363,967	0	661	0	0	661
8056	144,027	154,645	0	0	0	0	0
8297	69,235	69,235	0	560,213	0	0	560,213
8298	84,363	84,363	0	624,006	0	0	624,006
8318	117,135	117,135	0	0	0	0	0
9061	958,527	958,527	160,533	0	0	0	160,533
9305	958,890	1,136,407	190,324	0	0	0	190,324
9307	1,741,066	1,857,460	311,085	0	0	0	311,085
9316	619,238	835,321	139,899	0	0	0	139,899
9368	520,312	620,442	103,911	0	0	0	103,911
9395	1,058,776	1,530,895	256,392	0	0	0	256,392
9397	1,045,405	538,508	90,189	0	0	0	90,189
9427	589,665	669,988	112,209	0	0	0	112,209
9680	310,577	272,117	0	183,022	0	0	183,022
9681	608,532	415,504	69,588	0	0	0	69,588
9682	545,759	471,852	79,025	0	0	0	79,025
<b>Subtotal</b>	<b>\$15,244,373</b>	<b>\$16,411,253</b>	<b>\$1,692,048</b>	<b>\$1,387,799</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$3,079,847</b>
<b>Projects Reviewed for Duplicate Benefits:</b>							
7802	\$189,192	\$ 0	\$ 0	\$ 0	\$ 0	\$8,377	\$8,377
8058	191,291	0	0	0	0	8,841	8,841
8347	548,121	101,808	0	0	0	75,000	75,000
8350	424,099	72,142	0	0	0	77,000	77,000
8373	197,527	167,481	0	0	0	12,400	12,400
<b>Subtotal</b>	<b>\$ 1,550,230</b>	<b>\$ 341,431</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$181,618</b>	<b>\$ 181,618</b>
<b>Totals</b>	<b>\$43,813,491</b>	<b>\$42,036,647</b>	<b>\$2,903,207</b>	<b>\$1,502,418</b>	<b>\$746,554</b>	<b>\$181,618</b>	<b>\$5,333,797</b>



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