




Homeland Security

July 10, 2009

MEMORANDUM FOR: Nancy Ward
Regional Administrator
FEMA Region IX

FROM: 
Robert J. Lastrico
Western Regional Director

SUBJECT: *City of Los Angeles Department of Water & Power*
Los Angeles, California
Public Assistance Identification Number 037-44000-16
FEMA Disaster Number 1577-DR-CA
Audit Report Number DS-09-09

The Office of Inspector General audited public assistance funds awarded to the City of Los Angeles Department of Water & Power, Los Angeles, California (Department). The objective of the audit was to determine whether the Department expended and accounted for Federal Emergency Management Agency (FEMA) funds according to federal regulations and FEMA guidelines.

The Department received a public assistance subgrant award of \$11.2 million from the California Office of Emergency Services (OES is now the California Emergency Management Agency - CalEMA), a FEMA grantee, for debris removal, emergency protective measures, and permanent repairs to facilities damaged by severe storms beginning on December 27, 2004, and continuing through January 11, 2005. The audit covered the period December 27, 2004, to January 23, 2009, and included a review of five completed large projects¹ with a total project worksheet (PW) approved amount of \$6.65 million (see Exhibit). At the conclusion of our fieldwork, the Department had not submitted a final claim or requested closure of the completed projects but had received \$3.4 million in partial reimbursements for the \$7.2 million in costs it planned to claim under the five projects. As such, FEMA had not performed a final inspection and closeout of the projects.

We conducted this performance audit under the authority of *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 on our audit objective. The evidence obtained during the audit provides a reasonable basis for our findings and conclusions based on our audit objective.

¹ Federal regulations in effect at the time of the disaster set the large project threshold at \$55,500.

We interviewed FEMA, CalEMA, and Department officials, reviewed judgmentally selected samples of cost documentation to support invoices and personnel charges, and performed other procedures considered necessary to accomplish our objective. We did not assess the adequacy of the Department’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 Department’s method of accounting for disaster-related costs.

RESULTS OF AUDIT

Of the \$7.2 million in costs that the Department intends to claim for the five projects, \$2,632,125 is not in compliance with criteria required for federal reimbursement (the federal share of the costs questioned in this report total \$1,974,094). The table below lists the areas in which we questioned amounts to be claimed by the Department.

Finding	Subject	Amount Questioned
A	Improved Project Costs	\$2,169,000
B	Costs Covered by FEMA's Statutory Administrative Allowance	178,385
C	Accounting Records	218,230
D	Project Cost Eligibility	37,270
E	Costs Based on Equipment Rates	17,493
F	Costs for Fringe Benefits	11,747
Total		\$2,632,125

In addition, FEMA should deobligate \$2,105,746 in unneeded project funding for three of the five projects reviewed (Finding G). Also, as noted in the “Other Matters” section of this report, the eligibility and supportability of \$657,943 in force account labor and \$378,903 in force account equipment costs could not be determined and the issue is being referred to FEMA for resolution.

Finding A – Improved Project Costs

The Department received \$331,000 in project funding under PW 3016 for repairs to 230 linear feet (LF) of disaster damaged storm drainpipe. The Department completed the FEMA approved repairs and also performed additional improvements to its storm drainpipe system. The improvements consisted of repairs to an additional 560 LF (total of 790 LF) of storm drainpipe and lining the 790 LF of pipe with reinforced concrete. Final project costs totaled \$2,500,000. Since the additional work completed by the Department represented repairs beyond those required to restore the storm drainpipe to pre-disaster condition, improvements totaling \$2,169,000 (\$2,500,000 less \$331,000) are questionable.

According to Title 44, *Code of Federal Regulations*, Section 206.203(d) [44 CFR 206.203(d)], if a subgrantee desires to make improvements, but still restore the predisaster function of a damaged facility, the grantee's approval must be obtained. Also, federal funding for improved projects is limited to the federal share of the approved estimate of these eligible costs. In addition, 44 CFR 206.223 provides that an item of work must be required as a result of a major disaster to be eligible for financial assistance. Furthermore, during the execution of approved work, when a subgrantee finds that the actual project costs exceed the approved project estimates, 44 CFR 206.204(e) requires that the Department (subgrantee) evaluate each cost overrun, and when justified, request (through

the grantee) additional funding from FEMA. This request must be submitted to FEMA during the execution of approved work and before the project is completed.²

The Department did not obtain approval from either FEMA or CalEMA for the revised scope of work and for the additional project costs of \$2,169,000. Project records indicated that early in the project development phase, the Department requested funding for certain project improvements, but FEMA denied the request because the work was not disaster related. Department officials explained that subsequent to completing the improved project, in a letter dated August 8, 2008, they notified CalEMA about the project scope changes and increased costs. CalEMA had not responded to the Department's request for additional funding for the project and the Department planned to file a formal appeal if federal funding is denied.

Finding B – Costs Covered by FEMA's Statutory Administrative Allowance

The direct costs recorded by the Department for the three projects identified below included \$178,385 in charges covered by FEMA's statutory administrative allowance.

Project Number	Indirect/Overhead Charges
2407	\$90,449
2912	60,126
951	27,810
Total	\$178,385

According to 44 CFR 207.9(b)(2)³, the Department may receive funding to cover the necessary costs of requesting, obtaining, and administering its public assistance subgrants. The amount of funding is based on a percentage of net eligible costs under the Stafford Act. Under 44 CFR 207.9(c)(2)⁴, a subgrantee's indirect costs are not separately eligible for reimbursement because the percentage allowance in paragraph (b)(2) covers all necessary costs of requesting, obtaining, and administering federal assistance. When a disaster applicant's costs to administer federal assistance exceed FEMA's statutory administrative allowance, the excess costs cannot be claimed as direct project costs.

For all three projects, Department accounting records included overhead charges totaling \$145,942 for material handling and for managing department owned transportation equipment. In addition, the Department included a 25% equipment rental mark-up charge of \$32,443 under project 2912 to recoup the administrative costs it incurred in renting the equipment.

Since federal regulations limit the reimbursement of a subgrantee's administrative costs to funding provided by the percentage allowance, the Department's indirect costs are not separately eligible for reimbursement. Department officials agreed that the charges identified in the table above were administrative in nature and would not be submitted as direct costs in the Department's final claim.

² See 44 CFR 13.30(c)(2) and 44 CFR 13.30(d)(1).

³ This provision, which went into effect on November 13, 2007, includes provisions on administrative and management costs that were previously described in 44 CFR 206.228(a)(2)(ii) and 206.439(b)(1)(ii).

⁴ This provision on eligible costs went into effect on November 13, 2007 and was previously described in 44 CFR 206.439(c)(2).

Finding C –Accounting Records

Department records included \$173,613 in accounting errors for project 2407 and \$44,617 in unsupported contract costs for project 2985. According to 44 CFR 13.20(b)(2), the Department is required to maintain accounting records that identify how FEMA funds are used. In addition, 44 CFR 13.20(b)(6) requires that accounting records be supported by source documents such as cancelled checks, paid bills, and contracts.

- For project 2407, the Department charged \$173,613 in material costs belonging to another FEMA funded project (PW 951).
- Project records did not include support for a \$44,617 payment to a contractor under project 2985. While the records identified that a contractor was paid \$253,030 for completing disaster work, only \$208,413 of the invoiced costs could be tied directly to work performed under the project.

Because of the accounting error and the lack of support for contract costs, we question \$218,230 (\$173,613 plus \$44,617). Department officials agreed with our conclusion and noted that they would not submit these costs to FEMA for reimbursement.

Finding D – Project Cost Eligibility

The Department's accounting records for three projects included \$37,270 in costs unrelated to the FEMA-approved scopes of work.

- For project 2912, force account labor records (a) were incomplete and could not be associated with the scope of work or (b) identified charges that were for non-disaster tasks. These questionable charges totaled \$26,324.
- For project 2985, accounting records included \$8,852 in charges not included in the FEMA approved scope of work. The charges were associated with force account survey work performed 8 months after the project was completed in March 2006. Further, project records did not include any explanation on how the charges related to the scope of work.
- For project 2407, accounting records included \$2,094 in force account labor costs related to maintenance work and tasks unrelated to the approved project scope of work.

According to 44 CFR 206.223(a)(1), to be eligible for financial assistance, an item of work must be required as the result of the major disaster event. Office of Management and Budget (OMB) Circular A-87, *Cost Principles for State, Local, and Indian Tribal Governments*, Attachment A, Section C provides that for an item of cost to be allowed it must be reasonable and allocable to a particular cost objective. Department officials agreed that the \$37,270 (\$26,324 plus \$8,852 plus \$2,094 in costs allocated to the three projects were not related to the scope of work approved by FEMA.

Finding E – Costs Based on Equipment Rates

The Department's recorded costs for project 2912 included \$17,493 in force account equipment costs that exceeded FEMA's Schedule of Equipment Rates. Project records showed that the Department

established equipment rates and used those rates to record disaster related force account equipment costs. Department rates covered normal costs of equipment usage, fuel, maintenance, and in some cases, depreciation. According to 44 CFR 206.228(a)(1)(ii), where local guidelines are used to establish equipment rates, reimbursement will be based on those rates or rates in FEMA's Schedule of Equipment Rates, whichever is lower. However, if an applicant wishes to claim an equipment rate which exceeds the FEMA schedule, it must document the basis for that rate and obtain FEMA approval for an alternate rate [44 CFR 206.228(a)(1)(ii)].

The Department used a water truck for 745 hours of disaster related work and recorded claimable costs of \$42,264 based on its locally developed rate of \$56.73 per hour. FEMA's Schedule of Equipment Rates lists an hourly rate of \$33.25 for a comparable water truck. Using FEMA's rate, total claimable costs for this piece of equipment are \$24,771, or \$17,493 less than what the Department recorded. Department officials agreed with our conclusion and noted that except for this piece of equipment, Department rates were thought to be less than FEMA's rates because the existing rates do not include all of the costs incurred to maintain the equipment. Department officials said they would re-evaluate and revise their equipment rates as appropriate and submit them to CalEMA and FEMA for approval for use in future disasters. Nonetheless, since the Department's rate for the water truck exceeded FEMA's rate, the difference of \$17,493 is questionable (\$42,264 less \$24,771).

Finding F – Costs for Fringe Benefits

The Department's fringe benefits costs for force account labor for project 951 were based on an overstated nonproductive rate, thereby overstating fringe benefits costs by \$11,747. According to 44 CFR 13.20(b), the Department is required to maintain accounting records that identify how FEMA funds are used and to follow OMB cost principles, agency program regulations, and the terms of grant and subgrant agreements in determining reasonable costs, allowability, and allocability of costs. OMB Circular A-87, Attachment A, Section C, provides that for a cost to be allowed, the cost must conform to any limitation or exclusions set forth in federal law and grant requirements.

The Department's process for calculating the nonproductive rate (vacations, holidays, jury duty, sick leave, etc.) did not follow FEMA guidelines⁵ and the Department had no documentation justifying the use of an alternate methodology. When calculating the nonproductive rate, annual nonproductive hours of 365.36 should be divided by 2,080 - the total working hours in a year. This methodology produces a nonproductive rate of 17.57%. Instead, the Department first reduced the year's working hours by the nonproductive hours (2,080 less 365.36 equals 1,714.64) and then divided the annual nonproductive hours of 365.36 by 1,714.64. This methodology produced a nonproductive rate of 21.31% -- higher than FEMA's methodology by 3.74% (21.31% less 17.57%). In applying the difference in rates to total wages of \$314,079, the Department overstated the project's nonproductive costs by \$11,747 (3.74% times \$314,079).

Department officials stated they used state guidance, not FEMA guidance, for calculating the nonproductive costs for project 951. They agreed that by using state guidance, costs for project 951 were \$11,747 higher.

⁵ FEMA Form 90-128 calculates the straight time salaries and benefits rates by dividing annual nonproductive hours (numerator) by the total normal work hours for the year—excluding weekends (denominator).

Finding G– Project Funding

The Department completed the three projects identified in the table below 2 and 3 years ago but did not notify CalEMA or FEMA that over \$2.1 million in funds awarded to the projects was not needed and available for deobligation.

Project Number	Award Amount	Costs Incurred	Funds Not needed
951	\$2,968,110	\$1,499,512	\$1,468,598
2407	1,873,479	1,857,608	15,871
2985	883,159	261,882	621,277
Total	\$5,724,748	\$3,619,002	\$2,105,746

According to 44 CFR 206.205(b)(1), grantees must account for eligible costs for each large project and certify to FEMA that the reported costs were for eligible disaster work as soon as practicable after the Department has completed the approved work and requested payment.

According to 44 CFR 13.40(a), grantees are responsible for monitoring and reporting program performance to assure compliance with federal requirements and achievement of performance goals. In addition, 44 CFR 13.40(d) requires that as soon as known, grantees must inform FEMA of favorable developments which enable meeting time schedules and objectives sooner or at less cost than anticipated.⁶ CalEMA, through its project monitoring system, should receive this information quarterly from the Department. While the objective and scope of this audit did not include a review of CalEMA's project monitoring system, its Addendum to the State Administrative Plan for disaster number 1577-DR-CA says,

...OES [CalEMA] has adopted this system [Large Project Monitoring Program] for all large projects and has combined it with the current quarterly reporting process to develop a comprehensive automated "Progress Reporting System" whereby applicants [subgrantees] will provide updated information on all of their large projects to OES [CalEMA] electronically each quarter.

For the three projects listed above, the CalEMA and FEMA officials we spoke to said they were unaware that the projects had been completed at over \$2.1 million under budget.

Department officials told us that excess funds should be retained and used for underfunded projects. However, FEMA should deobligate the \$2.1 million associated with projects 951, 2407, and 2985 and obligate funds to cover overruns on other underfunded projects only after CalEMA makes a full accounting of eligible costs for eligible disaster work associated with those other projects.

This finding also indicates that CalEMA's project monitoring should be improved. However, we are not making a recommendation in that regard because we recommended in a different subgrantee report⁷ that the Regional Administrator require CalEMA to strictly follow (a) the monitoring and program performance reporting requirements of 44 CFR 13.40 and (b) its Addendum to the State

⁶ This CFR citation also requires the grantee to report problems, delays, and adverse conditions as soon as they become known.

⁷ DS-09-05, *California Department of Parks and Recreation*, dated May 20, 2009.

Administrative Plan to ensure that quarterly progress reports submitted by subgrantees are accurate, current, and complete and reflect significant developments in project execution.

Other Matters – Force Account Labor and Equipment Charges

The Department’s accounting records for projects 2912, 2407, and 951 included charges for force account labor and force account equipment that could not be verified.

Project Number	Force Account Labor	Force Account Equipment
2912	\$657,943	\$233,541
2407	0	91,054
951	0	54,308
Total	<u>\$657,943</u>	<u>\$378,903</u>

According to 44 CFR 13.20(b)(2), grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially assisted activities. Also, 44 CFR 13.20(b)(5) requires grantees and subgrantees to follow OMB cost principles, agency program regulations, and other terms of the grant and subgrant agreements in determining reasonable costs. OMB Circular A-87, Attachment A, Section C.2 provides that a cost is reasonable if, in nature and amount, it does not exceed that which would be incurred by a prudent person.

To verify that force account labor and equipment costs were supported and reasonable, the Department provided us copies of equipment operator time reports. Those reports identified the name of an employee, shift hours, equipment used, and number of force account labor and equipment use hours. We communicated our results to Department officials who informed us that the records they provided us were not the Department’s official records for force account labor. They explained that force account labor hours were maintained in electronic timesheets that are completed directly on-line by employees and supervisors and that the reports provided to us only supported disaster equipment usage hours.

Equipment operator hours (force account labor) are an integral source of data for validating equipment usage hours (force account equipment) and need to be reviewed concurrently by FEMA Region IX. Because the Department provided us new information at the conclusion of our field work, we are recommending that FEMA require CalEMA to verify the eligibility and supportability of labor and equipment charges for projects 2912, 2407, and 951 for the following reasons.

- FEMA previously denied the Department’s request for labor charges on project 2912. In June 2005, when 90% of the work was complete, the Department requested reimbursement for equipment operator charges totaling \$664,116, but because of inconsistencies with the financial information provided by the Department, FEMA only allowed a portion of the claim (\$32,325).
- Records for projects 2407 and 951 supporting force account equipment hours identified that recorded hours included periods when equipment was idle and not engaged in disaster work. Records for these two projects did not include issues with force account labor hours.
- Equipment operator time reports were incomplete. For example, (a) equipment usage hours were not recorded, (b) equipment usage hours could not be matched to equipment operator

hours, (c) reports did not include supervisory approvals, and (d) some reports did not include the actual time the equipment was checked out and returned by the operator.

- Equipment operator time reports and other project records indicated that some employees used pick up trucks to commute to the disaster affected areas, but instead of using a standard mileage rate, the Department charged a daily vehicle usage rate. Department officials noted that the pick up trucks daily rate was an internal rate charged to other city departments and represented the daily cost of operating the equipment.

RECOMMENDATIONS

We recommend that the Regional Administrator, FEMA Region IX, in coordination with CalEMA:

Recommendation #1. Inform the Department of its regulatory requirement to obtain prior written approval for (a) budget revisions resulting in the need for additional funds [44 CFR 13.30(c)(2)], and (b) any revision in the scope or objective of a project [44 CFR 13.30(d)(1)] (see Finding A).

We also recommend that the Regional Administrator, FEMA Region IX require CalEMA to

Recommendation #2. Disallow \$2,169,000 in project improvements for project 3016 identified by the Department as claimable costs (see Finding A).

Recommendation #3. Disallow \$463,125 in questionable costs relating to projects 951, 2407, 2912, and 2985 identified by the Department as claimable costs (see Findings B through F).

Recommendation #4. Deobligate \$2,105,746 in funds awarded for projects 951, 2407, and 2985, since the funds are no longer needed to accomplish the FEMA approved scopes of work (see Finding G).

Recommendation #5. Verify the eligibility and supportability of \$657,943 in force account labor charges for project 2912, and \$378,903 in force account equipment charges for projects 2912, 2407, and 951 both of which were identified by the Department as claimable costs (see Other Matters).

DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOW-UP

We discussed the results of this audit with CalEMA and Department officials on January 23, 2009. Those officials generally agreed with our findings or said they needed additional time to research the issues. We also notified FEMA of the audit results on March 26, 2009.

Please advise this office by September 8, 2009, of the actions taken to implement our recommendations. Please note that your responses should include target completion dates for actions planned and actual completion dates for actions taken. Should you have any questions concerning this report, please contact me at (510) 637-1482. Key contributors to this assignment are Humberto Melara and Ravi Anand.

Schedule of Audited Projects
 Audit of Los Angeles Department of Water & Power
 Los Angeles, California
 Public Assistance Identification Number 037-44000-16
 FEMA Disaster Number 1577-DR-CA

PW Number	PW Amount	Costs the Department Plans to Claim	Questioned Costs	Funds Not needed that should be Deobligated	Finding Reference
951	\$2,968,110	\$1,499,512	\$ 39,557	\$1,468,598	B,F,G
2407	1,873,478	1,857,608	266,156	15,871	B,C,D,G
2912	\$597,996	1,126,522	103,943	0	B,D,E
2985	\$883,159	261,882	53,469	621,277	C,D,G
3016	\$331,000	2,500,000	2,169,000	0	A
Total	\$6,653,743	\$7,245,524	\$2,632,125	\$2,105,746	