Office of Inspector General

U.S. Department of Homeland Security
Washington, DC 20528

Homeland Security

April 28, 2006

MEMORANDUM FOR: Margaret Young
FEMA Chief Financial Officer

David Garratt
Acting Director for FEMA Recovery Division

FROM: Dennis R White for Matt Jadacki
Special Inspector General for
Gulf Coast Hurricane Recovery

SUBJECT: *Review of FEMA Policy for Funding Public Assistance Administrative Costs*
Audit Report GC-HQ-06-40

RESULTS OF REVIEW

FEMA should initiate immediate action to correct weaknesses in awarding funds to cover grantee operations associated with the administration of public assistance grants. Currently, FEMA provides assistance in the form of an administrative allowance, as well as state management administrative grants to cover needs that are unmet by the allowance. However, there is a real potential for excess funding and a financial windfall for state grantees because the two fund sources cover essentially the same activities and no provisions exist for the state grantees to report or return unused funds granted under the allowance. Funding that the State of Louisiana has available for Hurricane Katrina administrative costs illustrates this point.

The State of Louisiana will receive an administrative allowance of approximately $24 million based on projected public assistance costs of $4.8 billion.[1] The allowance is based on a sliding scale formula, tied to the amount of public assistance awards--the larger the award, the larger the allowance. The allowance must be used to cover the extraordinary costs of state expenses associated

[1] The Disaster Mitigation Act of 2000 (DMA), Pub. L. No. 106-390, § 205(e) (Oct. 30, 2000), repealed section 406(f) of the Robert T. Stafford Disaster Relief and Emergency Assistance Act (Stafford Act), 42 U.S.C. § 5172(f), which authorized grantees an administrative allowance. Section 202(a) of the DMA added section 324 of the Stafford Act, requiring establishment by regulation of cost rates to determine contributions for management costs incurred by Stafford Act grantees. Section 202(b) of the DMA required continued use of section 406(f) until management cost rates were established by regulation. FEMA issued its proposed rule on August 20, 2002. 67 Fed. Reg. 56130-56136 (Aug. 30, 2002). It has yet to issue a final rule and continues to apply the formula under section 406(f).

with the administration of the public assistance program, including the overtime salaries of state personnel engaged in project development, inspections and audit, and travel and per diem costs.

On April 22, 2001, FEMA established Response & Recovery Policy 9525.11 making supplemental public assistance funds available to states to hire contractors to manage their programs, in place of grantee staff. Prior to this policy, FEMA did not pay for contractor costs associated with the state's program administration, although it did treat contractor overtime, travel, and per diem expenses as covered by the 406(f) allowance.

For Hurricane Katrina, the Louisiana Office of Homeland Security and Emergency Preparedness, the state grantee, requested and received a state management grant for $29 million ($26 million federal share).[2] According to the approved work statement, the $29 million was for funding a management consultant to "supplement the existing state recovery staff in providing on site project manager, grant management, project worksheet development, project applications, reports, audit and related field inspection." Unlike the 406(f) allowance that restricts funding for state employee costs to only overtime, the management grant provided funding for all personnel cost of the consultant. Thus, the management grant provided funding for all contractor personnel service costs, perhaps, alleviating the need for the state to have many of its employees work the disaster or incur overtime costs that would be funded by the 406(f) allowance. Under this scenario, a real potential exists that the state management grants may cover all or a substantial portion of the state's costs for public assistance program administration, with little or no need for the allowance. This could result in the state receiving a substantial amount of disaster funds that are not needed or used for eligible disaster costs.

Further complicating this dual funding situation is the absence of a budget for the allowance, or a requirement for states to report on fund use. For Louisiana Katrina operations, the management grant is supported by a budget, though sketchy, and a requirement for the state grantee to report and limit its charges to eligible expenditures. In contrast, the state grantee receives the full 406(f) allowance regardless of needs. FEMA programmed its disaster payment system to allow states to receive proportionate allowance payments when they receive payments for public assistance program expenditures.

For example, as of January 6, 2006, the Louisiana State grantee had an administrative allowance of $5.6 million available for use. However, according to the state grantee budget officer, no costs had been incurred from the allowance. Additionally, with the $26 million management grant to cover salaries, overtime, travel and other management consultant costs, the State grantee has limited its disaster recovery staff to 10 to 14 employees. With these conditions in mind, the State grantee is unlikely to spend a substantial portion of the projected total $24 million 406(f) allowance.

The State of Louisiana is cited in this report to illustrate weaknesses in the FEMA policies for funding administrative costs. The same situation will exist for other state grantees receiving both sources of administrative funding. The long-term solution to the problem is for FEMA to implement Section 324 of the Stafford Act, as added by the DMA, which requires the agency to establish

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[2] There are other proposed projects pending which may result in additional awards for administrative state management grants.

management cost rates to replace the administrative allowance and state management grants. Over five years have elapsed since this mandate, yet no new management cost regulations are in place. In addition, a more immediate remedy is needed to address funding and related control weaknesses related to Louisiana and other Gulf Coast states, where appropriate.

RECOMMENDATIONS

We recommend that FEMA's Chief Financial Officer, in coordination with the Acting Director of the Recovery Division:

1. Take immediate action to establish management cost rates to replace both the administrative allowance and state management grants.

2. Until new management cost rates are effected:

   a. Modify the policy for funding state administrative and management costs to require state grantees to first establish a budget detailing the proposed use of the projected amount of administrative allowance, and then limit the management grant to cover only those eligible costs that are not covered by the allowance.

   b. Require the state grantees to submit periodic financial status reports to FEMA on the use of the statutory administrative allowance and to refund amounts that cannot be used in accordance with the Stafford Act.

   c. Implement recommendations 2 and 3 as soon as possible for the Louisiana State grantee and other Gulf Coast grantees affected by Hurricanes Katrina, Rita, and Wilma, as appropriate.

DISCUSSION WITH MANAGEMENT AND FOLLOW-UP

We discussed the results of our review with the FEMA PA Officer for Louisiana Katrina operations. This official generally concurred with our observations.

Please advise us by May 22, 2006, of actions taken or planned to implement the recommendations. Should you have any questions concerning this report, please contact Gary J. Barard, Gulf Coast Audit Coordinator, at (770) 220-5228.

GENERAL COMMENTS

The nature and brevity of this assignment precluded the use of our normal audit protocols. Therefore, this review was not conducted according to generally accepted government auditing standards. Had we followed such standards, other matters may have come to our attention.

This review was conducted in conjunction with the President's Council on Integrity and Efficiency (PCIE) as part of its examination of relief efforts provided by the Federal government in the aftermath of Hurricane Katrina and Rita. As such, a copy of the report has been forwarded to the PCIE Homeland Security Working Group, which is coordinating Inspectors General review of this important subject.

This is the first of two reports addressing administrative costs for public assistance activities. Audit manager Jack Lankford and auditor Jerry Prem contributed to this report. A second report, to follow, will assess FEMA's procedures and practices for determining eligible activities and amounts awarded for state management grants.

cc: Under Secretary for Management
Acting Under Secretary for Emergency Preparedness and Response
Acting Chief Financial Officer, DHS
Chief Procurement Officer, DHS
Audit Liaison, DHS
Audit Liaisons, FEMA
Deputy Director, Gulf Coast Recovery