

**Management Advisory -
CalRecycle, a California
State Agency, Needs
Assistance to Ensure that
\$230 Million in Disaster
Costs are Valid**





OFFICE OF INSPECTOR GENERAL
Department of Homeland Security

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

March 6, 2017

MEMORANDUM FOR: Dr. Ahsha Tribble
Acting Regional Administrator, Region IX
Federal Emergency Management Agency
Thomas M. Salmon

FROM: Thomas M. Salmon
Assistant Inspector General
Office of Emergency Management Oversight

SUBJECT: *Management Advisory - CalRecycle, a California State Agency, Needs Assistance to Ensure that \$230 Million in Disaster Costs Are Valid*
Report Number OIG-17-44-D

Attached for your action is our final management advisory report, *CalRecycle, a California State Agency, Needs Assistance to Ensure that \$230 Million in Disaster Costs Are Valid*. We incorporated the formal comments provided by your office. We are currently auditing the California Department of Resources Recycling and Recovery (CalRecycle), a California state agency, to determine whether its policies, procedures, and business practices are adequate to manage Federal Emergency Management Agency (FEMA) grant funds. However, during our audit work we observed an issue that required management's attention.

Our advisory contains two recommendations aimed at directing the California Office of Emergency Services (California), to continue providing technical assistance to, and ensure compliance with all applicable Federal regulations to avoid improperly funding any of the \$230 million it expects to claim for debris removal cost. Your office concurred with both recommendations. Based on information provided in your response to the draft advisory, we consider both recommendations resolved but open. We will close these recommendations when we receive and review documentation that FEMA has completed its proposed corrective actions. Please email closeout documentation and request to Humberto.Melara@oig.dhs.gov.

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



Management Advisory

CalRecycle, a California State Agency, Needs Assistance to Ensure that \$230 Million in Disaster Costs Are Valid

Through this management advisory, we are bringing to your attention a condition that we identified during our current audit of FEMA Public Assistance grant funds awarded to the California Department of Resources Recycling and Recovery (CalRecycle). Our full audit will include a review of four contracts awarded by CalRecycle valued at about \$223 million to perform disaster-related work.

CalRecycle expects debris removal work will cost about \$230 million, and has received invoices totaling \$200 million from two contractors. However, the invoices included documentation with numerous discrepancies that did not fully support the invoiced costs as Federal regulations require. Therefore, FEMA has little assurance that these costs are valid and eligible.

This condition occurred because CalRecycle did not maintain a contract administration system adequate to ensure contractors complied with contract terms for submitting invoices. We discussed the deficiencies in supporting documentation with CalRecycle officials, and they are working with their contractors to correct the deficiencies and locate adequate support.

Our advisory contains two recommendations aimed at directing the California Office of Emergency Services (California), to continue providing technical assistance to, and ensure compliance with all applicable Federal regulations to avoid improperly funding any of the \$230 million it expects to claim for debris removal cost.

Background

In September 2015, two California wildfires destroyed over 146,000 acres and 2,876 structures. The President declared the disaster on September 22, 2015. Lake and Calaveras counties applied for Public Assistance to help them with debris removal and disposal of hazardous trees and vegetation that are within



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the Counties' rights-of-way. CalRecycle, however, applied for FEMA's Public Assistance to remove debris from private properties damaged by the fires.

California, a FEMA grant recipient, awarded CalRecycle two large projects (Projects 36 and 37) totaling \$142.7 million (net of \$22.9 million in estimated insurance proceeds) to fund debris removal work resulting from the 2015 wildfires. The award provides 75 percent Federal funding. FEMA plans to provide additional funding for the two large projects because CalRecycle expects debris removal costs to reach about \$230 million. By September 2016, California had paid CalRecycle about \$68.1 million in Public Assistance funding for disaster-related work.¹

Documentation Did Not Fully Support Costs

CalRecycle expects it will cost about \$230 million to complete debris removal work, and has received invoices totaling \$200 million from two contractors performing the work. As part of this management advisory, we conducted a limited review of the associated costs and noted numerous discrepancies with the invoices that did not fully support the invoiced cost as required by Federal cost principles and procurement standards.

Moreover, as of September 8, 2016, CalRecycle had paid its contractors about \$186.4 million of the \$200 million in invoiced costs, but had not completed its review of invoices nor collected all missing support records.² FEMA and California, therefore, should continue to assist CalRecycle in assuring that all costs are valid and eligible.

Federal regulations require grant recipients and subrecipients to maintain records that identify the source and application of funds for federally funded activities and maintain source documentation to support those accounting records (2 CFR 200.302(a) and (b)(3)). CalRecycle, however, has not fully complied with these requirements.

During our review of cost data and documentation that CalRecycle provided, we observed several instances where documentation was not sufficient to support costs. We brought this issue to CalRecycle officials' attention who said they were aware of the deficiencies and were working toward resolving them. These officials further explained that while reviewing initial invoice support

¹ California calculated the \$68,144,980 cost reimbursement as follows: \$100,955,526 claimed costs less 10 percent for retention, multiplied by 75 percent Federal cost share.

² California law requires CalRecycle to pay all undisputed aspects of the invoices (California Government Code section 927 et seq.).



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records, they identified significant deficiencies including, but not limited to, the following:

- costs for debris removed from locations not identified in the contract;
- contract labor costs without timesheets;
- costs for standby crews and equipment with no justification or support records; and
- lodging expenses without support records.

In one instance, CalRecycle determined that about \$1.5 million (60 percent) of a \$2.5 million invoice lacked proper support. CalRecycle officials stated that most deficiencies in the invoiced support documentation occurred because the prime contractors were not thoroughly reviewing the records before submitting them for payment. As a result, CalRecycle is working with the prime contractors to substantiate the deficient invoices. However, we determined that the most likely cause of the deficiencies is that CalRecycle did not always —

- maintain an adequate contract management system; and
- ensure contractors comply fully with the terms, conditions, and specifications of the awarded contracts as Federal regulations require (2 CFR 200.318(b)).

CalRecycle awarded four contracts for debris removal work to the two prime contractors. The terms of these contracts stipulate that the contractors must —

- submit invoices that are itemized and supported with documentation such as receipts, timesheets, etc. and
- ensure that all costs are reasonable, allocable, actual, and allowable.

However, CalRecycle did not initially hold the two contractors responsible for complying with these contract terms. The prime contractors often did not submit all receipts and timesheets with invoices or identify eligible work sites to support all of the costs of debris removed. CalRecycle officials said that upon identifying these discrepancies in the cost support records, they implemented corrective action by —

- hiring consultants to assist in reviewing invoiced support records;
- working directly with the prime contractors to help them resubmit adequate or missing invoiced support documentation;
- rejecting specific undocumented costs in lieu of rejecting entire invoices and returning them to the contractor; and
- tracking deficient source records.



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Conclusion

CalRecycle has implemented corrective actions to provide some assurance that costs it claimed are supported and eligible. However, by September 2016, CalRecycle had —

- paid its contractors \$186.4 million, or more than 93 percent of the \$200 million in invoiced costs;
- claimed \$68.1 million in Public Assistance funding;
- not fully reviewed records to support invoices — the consultants had reviewed \$108 million, but had yet to review about \$92 million; and
- had not substantiated all deficient documentation to support invoices.

Therefore, to prevent CalRecycle from potentially submitting reimbursement claims without adequate documentation, FEMA should direct California to —

- provide CalRecycle with further technical assistance to ensure cost reimbursement claims for debris removal work are supported fully with adequate documentation; and
- ensure CalRecycle collects all missing documentation from the contractors before submitting final claims for the grant.

Taking these steps should help FEMA avoid improperly funding any of the \$230 million in contract costs CalRecycle estimates it will claim for damages caused by this disaster. It will also allow CalRecycle the opportunity to supplement deficient documentation or locate missing records before too much time elapses.

Recommendations

We recommend that the Acting Regional Administrator, FEMA Region IX:

Recommendation 1: Direct California, as recipient, to provide CalRecycle with technical assistance to ensure compliance with all applicable Federal regulations, specifically for document support and contract management, and to avoid improperly funding any of the \$230 million (\$173 million Federal share) in contract costs CalRecycle estimates it will claim for damages caused by this disaster.

Recommendation 2: Direct California, as recipient, to ensure that all CalRecycle's cost reimbursement claims for debris removal work are supported with adequate documentation and that costs are eligible in accordance with FEMA's debris removal guidelines.



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Discussion with Management and Follow-Up

We discussed our observations with FEMA, California, and CalRecycle officials and included their comments in this management advisory report, as appropriate. We also provided a draft advisory report in advance to officials from FEMA on September 22, 2016; California on September 30, 2016; and CalRecycle on October 4, 2016. We also discussed the draft at an exit conference with FEMA on September 26, 2016, and with California and CalRecycle officials on November 2, 2016. FEMA officials agreed with our observations and recommendations, while California and CalRecycle disagreed.

FEMA officials provided a written response on October 24, 2016, agreeing with our observations and recommendations (see appendix B). FEMA expects to complete its proposed corrective actions to address our recommendations by July 31, 2017. Therefore, we consider the two report recommendations to be resolved but open.³ We will close these recommendations when we receive and review documentation that FEMA has completed its proposed corrective actions. Please email closeout documentation and request to Humberto.Melara@oig.dhs.gov.

The Office of Emergency Management Oversight major contributors to this report are Humberto Melara, Director; Louis Ochoa, Audit Manager; Renee Gradin, Auditor-in-charge; Paul Sibal, Auditor; Victor Du, Auditor, and Daniel Flores, Auditor.

Please call me with any questions at (202) 254-4387, or your staff may contact Humberto Melara, Director, Western Regional Office, at (510) 637-1463.

³ FEMA's initial estimated completion date for Recommendation 2 was December 31, 2016. Due to recent disasters in California, we approved an extension to July 31, 2017 to allow FEMA adequate time to respond to the recommendation.



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Appendix A

Objective, Scope, and Methodology

We are currently auditing FEMA Public Assistance grant funds awarded to CalRecycle, Public Assistance Identification Number 000-UUJ4B-00. Our full audit will include a review of four contracts awarded by CalRecycle valued at about \$223 million to perform disaster-related work. Our audit objective will be to determine whether CalRecycle's policies, procedures, and business practices are adequate to account for and expend FEMA Public Assistance Program grant funds according to Federal regulations and FEMA guidelines. We are conducting this audit early in the Public Assistance process to identify areas where CalRecycle may need additional technical assistance or monitoring to ensure compliance, before improperly expending any of the Federal grant funds to be awarded for FEMA Disaster Number 4240-DR-CA.

Our review covers the period September 9, 2015, the first day of the incident period, through September 8, 2016, our cutoff date for this advisory report. As of August 12, 2016, FEMA and California had only drafted the project worksheets to estimate the debris removal costs for the September 2015 wildfires. FEMA plans to provide additional funding for the two large projects as CalRecycle expects debris removal costs to reach about \$230 million. The award provides 75 percent funding for debris removal work for two large projects.⁴

To complete our management advisory report, we interviewed FEMA, California, and CalRecycle officials; assessed the adequacy of the policies, procedures, and business practices CalRecycle uses or plans to use to account for and expend Federal grant funds and to procure and monitor contracts for disaster work; reviewed applicable Federal regulations and FEMA guidelines; and performed other procedures considered necessary to accomplish our objective. We did not perform a detailed assessment of CalRecycle's internal controls over its grant activities because it was not necessary to accomplish our audit objective. We, however, as part of this management advisory, did a limited review of the associated costs. We conducted fieldwork activities at FEMA, California, and CalRecycle offices.

⁴ Federal regulations in effect at the time of the disaster set the large project threshold at \$121,600 [Notice of Adjustment of Disaster Grant Amounts, 79 Fed. Reg. 62,648 (Oct. 20, 2014)].



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Appendix A (Continued)

We are conducting 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 are conducting this audit by applying the statutes, regulations, and FEMA policies and guidelines in effect at the time of the disaster.



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Appendix B
FEMA Region IX Response

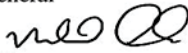
U.S. Department of Homeland Security
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1111 Broadway, Suite 1200
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OCT 24 2016



FEMA

MEMORANDUM FOR: Humberto U. Melara
Director, Western Regional Office
Office of Inspector General

FROM: Robert J. Fenton 
Regional Administrator
FEMA Region IX

SUBJECT: FEMA-4240-DR-CA
Subrecipient: California Department of Resources Recycling
and Recovery
PA ID: 000-UUJ4B-00
Response to Draft Audit Report, OIG-17-###-D, *CalRecycle,
A California State Agency, Does Not Have Adequate
Documentation to Support Fully About \$230 Million in
Disaster-Related Costs*
FEMA Log: 310013.02

On October 17, 2016, the Office of Inspector General (OIG) Western Regional Office transmitted the updated draft audit report *CalRecycle, A California State Agency, Does Not Have Adequate Documentation to Support Fully About \$230 Million in Disaster-Related Costs*. The OIG audited the U.S. Department of Homeland Security's Federal Emergency Management Agency (FEMA) Public Assistance grant funds awarded to California Department of Resources Recycling and Recovery (Subrecipient) under FEMA-4240-DR-CA. The audit report listed the following two (2) recommendations based on findings related to the role and responsibility of FEMA and the California Governor's Office of Emergency Services (Cal OES), as grantee, in ensuring that the County understands Federal requirements associated with Stafford Act disaster recovery grants:

Recommendation 1: Direct California, as grantee, to provide CalRecycle with technical assistance it may need to ensure compliance with all applicable Federal regulations, specifically for contract management, and to avoid improperly funding any of the \$230 million (\$173 million Federal share) in contract costs CalRecycle estimates it will claim for damages caused by this disaster.

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Appendix B (Continued)

*Mr. Humberto U. Melara
Draft Audit Report OIG-17-###-D
FEMA-4240-DR-CA, FEMA Log: 310013.2
Page 2 of 2*

FEMA's Response to Recommendation 1: Concur. FEMA will direct Cal OES, as grantee, to provide the Subrecipient with the technical assistance they may need to ensure compliance with all applicable Federal regulations, specifically addressing contract management and ways to avoid improperly funding any of the \$230 million (\$173 million Federal share) in contract costs the Subrecipient estimates they will claim for damages caused by this disaster.

FEMA considers this recommendation resolved and open. Estimated Completion Date is July 31, 2017.

Recommendation 2: Direct California, as grantee, to ensure that CalRecycle only submits costs reimbursement claims for debris removal work that are supported with adequate contract documentation and that costs are eligible in accordance with FEMA's debris removal guidelines.

FEMA's Response to Recommendation 2: Concur. FEMA works closely with Cal OES and all California subrecipients to ensure that federal regulations regarding the FEMA Public Assistance program are fully understood and properly applied. This is an ongoing and interactive process with seminars, classes, and discussions. Specifically, Cal OES disseminates program specific information, including the importance of adequate documentation and adherence to FEMA's cost eligibility guidelines, during the Applicants' Briefing at the beginning of each new disaster. FEMA then reiterates the information during the Kick-off Meeting. To stress the importance of this information reaching out to all subrecipients, in September 2016, additional trainings were conducted in conjunction with Cal OES to further educate state partners on procurement under FEMA Public Assistance awards. This is an ongoing training process. FEMA will continue to support Cal OES' efforts and obligation to educate and assist the Subrecipient and all public assistance subrecipients throughout California.

FEMA considers this recommendation resolved and open. Estimated Completion Date is December 31, 2016.

In summary, FEMA concurs with Recommendations 1 and 2. FEMA has taken the actions noted above. FEMA requests closure of all recommendations.

If you have any questions or require additional information, please contact William Roche, Recovery Division Director, at (510) 627-7250.



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Appendix C Report Distribution

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