



U.S. Department of Energy
Office of Inspector General
Office of Audit Services

Audit Report

Audit of Contract Transition
Activities at Los Alamos National
Laboratory

OAS-L-07-16

August 2007

memorandum

DATE: August 7, 2007

Audit Report No: OAS-L-07-16

REPLY TO

ATTN OF: IG-32 (A06LA046)

SUBJECT: Report on "Audit of Contract Transition Activities at Los Alamos National Laboratory"

TO: Deputy Administrator for Defense Programs, National Nuclear Security Administration

INTRODUCTION AND OBJECTIVE

Los Alamos National Laboratory (Los Alamos) is a federally-funded facility located in Los Alamos, New Mexico. Los Alamos' mission is to strengthen the nation's security, enhance the nation's defense, and reduce global terrorism threats related to weapons of mass destruction. The University of California was the sole management and operating contractor of Los Alamos from its inception in 1943 until May 31, 2006.

In May 2005, the Department of Energy (Department) competitively bid the contract to manage Los Alamos and in December 2005 awarded the contract to Los Alamos National Security, LLC (LANS), a limited liability company. LANS is comprised of Bechtel National, Inc.; the University of California; BWX Technologies, Inc.; and the Washington Group International, Inc. The contract, which commenced in June 2006, is for seven years and has a maximum award of about \$13.4 billion, including costs plus incentive fees.

The Department allowed about five months and approximately \$13 million dollars for the transition between contractors to be completed. We reviewed transition costs and activities to determine if costs incurred were allowable per the contract terms and federal guidelines and if the Department effectively managed the transition.

CONCLUSIONS AND OBSERVATIONS

Except as noted below, nothing came to our attention during the audit to indicate that the Department did not effectively manage the transition. However, we noted that pre-existing conditions identified during the transition and additional costs resulting from the change in contractors present financial and operational challenges.

During the course of the transition, LANS inspected numerous Los Alamos facilities and operations to identify any pre-existing conditions that might increase financial and operational risk. As a result of the inspections, LANS reported 58 conditions that require corrective action. These include action in major risk areas such as fire protection, nuclear criticality safety, environmental cleanup, cyber security, and weapons quality. For example, widely reported cyber security breaches that occurred at Los Alamos shortly after the transition illustrated the importance of expeditiously correcting major risk areas identified in the pre-existing conditions. In a Memorandum to the Secretary "Selected Controls Over Classified Information at the Los Alamos National Laboratory" (November 27, 2006), we reported that, although cyber security has been an area of particular interest over the years, significant procedural weaknesses continued to exist.

According to LANS management, each of the conditions identified was assigned to a high level manager responsible for developing and implementing a corrective action plan. Oversight of the action plans will be monitored by the Department's Los Alamos Site Office.

We noted that plans to correct some of the conditions will require a substantial amount of time and effort. In one case, a large environmental cleanup project is expected to take until 2015 to complete. The total estimated cost for the cleanup is \$1.7 billion. The Department and LANS agreed to address pre-existing conditions within current appropriations, which have remained fairly constant over the last five years at about \$2 billion.

LANS will also incur increased expenses related to the terms of the LANS contract. LANS reported that expenses would increase by about \$176 million over the previous contractor's expenses, due to increases in salary and 401K benefits, management fees and performance incentives, and New Mexico taxes. The Department and LANS agreed that increased costs could be absorbed through efficiencies and cost cutting measures, including voluntary attrition, redeployment of staff, and reductions in non-labor items (travel, materials, equipment, indirect costs, and subcontract services).

Correcting costly pre-existing conditions and absorbing increased contract costs within existing budgets is a significant challenge for the Department and LANS.

Our review also identified \$22,335 in questioned travel costs incurred during the transition. We have conveyed details of the questioned costs to the contracting officer for an allowability of cost determination.

RECOMMENDATIONS

Given the challenges associated with implementing substantial corrective actions at the same time as reducing costs, we recommend that:

1. The Manager, Los Alamos Site Office carefully monitor LANS progress on correcting pre-existing conditions and implementing cost cutting measures, and,

2. The Contracting Officer, Los Alamos Site Office make a determination regarding the allowability of questioned travel costs.

MANAGEMENT COMMENTS AND AUDITOR RESPONSE

The National Nuclear Security Administration (NNSA) agreed with the report and recommendations. NNSA agreed with our recommendation concerning the pre-existing conditions because it described its approach to contractor assurance, and agreed to make a determination on the allowability of questioned costs.

Management's comments and planned actions, if properly implemented, are responsive to our recommendations.

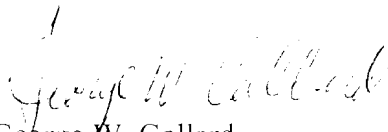
Management's comments are attached in their entirety.

SCOPE AND METHODOLOGY

We reviewed the transition costs and activities related to the change in prime contractors at Los Alamos National Laboratory to determine if activities were effectively managed and costs were in compliance with contract terms and federal acquisition regulations. The audit was conducted between June 2006 and March 2007 at Los Alamos National Laboratory.

We conducted our review in accordance with generally accepted government auditing standards. We included tests of compliance with those laws and regulations which could, if not observed, have a direct and material effect on the internal control structure. The criteria used to evaluate the costs and activities include the terms of the contracts, Federal Travel Regulations, Chapter 301, and FAR 31. While we did not rely on computer-processed data to satisfy the audit objective, we confirmed the validity of such data, when appropriate, by reviewing supporting source documents such as invoices and vouchers.

Management waived an exit conference.


George W. Collard
Assistant Inspector General
for Performance Audits
Office of Inspector General


Attachment

cc: Chief of Staff
Director, Policy and Internal Controls Management, NA-66
Manager, Los Alamos Site Office
Team Leader, Audit Liaison Team, CF-1.2



Department of Energy
National Nuclear Security Administration
Washington, DC 20545

MEMORANDUM FOR Joanne Hill
Director
NNSA Audits Division

FROM:  7/30/07
Richard Speidel
Director
Policy and Internal Controls Management

SUBJECT: Comments to Draft Report on LANL
Contract Transition Activities: A06LA046;
IDRMS No. 2006-18424

The National Nuclear Security Administration (NNSA) appreciates the opportunity to review the Inspector General's (IG) draft report, "Contract Transition Activities at Los Alamos National Laboratory." We understand that the scope of the audit was for the IG to review the transition costs and activities to determine if costs incurred were allowable per the contract terms and federal guidelines. We also understand that the IG wanted to determine if NNSA had effectively managed the transition.

NNSA agrees with the report and its corresponding recommendations. We appreciate the fact that the IG has stated that, during the audit, they did not find anything that would indicate that NNSA did not effectively manage the contract transition. Regarding the questioned costs cited in the report, the Contracting Officer will make a cost determination on the allowability of travel costs about which the IG had questions.

The IG also recommended that the new contractor continue its progress and the Federal establishment should monitor the progress on correcting pre-existing conditions and implementing cost cutting measures. NNSA appreciates the recommendation because it describes the basis precept of the Contractor Assurance System.

Should you have any questions about this response, please let me know.

cc: Donald Winchell, Manager, Los Alamos Site Office
David Boyd, Senior Procurement Executive
Karen Boardman, Director, Service Center

