

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

FEMA Public Assistance Grant
Funds Awarded to Paso Robles Joint
Unified School District, California

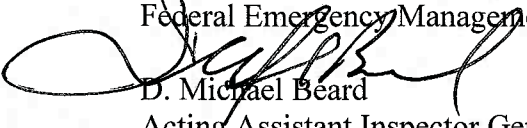




Homeland Security

FEB - 9 2012

MEMORANDUM FOR: Nancy Ward
Regional Administrator, Region IX
Federal Emergency Management Agency

FROM: 
D. Michael Beard
Acting Assistant Inspector General
Office of Emergency Management Oversight

SUBJECT: *FEMA Public Assistance Grant Funds Awarded to
Paso Robles Joint Unified School District, California*
FEMA Disaster Number 1505-DR-CA
Audit Report Number DS-12-03

We audited public assistance (PA) grant funds awarded to the Paso Robles Joint Unified School District, California (District), Public Assistance Identification Number 079-UHTF4-00. Our audit objective was to determine whether the District accounted for and expended Federal Emergency Management Agency (FEMA) grant funds according to federal regulations and FEMA guidelines.

The District received a PA award of \$17.8 million from the California Emergency Management Agency (Cal EMA),¹ a FEMA grantee, for emergency protective measures and permanent repairs to facilities damaged as a result of the San Simeon earthquake of December 22, 2003.² The award provided 75% FEMA funding for 7 large and 14 small projects.³ The audit covered the period from December 22, 2003, to August 11, 2011. We audited project charges for all seven large projects and two small projects, totaling \$19.1 million (see Exhibit, Schedule of Projects Audited).⁴

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 applying the statutes, regulations, and FEMA policies and guidelines in effect at the time of the disaster.

¹ At the time of the disaster, the grantee's name was the Governor's Office of Emergency Services, which became a part of Cal EMA on January 1, 2009.

² The 108th Congress' Conference Report from the House of Representatives (accompanying H.R. 4837) provided the City of Paso Robles, CA, additional funding for disaster relief activities as a result of the damages sustained in the 2003 San Simeon earthquake.

³ Federal regulations in effect at the time of the disaster set the large project threshold at \$54,100.

⁴ The \$19.1 million referenced here represents the total dollar amount of project charges audited. Although the District was awarded \$17.8 million from Cal EMA, it plans to claim \$19.1 million in project-related costs due to cost overruns.

We discussed issues related to this audit with FEMA, Cal EMA, and District officials; reviewed judgmentally selected project costs (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 District’s method of accounting for disaster-related costs and its procurement policies and procedures.

RESULTS OF AUDIT

Of the \$19,074,741 in project charges we reviewed, District officials did not expend or account for \$13,106,345 according to federal regulations and FEMA guidelines (see table 1).

Table 1: Summary of Questioned Costs			
Finding	Subject	Questioned Costs	Questioned Costs Included in Other Findings
A	Erroneous Repair vs. Replacement Decision	\$12,958,864	
B	Improper Procurement		\$2,736,887
C	FEMA Not Compensated for Real Property	145,481	
D	Unsupported Costs	2,000	
TOTAL		\$13,106,345	

Finding A: Erroneous Repair vs. Replacement Decision

FEMA erroneously funded the replacement of the Flamson Middle School building (building) for Project 245, entailing \$12,958,864 in improper (excessive) funding. This occurred because FEMA officials did not use complete and correct information when deciding to replace, rather than repair, the building.

Code of Federal Regulations, Title 44 (44 CFR), and FEMA guidelines stipulate that—

- A facility is considered repairable when the disaster damages do not exceed 50% of the cost of replacing the facility to its predisaster condition, and it is feasible to repair the facility so that it can perform the function for which it was being used as well as it did immediately prior to the disaster. If a damaged facility is not repairable ..., approved restorative work may include replacement of the facility. (44 CFR 206.226(f)(1-2))
- Replacement costs are eligible if repair costs are equal to or greater than 50% of the cost to replace a facility. Replacement costs include the costs for all work necessary to provide a new facility of the same size or design capacity and function as the damaged facility in accordance with current codes and standards. (FEMA 322, *Public Assistance Guide*, October 1999, p. 29)

FEMA officials did not meet these federal criteria—referred to as the 50 Percent Rule—in calculating disaster assistance based on the estimated repair costs relative to the estimated replacement cost of

the building. In calculating whether to replace or repair the building,⁵ FEMA accepted the estimated repair cost of \$4,697,088⁶ and estimated replacement costs at \$7,582,734.⁷ Thus, FEMA determined that it was more appropriate to replace the building than to repair it because the estimated repair costs were 62% of the estimated replacement cost—well over 50%. However, FEMA officials, relying on District-provided documentation, used incorrect square footage in their calculations because they did not include codes and standards (and applicable costs per square foot) in determining this percentage. If FEMA had correctly applied the 50 Percent Rule, the decision would have been to fund the cost to repair the existing building (figure 1) to its predisaster condition, rather than to fund 100% of the cost to replace it with a new building (figure 2).



Figure 1: Previous Flamson Middle School Building (March 2004)
Source: FEMA



Figure 2: New Flamson Middle School Building (October 2010)
Source: Dave Skinner Photography

⁵ FEMA typically performs the repair vs. replacement calculation by comparing the estimated sum of (base) construction costs (i.e., Part A costs) of each of the repair and replacement scenarios using the Cost Estimating Format (CEF)—FEMA’s uniform method of estimating costs incurred across the entire spectrum of eligible work for large projects (see *CEF for Large Project Instructional Guide, Version 2*, p. 20). However, in this instance, FEMA did not limit its comparison to base costs because specific congressional legislation directed that FEMA use the cost estimate developed by a general contractor (see notes 2 and 6), which included costs in addition to base costs. Consequently, to ensure consistency with FEMA’s methodology for determining repair vs. replacement eligibility (which incorporated more than base costs), we likewise considered those additional costs that FEMA incorporated into its calculations when performing our own analyses (e.g., costs per square foot).

⁶ This estimate was based on the 108th Congress’ Conference Report, which ensured funding for—and agreement with—general contractor earthquake repair estimates with regard to the damages sustained at Flamson Middle School (see note 2).

⁷ This amount of \$7,582,734 does not include \$762,600 in demolition costs for the existing building, which FEMA estimated and initially funded at \$8,345,334. FEMA’s estimated replacement costs for the building did not include demolition per FEMA guidelines (FEMA 322, *Public Assistance Guide*, October 1999, p. 29).

The cost information FEMA used—derived from the building’s original plans and District sources—was based on the assumptions that the replacement building would consist of 36,000 square feet and would take approximately 25 months to complete. However, the replacement building is more than one third larger—48,655 square feet—and cost more than twice as much to construct as originally estimated—\$17,655,952. FEMA did not consider the additional square footage required by codes and standards (such as larger classrooms, hallways, etc.), which necessitated construction of a larger building, nor the amount of time needed to complete the project (which increased costs).

Further, Cal EMA and FEMA officials should have reevaluated this project before obligating the \$7,919,264 in additional funding beyond the \$8,345,334 initial estimate. As early as 2005, District officials recognized that FEMA’s information was incorrect, and they eventually requested, through Cal EMA, that FEMA revise its calculations and obligate additional funding to accommodate—

- The actual size of the building: 48,655 vs. 36,000 square feet, based on the inclusion of codes and standards; and
- Additional costs per square foot: \$97 vs. \$275, based on project delays.

As a result, we concluded that FEMA allowed for the demolition of a building—which the District proceeded with replacing—that only should have been restored to its predisaster condition.

Therefore, we questioned \$12,958,864 for Project 245: all project costs (\$17,655,952) less the accepted cost estimate for repair (\$4,697,088).

FEMA and District officials agreed with our finding that FEMA’s decision to replace the building was based on incorrect (and incomplete) information. However, both parties believe that replacement was nevertheless warranted. District officials believe that repairing the original building was not a viable option due to the extent of damage it incurred, regardless of the repair versus replacement calculations. However, the engineering and general contractor’s assessment indicated that the building could be repaired.

FEMA officials believe that their calculations, once corrected, would nevertheless justify the replacement of the building, and that the majority of the additional square footage may be the result of building improvements and not codes and standards.⁸ FEMA officials acknowledged that this contradicts District officials’ position that the total additional square footage of the building was based on codes and standards. Our analysis, based directly on the District’s source documentation relating to architectural determinations, sustains the position that the increased square footage was predominantly a result of codes and standards. Our review of various improvements to the building (e.g., skylights) generally reveals a limited impact on square footage.

⁸ FEMA officials question whether the District incorporated (non-code/standard based) improvements into the building’s design (which resulted in additional square footage), thus making this project an improved project. Consequently, FEMA officials contend that they must re-review the charges associated with the project and disallow any ineligible costs. We did not evaluate/question this project as an improved project, however, because (1) the District did not follow the process for an improved project—including obtaining review by FEMA prior to construction, as well as prior approval by the Grantee, and (2) our analyses support that the fundamental bases on which this project was approved (for replacement) were incorrect, thus rendering the entire project ineligible and the improved project aspect moot.

Finding B: Improper Procurement

District officials improperly procured three contracts worth \$2.7 million (see table 2) for architectural and engineering services, construction testing services, and construction inspections for Project 245. The District did not use full and open competition, thus FEMA has no assurance that the District paid reasonable prices.

Federal procurement standards require the District to—

- Perform procurement transactions in a manner providing full and open competition except under certain circumstances when procurement by noncompetitive proposal is permitted. 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. (44 CFR 13.36(c)(1) and (d)(4)(i)(B))
- Take all necessary affirmative steps to assure that minority firms, women’s business enterprises, and labor surplus area firms are used when possible. (44 CFR 13.36(e)(1))
- Maintain records sufficient to detail the significant history of the procurement, including the rationale for the method of procurement, basis for contractor selection, and basis for the contract price. (44 CFR 13.36(b)(9))
- Prepare a cost or price analysis in connection with every procurement action, including contract modifications. (44 CFR 13.36(f)(1))
- Include mandatory contract provisions detailed in 44 CFR 13.36(i).

In addition, FEMA’s *Public Assistance Guide* (FEMA 322, *Public Assistance Guide*, October 1999, p. 39) specifies that—

- Contracts must be of reasonable cost, generally must be competed, and must comply with federal, state, and local procurement standards.
- Noncompetitive proposals should be used only when the award of a contract is not feasible under small purchase procedures, sealed bids, or competitive proposals, and one of the following circumstances applies: (1) the item is available only from a single source, (2) there is an emergency requirement that will not permit a delay, (3) FEMA authorizes noncompetitive proposals, or (4) solicitation from a number of sources has been attempted and competition is determined to be inadequate.

District officials did not solicit competitive bids in awarding contracts and services for Project 245. Further, they could not reasonably justify why full and open competition did not occur. For example, federal regulations allow for flexible (e.g., noncompetitive) contracting under exigent circumstances. However, exigency was not a factor for this work; the work was permanent in nature and not emergency-oriented. For Project 245, District officials awarded one of the contracts to the same contractor they employed before the disaster, and (for the other two contracts) to familiar contractors that were located near the District.

Full and open competition increases the probability of reasonable pricing from the most qualified contractors and allows the opportunity for minority firms, women’s business enterprises, and labor surplus area firms to participate in federally funded work. Further, full and open competition helps discourage and prevent favoritism, collusion, fraud, waste, and abuse.

In addition to awarding the contracts noncompetitively, District officials did not always have formal written contracts, could not identify exactly what was included in the contractors’ rates, and did not follow other mandatory federal procurement criteria (see table 2). Specifically, they did not (1) take all necessary affirmative steps to assure that minority firms, women’s business enterprises, and labor enterprise surplus area firms were used when possible; (2) maintain records including the rationale why the procurement was not competed; (3) prepare a cost or price analysis for each procurement action; and (4) include the required provisions within their contracts.

Contract / Work Performed	Competitively Procured?	Took All Necessary Affirmative Steps?	Maintained Sufficient Procurement Records?	Prepared Cost/Price Analyses?	Included Mandatory Contract Provisions?	Questioned Contract Costs
A&E	No	No	No	No	No	\$1,889,203
Construction Testing	No	No	No	No	No	424,388
Construction Inspections	No	No	No	No	No	423,296
TOTAL						\$2,736,887

Therefore, we questioned \$2,736,887 in ineligible costs associated with Project 245. Because this amount was already questioned in finding A, we did not separately recommend disallowance per this finding. District officials agreed that they did not compete the contracts associated with this project, although the A&E contractor was “prequalified” by the District—5 years prior to the disaster—to perform work for the District. This does not, and cannot, excuse the District from the requirement to comply with federal procurement rules and regulations applicable to federally awarded (FEMA PA) funds.

Finding C: FEMA Not Compensated for Real Property

District officials kept three modular buildings beyond the time they were needed for disaster-related purposes, without compensating FEMA for the applicable fair market value.

Federal real property regulations and rules outlined in 44 CFR 13.31 and the Office of Management and Budget Circular A-110 (Section 32) stipulate that real property acquired under a grant or subgrant shall only be used for the originally authorized purposes.⁹ When the buildings were no longer needed for disaster-related purposes, the District should have requested disposition instructions from FEMA, and FEMA would have—

⁹ Criteria relevant to this finding relate to real property. Although modular buildings, in some circumstances, may be considered equipment, we consider (and FEMA officials consider) these particular assets real property.

- Permitted the District to retain title without further obligation to FEMA after it compensated FEMA for that percentage of the current fair market value of the property attributable to the federal participation in the project;
- Directed the District to sell the property and pay the federal government for that percentage of the current fair market value of the property attributable to the federal participation in the project; or
- Instructed the District to transfer title to the property to FEMA or to an eligible third party, whereby the District would have been entitled to compensation for its attributable percentage of the current fair market value of the property.

Under Project 175, the District purchased three modular buildings totaling \$193,974 for temporary relocation while the Flamson Middle School replacement building was under construction. Although these modular buildings could no longer be used for disaster-related purposes as of June 30, 2010, when construction of the Flamson Middle School was complete, the District continued to use them for its own, nondisaster-related use, without notifying FEMA or compensating FEMA the applicable fair market value of these buildings for the usage during the nondisaster-related period.

According to the calculations by the manufacturer for these specific buildings, the current fair market value for each modular building is higher than the original purchase price, due to appreciation and market conditions. However, the District attested that the current market value is negligible. To determine the actual fair market value, we attempted to locate an impartial resource that would provide such information (such as property tax records on the buildings or a commercial value index). The data were not available or were nonexistent. Consequently, we spoke with FEMA officials to determine their methodology for calculating monetary values absent fair market value information. They told us that a general practice of theirs is to use the net book value as a substitute for the fair market value when the fair market value cannot be determined.¹⁰

Because the District recorded these modular buildings as fixed assets in its accounting records, using a 25-year schedule of depreciation, we calculated that the net book value from April 12, 2004 (when the District began using the buildings) until June 30, 2010 (when the buildings were no longer needed for disaster-related purposes) is \$145,481,¹¹ as illustrated in table 3:

Modular Building	Purchase Price	District's Depreciation Schedule	Start of Use	End of Use	Depreciation	Net Book Values / Questioned Costs
Office	\$57,280	25 Years	4/12/2004	6/30/2010	\$14,320	\$42,960
Office	57,280	25 Years	4/12/2004	6/30/2010	14,320	42,960
Library	79,414	25 Years	4/12/2004	6/30/2010	19,853	59,561
TOTAL	\$193,974				\$48,493	\$145,481

¹⁰ The net book value of an asset amounts to its original cost (its book value) less the cumulative depreciation.

¹¹ The total net book value we questioned amounts to the total purchase price of \$193,974 less the depreciation of \$48,493.

Therefore, in the absence of current fair market values, we question \$145,481 in ineligible costs for the three buildings. District officials agreed with this finding, stating that they used the modular buildings for nondisaster-related purposes. However, they believe that the buildings currently have negligible market value, and that they should therefore be relieved from the requirement of compensating FEMA for these costs.

Finding D: Unsupported Costs

The District charged \$2,000 in unsupported costs for Project 175.

Federal regulations, rules, and FEMA guidelines require that—

- Costs be adequately documented to be allowable under a federal award (OMB Circular A-87, Revised; Attachment A, section C.1 (j)); and
- Subgrantees have fiscal controls and accounting procedures that permit the tracing of funds to a level of expenditure adequate to establish that such funds are not used in violation of applicable laws. (44 CFR 13.20(a)(2))

The District claimed project costs of \$8,175 rather than the actual payment to the vendor of \$6,175. Because the amount claimed exceeded the payment to the vendor, we questioned the unsupported costs of \$2,000. District officials agreed with this finding.

RECOMMENDATIONS

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

Recommendation #1: Disallow \$12,958,864 (federal share \$9,719,148) in ineligible replacement costs charged to Project 245 (finding A).

Recommendation #2: Establish policies and procedures that require FEMA personnel to review and revise project cost estimates calculated within Part A of the *Cost Estimating Format* for repair vs. replacement eligibility determinations if additional information becomes available prior to construction (finding A).

Recommendation #3: Disallow \$2,736,887 (federal share \$2,052,665) in ineligible procurement costs charged to Project 245 as part of the total amount recommended for disallowance in finding A (finding B).

Recommendation #4: Either (1) disallow the net book value of \$145,481 (federal share \$109,111) for Project 175 as a result of noncompliance with federal rules, regulations, and guidelines requiring FEMA to be compensated for the applicable value of the three modular buildings from the time they were no longer needed for disaster-related purposes; or (2) timely determine the fair market value of the modular buildings to determine the monetary value owed FEMA and proceed to expeditiously recoup that amount of funding (finding C).

Recommendation #5: Disallow \$2,000 (federal share \$1,500) in unsupported costs for Project 175 (finding D).

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOWUP

We discussed the results of this audit with District 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 September 27, 2011, and FEMA on October 21, 2011. We discussed these findings and recommendations at exit conferences held with Cal EMA and District officials on October 4, 2011, and with FEMA on October 27, 2011. District officials disagreed with findings A, B, and C and agreed with finding D. FEMA disagreed with finding A, and agreed with findings B, C, and D. Cal EMA officials withheld 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 responsible parties and any other supporting documentation necessary to inform us about the current status of each 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. Significant contributors to this report were Humberto Melara, Devin Polster, Ravi Anand, and Montul Long.

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

cc: Administrator, FEMA
Audit Liaison, FEMA Region IX
Audit Liaison, FEMA (Job Code G-11-018)
Audit Liaison, DHS

EXHIBIT

Schedule of Projects Audited
December 22, 2003, to August 11, 2011
Paso Robles Joint Unified School District, California
FEMA Disaster Number 1505-DR-CA

Project No.	Project Award Amount	Project Charges	Costs Questioned				Total: Findings (A–D)
			Erroneous Repair vs. Replacement Decision (Finding A)	Improper Procurement (Finding B)	FEMA Not Compensated for Real Property (Finding C)	Unsupported Costs (Finding D)	
175	\$675,632	\$675,632			\$145,481	\$2,000	\$147,481
190*	38,569	32,798					
193*	30,404	32,293 ¹²					
208	85,363	85,363					
214	125,414	125,414					
220	110,477	110,477					
234	235,922	235,922					
236	120,890	120,890					
245	16,264,598	17,655,952 ¹³	\$12,958,864	\$2,736,887			\$12,958,864
Total	\$17,687,269	\$19,074,741	\$12,958,864	\$2,736,887¹⁴	\$145,481	\$2,000	\$13,106,345

* Small Project

¹² There was no net small project overrun; thus, District officials did not claim a net small project overrun.

¹³ District officials completed Project 245 and charged \$17,655,952 to the project. They intend to claim \$1,391,354 in (ineligible) cost overruns beyond the FEMA-obligated award (\$17,655,952 less \$16,264,598).

¹⁴ To avoid duplication, this amount—included in the questioned costs recommended for disallowance in finding A—is not (again) included in the total questioned costs.

ADDITIONAL INFORMATION AND COPIES

To obtain additional copies of this report, please call the Office of Inspector General (OIG) at (202)254-4100, fax your request to (202)254-4305, or e-mail your request to our OIG Office of Public Affairs at DHS-OIG.OfficePublicAffairs@dhs.gov. For additional information, visit our OIG website at www.oig.dhs.gov or follow us on Twitter @dhsoig.

OIG HOTLINE

To report alleged fraud, waste, abuse or mismanagement, or any other kind of criminal or noncriminal misconduct relative to Department of Homeland Security programs and operations:

- Call our Hotline at 1-800-323-8603
- Fax the complaint directly to us at (202)254-4292
- E-mail us at DHSOIGHOTLINE@dhs.gov; or
- Write to us at:
DHS Office of Inspector General/MAIL STOP 2600,
Attention: Office of Investigation - Hotline,
245 Murray Drive SW, Building 410
Washington, DC 20528

The OIG seeks to protect the identity of each writer and caller.