

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

FEMA Improperly Applied the 50 Percent Rule in Its
Decision To Pay for the Replacement of the
Martinsville High School, Martinsville, Illinois





OFFICE OF INSPECTOR GENERAL

Department of Homeland Security

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

JAN 14 2013

MEMORANDUM FOR: Andrew Velasquez III
Regional Administrator, Region V
Federal Emergency Management Agency

FROM: *Jonda Hadley for*
D. Michael Beard
Assistant Inspector General
Office of Emergency Management Oversight

SUBJECT: *FEMA Improperly Applied the 50 Percent Rule in Its
Decision To Pay for the Replacement of the Martinsville
High School, Martinsville, Illinois*
FEMA Disaster Number 1771-DR-IL
Audit Report Number DD-13-04

We audited Public Assistance (PA) grant funds awarded to Martinsville Community Unit School District #C-3 (Martinsville), Martinsville, Illinois (PA Identification Number 023-UF91H-00). Our audit objective was to determine whether Martinsville accounted for and expended Federal Emergency Management Agency (FEMA) grant funds according to Federal regulations and FEMA guidelines.

The Illinois Emergency Management Agency (IEMA), a FEMA grantee, awarded Martinsville \$13.5 million for damages caused by severe storms and flooding that occurred June 1 to July 22, 2008. The award provided 75 percent FEMA funding for four large projects.¹ The audit covered the period June 1, 2008, through May 4, 2012, the cutoff date of our audit, and included a review of 100 percent of the total award (see Exhibit A, Schedule of Projects Audited). As of the cutoff date of our audit, all projects remained open.

We conducted this performance audit between March and October 2012 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

¹ Federal regulations in effect at the time of the disaster set the large project threshold at \$60,900.



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audit objective. We conducted this audit according to the statutes, regulations, and FEMA policies and guidelines in effect at the time of the disaster.

We interviewed FEMA, IEMA, and Martinsville 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 Martinsville's internal controls applicable to grant activities because it was not necessary to accomplish our audit objective. We did, however, gain an understanding of Martinsville's method of accounting for disaster-related costs and its procurement policies and procedures.

BACKGROUND

Severe storms and flooding damaged Martinsville's high school. Wind damaged the roof, and rain overwhelmed the roof drainage systems, causing extensive damage to the building. FEMA applied its 50 Percent Rule calculation to determine whether it would be more cost effective to replace, rather than repair, the school. FEMA generally makes this calculation by comparing estimated repair costs with estimated replacements costs. However, in arriving at its 50 Percent Rule determination, FEMA must adjust its repair and replacement estimates based on the requirements of the 50 Percent Rule.

The "50 Percent Rule"

According to Federal regulation 44 CFR 206.226(f)(1), "A facility is considered repairable when disaster damages do not exceed 50 percent of the cost of replacing a facility...." FEMA refers to this regulation as the 50 Percent Rule and implements it according to its Disaster Assistance Policy 9524.4. This policy provides the decisionmaking tool to determine whether FEMA should fund the repair or replacement of a disaster-damaged facility.² The tool compares certain repair costs with certain replacement costs and results in a fraction that expresses repair costs as a percentage of replacement costs. The calculation specifically excludes many otherwise allowable repair and replacement costs that FEMA will ultimately pay under the PA program.

FEMA policy excludes these costs because including them in the repair or replacement decision calculation could distort the results. For example, according to FEMA, if the repair side of the calculation included seismic upgrade costs to undamaged elements of

² Various Federal policies and publications clarify 44 CFR 206.226(f)(1). These include FEMA 322 Public Assistance Guide (June 2007), p. 36; Public Assistance Policy Digest (January 2008), p. 113; and Disaster Assistance Policy DAP9524.4 (September 24, 1998). FEMA updated DAP9524.4 on March 25, 2009.



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the building, then the repair costs of older buildings with even minor damage could exceed the 50 percent cost threshold because of the comparatively high cost of code-triggered whole-building upgrades, seismic upgrading, and related repairs.

FEMA bases its exclusion of certain costs on the premise that, when a facility is so severely damaged (not including code-triggered whole-building upgrades) that the cost to repair the damage exceeds 50 percent of the cost of a new building, it is often justifiable and reasonable to replace the building. However, including certain code-triggered whole-building upgrade costs with the costs of the repairs to the damaged elements would likely cause erroneous decisions to fund new facilities rather than repair structurally sound and lightly damaged facilities.

Specifically, the numerator of the fraction includes only the direct cost of repairing the disaster damage, referred to as “hard” costs, and may include costs associated with the current repair codes and standards that apply to the damaged elements only.³ The numerator does not include costs associated with—

- a. Upgrades and other elements triggered by codes and standards,
- b. Design associated with upgrades,
- c. Demolition of entire facility,
- d. Site work,
- e. Applicable project management costs,
- f. Contents, and
- g. Hazard mitigation measures.

The denominator of the fraction is the cost of replacing the facility based on its predisaster design and according to applicable codes and standards currently in effect. The denominator does not include costs associated with—

- a. Demolition,
- b. Site work,
- c. Applicable project management costs,
- d. Contents, and
- e. Hazard mitigation measures.

³ Only direct construction costs, known as “hard” costs, can be included in the numerator or denominator of either the repair or the replacement costs. “Soft” costs include the costs for project management, architectural and design fees, and insurance.



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Deciding to repair a facility may not necessarily result in cost savings to taxpayers after all allowable costs under the PA program are included. However, FEMA caps the total repair costs at the estimated cost to replace the facility.

RESULTS OF AUDIT

Martinsville accounted for FEMA grant funds on a project-by-project basis as required by Federal regulations. However, FEMA Region V officials did not correctly apply the 50 Percent Rule when deciding to replace, rather than repair, Martinsville High School. Martinsville also did not follow Federal procurement standards when contracting with the high school's architectural and engineering (A/E) firm and did not obtain the required type of insurance coverage for the new school. As a result, we question the following ineligible amounts, which total \$9,272,138:

- \$1,136,581, which represents the difference between actual claimed replacement costs at the time of the audit and the estimated repair costs used in the 50 Percent Rule calculation (\$9,262,096 minus \$8,125,515) (finding A).
- \$805,630 for improper contracting cost for a noncompetitive A/E contract (finding B).
- \$7,329,927 in claimed costs for the uninsured school. To avoid duplicate questioned costs, this amount is net of costs questioned in findings A and B (\$9,272,138 claimed minus \$1,136,581 and \$805,630) (finding C).

In addition, FEMA should deobligate approximately \$2.2 million of unused Federal funds and put them to better use (finding D).

Some of the problems we identified in this report occurred because IEMA did not take a proactive role in Martinsville's subgrant activity as required under Federal regulation. Inadequate State oversight has been a recurring problem identified in our audits of FEMA's PA program (finding E). FEMA, for its part, made significant errors in determining the building's eligibility for replacement under the 50 Percent Rule. Following a recent Office of Inspector General report, FEMA headquarters acknowledged problems in the application of its 50 Percent Rule policy and promised to take steps to improve controls over its decisionmaking process.⁴

⁴ *FEMA's Decisions To Replace Rather Than Repair Buildings at the University of Iowa*, Audit Report Number DD-12-17, June 19, 2012.



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Finding A: FEMA Improperly Applied the 50 Percent Rule in Its Decision To Pay for the Replacement of Martinsville High School

FEMA Region V officials incorrectly applied the 50 Percent Rule to determine whether Martinsville should repair or replace its high school. The calculation included several cost elements not allowed in FEMA’s 50 Percent Rule calculation. As shown in table 1, FEMA incorrectly included costs for seismic upgrades and unallowable “soft” costs, including A/E fees, in the repair costs (numerator), and demolition, site work, information technology, general conditions, overhead and profit, contingencies, and professional fees in the replacement costs (denominator). Consequently, FEMA’s calculation resulted in a 63 percent ratio of repair costs to replacement costs, indicating that FEMA should fund the building’s replacement. In contrast, when calculated correctly, the ratio reaches only 32 percent, far short of the 50 percent minimum needed to justify replacement.



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Table 1. 50 Percent Rule Comparisons

Type of Cost	FEMA- Included Costs	Incorrect Percent	Correct Percent	Allowable 50 Percent Rule Costs
Repair Costs				
Surface Flooding	\$ 829,661			\$ 829,661
Other Damage	1,395,854			1,395,854
Seismic Steel Frame	4,800,000			0
A/E Fees	<u>1,100,000</u>			<u>0</u>
Total Estimated Repair	\$8,125,515			\$2,225,515
Replacement Costs				
Demolition	\$ 1,269,514			\$ 0
Site Work	325,000			0
New Construction	6,379,780			6,379,780
Fixed Equipment	530,650			530,650
Information Technology	125,000	63%	32%	75,000 ⁵
General Conditions	1,294,492			0
Overhead and Profit	862,994			0
Contingency	1,078,743			0
Professional Fees	<u>1,000,294</u>			<u>0</u>
Total Estimated Replacement	\$12,866,467			\$6,985,430

Most notably, FEMA included \$4.8 million for seismic reinforcement on the repair side of the equation that is unallowable in the 50 Percent Rule calculation. Martinsville is located near the New Madrid Seismic Zone, and, according to FEMA Region V, the extent of the damage triggered the legally required seismic reinforcement. FEMA Disaster Assistance Policy 9524.4 states that “disaster damage” for the purpose of calculating the 50 Percent Rule includes only the costs of repairing the damaged components. Typically, seismic reinforcements improve and extend the useful life of a building, but are not necessary to repair damaged elements of the building. It is important to note that, under the 50 Percent Rule, FEMA will reimburse legally required seismic upgrade costs. However, these seismic upgrade costs are not allowed in the numerator of the 50 Percent Rule calculation.

FEMA Region V officials asserted that the seismic upgrade was necessary to repair the flood-damaged elements safely, but did not provide us with any evidence of the

⁵ Excludes \$50,000 of unallowable information technology equipment as a replacement cost element.



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weakness of the structure or that the seismic work was in any other way necessary to repair the building. If the seismic upgrade were somehow necessary to repair the damaged elements back to their predisaster condition, these costs would have been allowable in the 50 Percent Rule calculation. However, the engineer who performed the damage assessment told us that Martinsville could have safely repaired the school without the seismic reinforcement. In any case, FEMA Region V should have developed and retained documentation supporting its assertion that a structural weakness required seismic reinforcement to repair the school safely.

According to FEMA 322 Public Assistance Guide (June 2007), p. 36, "Repair cost includes only those repairs, including non-emergency mold remediation, associated with the damaged components and the codes and standards that apply to the repair of the damaged components." Only direct construction costs, or "hard" costs, can be included in the numerator or denominator of either the repair or the replacement costs. "Soft" costs include the costs for project management, architectural and design fees, and insurance. Because FEMA did not correctly apply the 50 Percent Rule, we question \$1,136,581 as ineligible. We calculated the \$1,136,581 in questioned costs as the difference between the net actual claimed replacement costs at the time of the audit (\$9,262,096; see project 978 in table 3) and the total estimated repair costs used in the 50 Percent Rule calculation (\$8,125,515; see table 1), or \$9,262,096 minus \$8,125,515.



Figure 1. The New Martinsville High School



FEMA Region V officials agreed that they included unallowable “soft” costs in their 50 Percent Rule calculation, but could not explain why the FEMA contractor who prepared the calculation included the inappropriate costs or how these errors could have occurred and not been detected. If FEMA officials had independently reviewed the calculations before approving the building for replacement, they might have detected and prevented these calculation errors. Although FEMA headquarters has promised to develop review procedures for its 50 Percent Rule, in the interim, FEMA Region V should develop and implement interim procedures to ensure that qualified and independent professionals review these calculations.

FEMA Region V officials said that they have taken steps to modify the implementation of the 50 Percent Rule by instructing all field staff to refer 50 Percent Rule determinations to Region V for review by its technical experts. These officials also said that they plan to gather more information to determine why the region’s 50 percent review process is not doing a better job of detecting errors.

Although FEMA Region V agreed that it should not have included “soft” costs in its calculation, it did not concur that the seismic upgrade was unallowable in the calculation. Region V officials said that they disagreed because, at the time of the disaster, FEMA headquarters was revising the 50 Percent Rule policy to include codes and standards language, and the guidance available at the time of the project formulation allowed for seismic reinforcement. The officials also determined that the structure of the school was so damaged that it triggered codes and standards requiring



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seismic steel reinforcement. However, as discussed above, FEMA's policies specifically prohibit including these triggered costs in the 50 Percent Rule calculation.

Further, FEMA headquarters has never provided us with evidence that it is considering allowing seismic upgrades in the 50 Percent Rule calculation, either at the time of this disaster or now. Finally, FEMA Region V could not provide evidence that the flooding had so weakened the facility that it could have been repaired safely only by seismic reinforcement. On the contrary, the engineer who performed the damage assessment told us that the facility could have been repaired safely without the seismic upgrade.

Finding B: Martinsville Improperly Awarded an \$805,630 Noncompetitive Contract

Martinsville did not comply with Federal procurement standards when it awarded a noncompetitive A/E contract for the design and construction management of Martinsville High School. Therefore, we question \$805,630 as ineligible because Martinsville improperly procured this work. Federal regulation 44 CFR 13.36(d)(4)(i) allows applicants to use noncompetitive contracts only in specific circumstances, stating, "Procurement by noncompetitive proposals may be used only when the award of a contract is infeasible under small purchase procedures, sealed, bids or competitive proposals and one of the following circumstances applies: (A) The item is available only from a single source; (B) The public exigency or emergency for the requirement will not permit a delay resulting from competitive solicitation; (C) The awarding agency authorizes noncompetitive proposals; or (D) After solicitation of a number of sources, competition is determined inadequate." None of these exceptions applied.

Rather than competing this contract openly, Martinsville amended a previous contract with an A/E firm that had performed work for the school district before the flooding. According to a Martinsville official, the school needed an A/E firm immediately to determine its course of action related to flood damages, and school officials did not know that they were required to openly compete the contract. However, obtaining immediate help to set a course of action is far different from hiring an A/E firm to design and manage the construction of a multimillion-dollar high school over a period of years. Also, Martinsville had ample time, 7 months from the disaster declaration date to the signing of the A/E contract, to properly procure the contract.

Further, Martinsville officials did not take affirmative steps to ensure that minority firms, women's business enterprises, and labor surplus area firms were used when possible, as 44 CFR 13.36(e)(1) requires. 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



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prime contractor, if subcontracts are to be used, to take the affirmative steps listed in 44 CFR 13.36(e)(2)(i) through (v). Martinsville did not give these types of firms the opportunity to bid on the A/E contract as required, because Martinsville officials did not know about these requirements.

Finding C: Martinsville Has Not Obtained the Required Flood Insurance

As of August 14, 2012, a year after the newly constructed high school opened, Martinsville officials had not obtained the \$12,989,816 in required flood insurance. As a result, Martinsville does not have adequate insurance coverage in case the high school suffers flood damage again. The need for insurance renders the entire building and its contents ineligible for FEMA funding until Martinsville officials obtain the proper insurance coverage.

Federal regulation 44 CFR 206.252(d) states, “The grantee or subgrantee is required to obtain and maintain flood insurance in the amount of eligible disaster assistance, as a condition of receiving Federal assistance that may be available.” In addition, FEMA 322, Public Assistance Guide (June 2007), p. 123, states, “As a condition for receiving Public Assistance for permanent work, an applicant must obtain and maintain insurance to cover that facility for the hazard that caused the damage. Such coverage must, at a minimum, be in the amount of the estimated eligible damages for that structure prior to any reduction.”

As shown in table 2, FEMA estimated total eligible damages for the high school at \$12,989,816, before reductions for insurance, which included \$12,866,467 for the facility and \$123,349 for the contents. Therefore, Martinsville is required to obtain flood insurance coverage in the amount of \$12,989,816 because that is FEMA’s gross estimate of the damages.

Table 2. Gross and Net Award Amounts

Project	Gross Award Amount	Reductions for Anticipated Insurance Proceeds	Net Award Amount
978	\$12,866,467	(\$1,395,354)	\$11,471,113
629	123,349	(77,710)	45,639
Totals	\$12,989,816	(\$1,473,064)	\$11,516,752

Although IEMA notified Martinsville of the insurance requirement, IEMA officials said that they cannot compel Martinsville to purchase insurance. An IEMA official said that



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the authority to enforce that requirement rested with FEMA. We disagree, because IEMA can withhold funding from an applicant until the applicant complies with the requirements of FEMA's PA program. It is important to note that Federal regulation requires the State (grantee) to manage the day-to-day activities of subgrantees:

44 CFR 13.40 Monitoring and reporting program performance.

- (a) *Monitoring by grantees.* Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity.

A Martinsville official said that the school district had not yet obtained flood insurance primarily because the district did not believe it should be required to purchase the insurance for the full amount of the project when it cost somewhat less to rebuild the school. However, FEMA policy requires that insurance be obtained within a reasonable period of the completion of construction. An IEMA official responsible for the grant said that he understood Martinsville's reluctance to purchase flood insurance for the full project funding because the final cost of construction was less than the estimated cost. However, regardless of Martinsville's reluctance, Federal regulations require that insurance coverage "must, at a minimum, be in the amount of the estimated eligible damages for that structure prior to any reduction." At the time of our audit, FEMA's gross estimate of damages remained at \$12,989,816 for the facility and its contents, so that is the amount of insurance required.

IEMA informed Martinsville officials in a September 15, 2011, email message that they were required to purchase flood insurance in the amount of \$12,866,467, which is the estimated eligible damages to the facility before the reduction for insurance. At the time of the audit, Martinsville officials were not aware that they were also required to insure the contents of the building for flood damage in the amount of \$123,349. A FEMA official told us that neither Martinsville nor IEMA had informed FEMA that Martinsville had not purchased the required flood insurance until after we began this audit. IEMA, in its role as the grantee, should have informed FEMA that the subgrantee had not purchased the required flood insurance and withheld reimbursements until Martinsville obtained the required insurance.

Section 311(a)(2) of the *Robert T. Stafford Disaster Relief and Emergency Assistance Act* states that, "In making a determination with respect to availability, adequacy, and necessity under paragraph (1), the President shall not require greater types and extent of insurance than are certified to him as reasonable by the appropriate State insurance



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commissioner responsible for regulation of such insurance. In addition, the FEMA Public Assistance Guide (June 2007, p. 123) states, "An applicant is exempt from this requirement for facilities for which, in the determination of the State insurance commissioner, the type and/or extent of insurance being required by FEMA is not reasonable." However, Martinsville has not applied for or obtained such an exemption.

If Martinsville does not obtain the required amount of flood insurance or obtain a waiver for the requirement, FEMA should disallow the entire net amount Martinsville claimed for the high school, or \$9,272,138 after adjustments for actual insurance proceeds received (see finding D and table 3). However, this amount includes \$1,136,581 questioned in finding A and \$805,630 questioned in finding B (see Exhibit A, Schedule of Projects Audited). Therefore, to avoid questioning the same costs twice, we are recommending that FEMA disallow the net amount of \$7,329,927 for this finding (\$9,272,138 claimed minus \$1,136,581 and \$805,630). If Martinsville obtains the required insurance coverage, the amounts in findings A and B remain questioned.

Finding D: FEMA Should Deobligate \$2.2 Million in Unused Funds

FEMA should deobligate approximately \$2.2 million in unused funds from Projects 978 and 629 and put those funds to better use. Martinsville claimed \$9,623,876 for the facility (Project 978), with approximately \$100,000 in outstanding costs to be claimed. Martinsville also claimed \$45,639 for the contents of the facility (Project 629). As shown in table 3, Martinsville's gross claim amount for the high school was \$9,769,515 (\$9,623,876 plus \$100,000 plus \$45,639).⁶ However, at the time of our audit, FEMA had not adjusted the gross award amounts (see table 2), and Martinsville had not adjusted its gross claim amounts for the insurance proceeds it received in late 2008 and early 2009.

As a result, the \$2.2 million in excess funds remain obligated but unused. The new Martinsville High School opened in August 2011, and construction was substantially complete by the end of the month. By May 2012, Martinsville had claimed \$9,623,876 for the facility, with an additional \$100,000 to be claimed (Project 978) and \$45,639 for the contents (Project 629). FEMA, working with IEMA and Martinsville, should have reduced the gross claim amounts for the high school by the amounts of insurance proceeds Martinsville received, for a net claim amount of \$9,272,138.

⁶ If Martinsville does not claim the additional \$100,000 as planned, FEMA should add this amount of unused funds to the amount we recommend for deobligation.



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Table 3. Gross and Net Claim Amounts

Project	Gross Claim Amount	Reductions for Insurance Proceeds	Net Claim Amount
978	\$9,723,876	(\$461,780)	\$9,262,096
629	45,639	(\$35,597)	\$10,042
Totals	\$9,769,515	(\$497,377)	\$9,272,138

The difference between the net award amount of \$11,516,752 (table 2) that remains obligated and the net claim amount of \$9,272,138 (table 3) is \$2,244,614.

Reducing unneeded funding in a timely manner (1) releases funds to cover cost overruns on other projects associated with the disaster, (2) provides a more accurate status of PA program costs for a disaster, and (3) is consistent with appropriations law and Statement of Federal Financial Accounting Standards Number 5, which require obligations/liabilities in FEMA’s accounting system to be recorded accurately and supported.

Finding E: Grant Management Issues

Some of the problems we identified in this report occurred because IEMA did not take a more proactive role in Martinsville’s subgrant activity. If IEMA officials had reviewed Martinsville’s A/E contract, they would have realized that it did not comply with Federal requirements; and IEMA should have notified FEMA of Martinsville’s continuing failure to purchase required flood insurance. Federal regulation 44 CFR 13.37(a)(2) requires grantees to ensure that subgrantees are aware of the requirements imposed on them by Federal regulations. Further, 44 CFR 13.40(a) requires grantees to manage the day-to-day operations of subgrant-supported activities and to monitor subgrant-supported activities to ensure compliance with applicable Federal requirements. IEMA officials had no comments regarding why Martinsville did not competitively award the A/E contract, but they did not believe it was IEMA’s responsibility to ensure that Martinsville met insurance requirements because IEMA does not have the statutory authority to compel subgrantees to purchase insurance.

We disagree with IEMA’s position that it is not the grantee’s responsibility to ensure that subgrantees meet Federal insurance requirements. As stated previously, Federal regulations require grantees to monitor grant- and subgrant-supported activities to ensure compliance with applicable Federal requirements. It is not FEMA’s responsibility to ensure that subgrantees comply with insurance requirements. Although FEMA has the authority to obligate and deobligate Federal funds, all PA funds flow through the



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grantee to the subgrantee. Therefore, the grantee controls Federal funds paid to or recovered from its subgrantees and is responsible for a subgrantee's performance and compliance with Federal requirements.

IEMA officials disagreed with this finding, saying that they are proactive in grant management but are not always able to monitor all aspects of a grant because of budgetary restraints that restrict hiring. According to an IEMA official, with limited staffing, IEMA sometimes must make choices in prioritizing grant management functions.

RECOMMENDATIONS

We recommend that the Regional Administrator, FEMA Region V:

Recommendation #1: Disallow \$1,136,581 (\$852,436 Federal share) of ineligible funds claimed for actual replacement costs in excess of estimated repair costs (finding A).

Recommendation #2: Establish interim policies and procedures to ensure that 50 Percent Rule decisions are supported and independently reviewed by qualified professionals (finding A).

Recommendation #3: Disallow \$805,630 (\$604,223 Federal share) of improperly procured contract costs as ineligible, unless FEMA grants an exemption for all or part of the costs as provided for in 44 CFR 13.6(c) and Section 705(c) of the *Robert T. Stafford Disaster Relief and Emergency Assistance Act*, as amended (finding B).

Recommendation #4: Disallow \$7,329,927 (Federal share \$5,497,445) as the net ineligible, uninsured portion of Martinsville's new school unless Martinsville either obtains and maintains flood insurance to cover the full amount of eligible disaster assistance provided for the new school (finding C) or obtains an exemption for the requirement. The amount questioned is net of the amounts questioned in findings A and B (\$9,272,138 minus \$1,136,581, minus \$805,630).

Recommendation #5: Deobligate \$2,244,614 (\$1,683,461 Federal share) of unused funds from Projects 978 and 629 and put those Federal funds to better use (finding D).

Recommendation #6: Require IEMA to develop and implement procedures to provide reasonable assurance that subgrantees comply with Federal regulations (finding E).



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DISCUSSION WITH MANAGEMENT AND AUDIT FOLLOWUP

We discussed the results of our audit with Martinsville, IEMA, and FEMA officials during our audit and included their comments in this report, as appropriate. We also provided a draft report in advance to these officials and discussed it with them during exit conferences held between October 5 and 23, 2012. Martinsville and IEMA officials disagreed with our findings or deferred comments until after we issue our final report. FEMA disagreed with findings A and E, and agreed with findings B, C, and D.

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 the 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. We will post the report on our website for public dissemination. Significant contributors to this report were Tonda Hadley, Director; Christopher Dodd, Audit Manager; William Lough, Auditor-in-Charge; and Jacob Farias, Program Analyst.

Should you have questions, please call me at (202) 254-4100, or your staff may contact Tonda Hadley, Director, Central Regional Office, at (214) 436-5200.



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EXHIBIT A

Schedule of Projects Audited
June 1, 2008, to March 28, 2012
Martinsville Community Unit School District #C-3, Martinsville, Illinois
FEMA Disaster Number 1771-DR-IL

We questioned FEMA’s 50 Percent Rule calculations in finding A, and Martinsville’s improper contracting in finding B. These questioned costs were also included in the costs we questioned under finding C for lack of proper insurance coverage (see below). However, because we cannot question the same costs more than once, we netted the duplicate questioned costs out of the amount questioned in finding C. The net effect is to question the total amount of \$9,272,138, or the entire amounts claimed after adjustments for actual insurance proceeds received under projects 978 and 629 (\$9,262,096 plus \$10,042). Therefore, if FEMA allows the questioned costs under findings A and B, FEMA should continue to disallow the total questioned costs under finding C. Conversely, if FEMA allows questioned costs under finding C, those costs should remain questioned under findings A and B.

Project Number	Net Award Amount	Finding A	Finding B	Finding C	Total Costs Questioned	Funds Put to Better Use (Finding D)
978	\$11,471,113	\$1,136,581	\$805,630	\$9,262,096	\$11,204,307	\$2,209,017
1513	1,635,372					
1514	379,233					
629	<u>45,639</u>	<u>0</u>	<u>0</u>	<u>10,042</u>	<u>10,042</u>	<u>35,597</u>
Subtotals	<u>\$13,531,357</u>	<u>\$1,136,581</u>	<u>\$805,630</u>	<u>\$9,272,138</u>	<u>\$11,214,349</u>	<u>\$2,244,614</u>
Less Costs Questioned Twice:						
Finding A				(1,136,581)	(1,136,581)	
Finding B				<u>(805,630)</u>	<u>(805,630)</u>	
Totals (net)		<u>\$1,136,581</u>	<u>\$805,630</u>	<u>\$7,329,927</u>	<u>\$ 9,272,138</u>	<u>\$2,244,614</u>



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EXHIBIT B

Report Distribution List
Martinsville Community Unit School District #C-3, Martinsville, Illinois
FEMA Disaster Number 1771-DR-IL

Department of Homeland Security

Secretary
Chief Financial Officer
Under Secretary for Management
Audit Liaison, DHS
Acting Chief Privacy Officer

Federal Emergency Management Agency

Administrator
Chief of Staff
Acting Chief Financial Officer
Chief Counsel
Chief Procurement Officer
Director, Risk Management and Compliance
Audit Liaison, FEMA Region V
Audit Liaison, FEMA (Job Code G-12-019)

Grantee

Public Assistance Coordinator, Illinois Division of Emergency Management

State

Director, Performance Audits, State of Illinois

Subgrantee

Superintendent, Martinsville Community Unit School District #C-3

ADDITIONAL INFORMATION AND COPIES

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