I. EXECUTIVE SUMMARY

The Office of Inspector General reviewed a contract awarded by the City of New Orleans to MWH Americas, Inc. (MWH) to manage the City's program for repair and rehabilitation of City-owned buildings, facilities, and streets. This contract was awarded in December 2007, after the City determined that it was necessary to increase its project management capacity to deal with an unprecedented volume of construction projects to repair damage from Hurricanes Katrina and Rita.

The contract awarded to MWH was based on a request for proposals that sought the services of one person to coordinate all of the City's large scale projects at a maximum annual cost of $150,000. After MWH was selected the parties entered into private negotiations over a four-month period that resulted in a major contract estimated to be worth up to $48 million. The drastic change in the scope and nature of the contract rendered the competitive procurement process irrelevant. Because the City did not require MWH to submit a fee schedule with its proposal, MWH faced no competitive pressure during the fee negotiations.

Through this contracting arrangement, the City in effect privatized major responsibility for managing the City's capital program, transferring many of the management functions formerly conducted by City employees to MWH. This shift of management responsibilities placed a daunting burden on the City to maintain control over the cost of the capital program, including the cost of MWH's fees. The contract terms negotiated by the City, however, did not provide appropriate controls or incentives to contain costs. MWH's compensation was based solely on the number of hours billed without regard to milestones or progress on projects. These terms provided a disincentive to work efficiently and did not allow the City to hold MWH accountable for keeping costs within budget. MWH was also allowed to mark up all direct costs by about 23%. These mark-ups, or cost-plus-percentage-of-cost terms, are prohibited under FEMA reimbursement rules because they provide an incentive to maximize costs.

We determined that City contract oversight was inadequate to protect against excessive fees and inappropriate charges. The City is relying heavily on FEMA reimbursement to fund its capital program, including the cost of MWH's project management services. FEMA has agreed to reimburse the City for MWH's fees on eligible projects provided they do not exceed 8 percent of design and construction cost. The City, however, included non-FEMA eligible work in MWH's contract and did not require MWH to allocate billings on a project-by-project basis, as required by FEMA rules. Concerned about the City's liability for fees that will not be reimbursed by FEMA, the Executive Assistant to the Mayor serving as the Director of the City's Project Delivery Unit (referred to in this report as the "PDU Director") asked a financial management consultant to conduct an analysis of MWH billings under the contract through July 2009. The City's analysis found that MWH billings had far exceeded the rate of progress on projects. In response, the City instituted changes, including reducing the number of projects

MWH would manage to control the spiraling costs. Despite these changes, the compensation structure of the contract continues to hinder the City's ability to control costs.

Other significant problems identified in this report include the City's failure to include a key personnel clause or to establish qualifications for any of the positions identified in the contract's rate schedule, making it difficult for the City to ensure that individuals in key positions have the necessary expertise or that billing rates are justified based on qualifications. The City also failed to require MWH to itemize more than $1.3 million in billings for direct costs. As a result, the City paid blindly for costs without knowing whether the expenses were reasonable or appropriate. We also found that MWH employees submitted reimbursement requests to the company for gifts to City employees and elected officials, including employees responsible for overseeing MWH's work. Under state and local ethics laws, a City employee may not accept gifts or gratuities from anyone who has or seeks to obtain a contract with the employee's agency.

Our review found that the City currently lacks a coherent plan for funding all the recovery projects it has undertaken. The State of Louisiana created a $200 million revolving fund to allow the City access to up-front cash flow while awaiting FEMA reimbursement on recovery projects. The City has relied on this revolving fund to pay for project expenses, including fees to MWH, that will not be reimbursed by FEMA. The City is in danger of exhausting this fund before completing all FEMA-eligible work, thereby jeopardizing critical projects. The City's ability to bring recovery administration and project management costs under control will have profound consequences for the recovery program. The report therefore includes the following recommendations:

Recommendation 1. The City Should Procure a New Contract for Project Management Services.

Recommendation 2. The City Should Develop Contract Terms that Protect the City's Interests and Provide Incentives for Containing Costs.

Recommendation 3. The City Should Institute Effective Contract Oversight Procedures.

Recommendation 4. The City Should Ensure that All City Employees and Elected Officials Receive Training in State Ethics Laws and the City's Code of Ethics.