



U.S. Department of Energy
Office of Inspector General
Office of Audits and Inspections

AUDIT REPORT

The Office of Fossil Energy's Regional Carbon
Sequestration Partnerships Initiative

OAI-M-16-03

December 2015



Department of Energy
Washington, DC 20585

December 18, 2015

MEMORANDUM FOR THE ASSISTANT SECRETARY, OFFICE OF FOSSIL ENERGY

FROM: *Daniel M. Weeber*
Daniel M. Weeber
Assistant Inspector General
for Audits and Administration
Office of Inspector General

SUBJECT: INFORMATION: Audit Report on the “The Office of Fossil Energy’s
Regional Carbon Sequestration Partnerships Initiative”

BACKGROUND

The Office of Fossil Energy (Fossil Energy) Regional Carbon Sequestration Partnerships Initiative (Initiative) was established in 2003 to develop the technology, infrastructure, and regulations needed to implement large-scale CO₂ storage in different regions and geologic formations. The Initiative involves seven regional partnerships that are comprised of state agencies, universities, and private companies. Overall, the partnerships represent more than 400 unique organizations in 43 States and 4 Canadian Provinces. Funding is provided to the regional partnerships through cooperative agreements valued at about \$829 million, with the Department of Energy (Department) share totaling approximately \$591 million and partner members contributing about \$238 million on a cost-share basis. As of April 2015, about \$503 million of the Department’s share had been obligated, of which approximately \$378 million had been reimbursed in claimed costs.

The Office of Inspector General has considered contract and financial assistance award management to be a significant management challenge for a number of years. For example, our audit report on *The Department of Energy’s Industrial Carbon Capture and Storage Program Funded by the American Recovery and Reinvestment Act* (OAS-RA-13-15, March 2013) found that the Department had not always effectively managed the Industrial Carbon Capture and Storage Program and the use of *American Recovery and Reinvestment Act of 2009* funds. In light of previous concerns and the significant amount of funding for the Initiative, we initiated this audit to determine whether the Initiative was managed in an effective and efficient manner.

RESULTS OF AUDIT

The Department had not always effectively managed the Initiative’s financial assistance awards. In particular, our testing revealed that one of the two partnerships we reviewed, the Midwest Geological Sequestration Consortium, managed through a cooperative agreement with the University of Illinois, had been reimbursed or allowed to claim cost share for approximately

\$5.1 million in unsupported and questionable project costs incurred by one of its subrecipients, Schlumberger Carbon Services (Schlumberger). Specifically, the Department reimbursed the University of Illinois approximately \$3.8 million in costs that were unsupported, accepted \$1.2 million in claimed cost sharing that was similarly unsupported, and reimbursed the University of Illinois for at least \$48,000 in costs that were questionable and/or specifically unallowable under Federal regulations or the terms of the financial assistance agreement.

With regard to the other reviewed partnership, the Midwest Regional Carbon Sequestration Partnership, managed through a cooperative agreement with Battelle Memorial Institute, nothing came to our attention to indicate that it had not implemented appropriate controls to ensure that only adequately supported and allowable costs were charged to the Department. Specifically, we did not identify any significant issues based on the results of our transaction testing.

Furthermore, we determined the Initiative had made significant progress toward achieving its mission, objectives and goals, and had demonstrated that greenhouse gas emissions can be sequestered in various geologic formations. The Department reported that, as of November 2014, the Initiative had injected more than 7.2 million metric tons of CO₂ into various geologic formations.

Unsupported Intradivision Costs

We found that Schlumberger had not provided to the University of Illinois sufficient supporting documentation for about \$5 million in claimed costs in the sample of invoices we reviewed associated with intradivision transactions within the company. Absent detailed documentation to support these transactions, we were unable to determine whether these costs charged to the project were reasonable, allowable, or allocable to the project. As such, we question approximately \$5 million in costs claimed as unsupported, including approximately \$3.8 million in reimbursements and \$1.2 million in cost share.

The terms and conditions of the subaward agreement included a clause indicating that direct costs had to be adequately supported with detailed receipts, and that the level of detail provided must clearly indicate where funds were expended. Specifically, support for labor costs must include labor category, hourly rate, and the labor cost per category; equipment costs must be supported by a voucher/receipt or invoice; supporting data for travel must include transportation and per diem costs; and supplies should be labeled by category and supported by receipts. However, we found that Schlumberger had not provided the University of Illinois with adequate support, but instead included “one line” explanations for approximately \$3.8 million in reimbursed costs attributed to the intradivision transactions. For example, intradivision costs submitted and reimbursed included the following:

- A \$330,000 invoice with a description indicating total amounts for “Job Charges,”
- A \$18,711 invoice for four employees’ time charges with no descriptive detail and/or supporting timecards, and
- A \$75,000 invoice with a description of total charges for “work completed so far.”

When we requested additional supporting documentation for these three costs, Schlumberger was unable to provide additional sufficient supporting details.

Similarly, Schlumberger failed to provide adequate supporting documentation for approximately \$1.2 million in costs it claimed as cost share, as required by the subaward. In particular, Schlumberger provided to the University of Illinois only a spreadsheet with high-level costs without a detailed breakdown of the costs as support for \$1 million of cost share. Similarly, for the remaining \$200,000, we found the same type of high-level documentation without detail. During our review, the Department requested additional detail from Schlumberger; however, they concluded that no additional detail was available. Subsequently, the Department agreed that there was insufficient detail to support the cost share claimed. The Department's financial assistance regulations in 10 CFR 600.313, require that all costs claimed as cost share be verifiable from the recipient's records.

Other Unsupported and Unallowable Costs

During our review of selected invoices, we found that Schlumberger had charged, and been reimbursed, over \$48,000 in costs that were either unsupported or unallowable under the terms and conditions of the subaward, as well as Federal regulations. The Department's Financial Assistance Rules require that recipients of financial assistance awards have a system of internal controls, as well as accounting systems in place, to ensure that unallowable costs are not charged to the Government. Of the costs incurred by Schlumberger for which details were available, we identified a number of unallowable costs. For instance, we identified the following reimbursements:

- About \$41,000 in estimated costs pending "price quotes." Payment of estimated costs is not allowable per the terms and conditions of the subaward agreement.
- Alcohol, in the amount of approximately \$230, that was included in travel and business meal expenses. Reimbursements for alcohol are unallowable under FAR Part 31.205-51.
- Unsupported travel and business meals in the amount of about \$2,850. In some cases, no receipts were provided, and in other instances only a credit card receipt with no detailed information was provided. In the absence of these details, it is impossible to ascertain whether charges were allowable or reasonable. Per the Federal Travel Regulation and Schlumberger's policies, which are applicable to the subaward, a detailed receipt is required for actual meal expenses.
- More than \$4,500 for business meals where a listing of participants had not been provided. While FAR Part 31.205-43(c) allows for reimbursement of meals at business meetings, it also requires that any individuals in attendance be essential to achieve the purpose of the meeting. Similar to the example above, without this detail, it is impossible to determine whether participants were essential, whether the cost would be

unallowable entertainment under FAR Part 31.205-14, and whether the cost was allowable and reasonable per FAR Parts 31.201-2 and 31.201-3. Further, Schlumberger's own policies require documentation of these participants.

- Costs that were identified as entertainment or gifts, which are unallowable under FAR Part 31.205-13 and Part 31.205-14. Specifically, in one instance, Schlumberger was reimbursed \$664 for costs identified as "Entertainment (Clients)" by one of its divisions. There were no additional details or receipts associated with the charge. In another instance, Schlumberger was reimbursed for a gift certificate provided to an individual associated with the project. However, because the amount of the gift certificate had been lumped into other costs and no supporting details had been provided, we were unable to determine the exact amount of the gift certificate.

Performance Monitoring and Oversight

The issues we identified occurred, in part, because the Department had not ensured that the University of Illinois fully reviewed Schlumberger's invoices to verify that costs were adequately documented. Further, the Department had not fully considered or taken timely action on the results of prior audit reports.

Billing Oversight

The Department had not ensured that the University of Illinois fully reviewed claimed costs submitted by Schlumberger, including amounts reimbursed or claimed as cost share, to verify that costs were adequately documented. The Department's financial assistance regulations, found in 10 CFR 600.151, state that recipients are responsible for managing and monitoring all aspects of the project, including subawards. Department officials told us that requirements to flow down certain terms from the cooperative agreement to subrecipients and the recipient's obligation to provide oversight of its subrecipients and vendors are designed to facilitate the compliance with laws and financial assistance regulations by all project participants. As stated above, the terms and conditions of the subaward agreement clearly defined the required detailed documentation that should have been submitted for reimbursement of project costs. However, the University of Illinois did not identify or question the lack of adequate support for intradivision work. Although officials asserted that they performed both financial and technical monitoring of the awards, they acknowledged that in this case, the lack of detailed supporting documentation may have hampered their review of the financial aspects of the monitoring process. Additionally, a more robust review by the University of Illinois could have identified some of the questioned costs from our review. Specifically, the estimated costs, the costs for business meals, and the costs associated with alcohol were clearly identifiable based on documentation submitted.

Prior Audit Report Findings

The Department had not always considered Office of Management and Budget Circular A-133 (A-133) audit findings and recommendations, nor had it taken timely action on the Defense Contract Audit Agency's (DCAA) audits in managing the project. Department officials stated that for existing financial assistance awards, they review all recent audit information prior to any

budget continuations or other major actions, such as budget revisions. However, we noted that these budget actions frequently occurred several years after the audits are conducted. Prior audit reports conducted on the University of Illinois and Schlumberger raised several red flags regarding weaknesses associated with accounting systems. Specifically:

- A University of Illinois FY 2012 A-133 audit report contained a finding and recommendation related to an “inadequate process for monitoring cost share requirements.” The audit found that the University of Illinois did not have an adequate process in place to ensure expenditures used to meet cost sharing requirements were allowable. In particular, information provided by a University of Illinois subrecipient was not sufficient to allow the University of Illinois to determine whether the costs met allowable cost criteria, including whether the expenditures were adequately supported and documented by the subrecipient.
- The Department requested several audits of Schlumberger from DCAA. Because Schlumberger had no previous Government audit history, DCAA performed a pre-award audit and a subsequent audit of its accounting system. The accounting system audit found significant deficiencies that were considered to be material weaknesses in Schlumberger’s accounting system and concluded that incorrect charges and billings to Government contracts could occur as a result. In particular, the audit found that Schlumberger was summarizing costs rather than providing the amount of detail required by the current contract, such as labor categories, hourly rates, and labor costs per category. As such, DCAA recommended the Department pursue suspension of a percentage of progress payments or reimbursement of costs. Even though the payment suspension criteria cited by the DCAA report were not specific to the Department, similar provisions within the Department’s regulations were available to address the recommendation.

Had the Department followed up on the findings and recommendations from these prior audit reports, it is likely that the questioned costs identified in our review would not have occurred or would have been detected in a timelier manner.

Impact and Path Forward

Without effective financial management of the partnership awards under the Initiative, there was an increased risk that questionable and/or unallowable costs would be charged, resulting in wasted and misused taxpayer dollars and effectively reducing the amount of funds available for the project objectives. We believe control weaknesses identified in our report could result in similar issues with other partnerships awards under this Initiative. Specifically, we found that Schlumberger was also a participant on other regional partnerships. If the same conditions exist with those agreements, then it is likely that the Initiative has substantially higher unsupported and questionable costs.

Given that more than \$200 million budgeted for the Initiative remained to be expended as of August 2015, the Department has an opportunity to make improvements to enhance the management of the Initiative’s financial assistance awards, as well as other Federal awards.

RECOMMENDATIONS

To address the issues identified in our report, we recommend that the Assistant Secretary for the Office of Fossil Energy:

1. Direct the Contracting Officer to resolve the identified questioned costs totaling about \$5.1 million;
2. Emphasize to the Initiative's financial assistance recipients their responsibility to provide sufficient oversight of costs claimed by and reimbursed to subrecipients;
3. Develop a comprehensive process to address and/or consider findings and recommendations from relevant external audit reports in a timely manner to ensure proper controls are in place; and
4. Identify other Fossil Energy projects for which Schlumberger is a participant, and review costs for issues similar to those we identified.

MANAGEMENT RESPONSE

Management generally agreed with the findings, concurred with the recommendations, and provided corrective actions to address the issues identified in the report. Specifically, Fossil Energy agreed to resolve questioned costs and take appropriate actions regarding any costs determined unallowable. In addition, Fossil Energy stated that it would reinforce to recipients their responsibilities for oversight of subrecipients' costs, enhance its procedures for identifying and tracking external audit reports, and identify other projects for which Schlumberger is a participant and review billings for possible unsupported and unallowable costs. Management's response also reiterated and clarified some points of information made orally to the Office of Inspector General with respect to certain findings. Management's formal comments are included in Attachment 3.

AUDITOR COMMENTS

We consider management's comments and planned corrective actions to be responsive to our findings and recommendations. Additionally, we considered management's suggested clarifications to the report and made revisions, as appropriate.

Attachments

cc: Deputy Secretary
Under Secretary for Science and Energy
Chief of Staff

OBJECTIVE, SCOPE, AND METHODOLOGY

OBJECTIVE

The objective of this audit was to determine whether the Office of Fossil Energy's Regional Carbon Sequestration Partnerships Initiative (Initiative) was managed in an effective and efficient manner.

SCOPE

We conducted the audit from March 2014 to December 2015 at the National Energy Technology Laboratory in Pittsburgh, Pennsylvania; two cooperative agreement awardees, Battelle Memorial Institute in Columbus, Ohio, and the University of Illinois in Champaign, Illinois; and one subrecipient, Schlumberger Carbon Services in Denver, Colorado. The scope included management of Initiative funds between 2008 and 2014. We conducted this audit under the Office of Inspector General project number A14PT028.

METHODOLOGY

To accomplish our audit objective, we:

- Reviewed and summarized Initiative background.
- Reviewed laws, regulations, policies, and procedures related to the Initiative and Federal financial assistance awards.
- Reviewed prior reports issued by the Office of Inspector General, the Government Accountability Office, the Defense Contract Audit Agency, and independent accounting firms under the *Single Audit Act* and the Office of Management and Budget Circular A-133.
- Interviewed selected financial assistance recipient and subrecipient project officials to discuss project status, roles and responsibilities, results of audit findings, procurement procedures, and supporting details for costs incurred.
- Interviewed Department of Energy (Department) project managers and contract specialists responsible for the regional partnerships to determine the status of each project, and technical and financial monitoring activities.
- Obtained and reviewed award documentation and selected invoices for each of the seven recipients in the Initiative from Department files and information systems, including the Strategic Integrated Procurement Enterprise System, Financial Accounting Support Tool, Vendor Invoice Approval System, and Federal Information Tracking System.
- Judgmentally selected two of the seven awards to conduct site visits. We judgmentally selected sites based on the value of the award and amounts reimbursed. Additionally,

we took into consideration findings and recommendations based on external audit reports. Further, based on an initial review of information at one of the recipients, we selected and conducted a site visit at one of the subrecipients.

- At the two recipients visited, we selected a sample of invoices for review. Invoices were judgmentally selected based on dollar value and project stage, i.e., invoices from both early in the project and current at the time of our audit. The sample included eight invoices totaling \$5.2 million from a universe of \$114.6 million. Because our sample was not statistical, we could not project the sample results to the universe of costs charged to the projects.
- At the subrecipient, we selected a sample of 28 invoices totaling about \$7.6 million, from a universe of 86 invoices with a total value of almost \$25.5 million. Initially, we randomly selected 20 invoices during our site visit to the subrecipient. Subsequently, we judgmentally selected an additional eight subrecipient invoices that coincided with, and allowed for a comparison against, the recipient invoices we reviewed (as previously noted in the bullet above). Because our total sample was not statistical, we could not project the sample results to the universe of costs charged to the Initiative.
- At the sites visited, we reviewed selected costs claimed and reimbursed; the amount of cost share negotiated, approved, or claimed; internal and external audits and reviews; financial oversight policies and procedures; subcontracting practices, policies, and procedures related to Government projects; and the status of work planned or completed on the projects.

We conducted this performance audit in accordance with 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 on our audit objective. We believe that the evidence obtained provided a reasonable basis for our findings and conclusions based on our audit objective. In particular, we assessed compliance with the *GPRA Modernization Act of 2010* and found that performance measures had been established for the Initiative. Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. Finally, we conducted an assessment of computer-processed data relevant to our audit objective by comparing the data to source documents. We determined the data to be reliable for our purposes.

Management waived an exit conference on December 8, 2015.

RELATED REPORT

Audit Report on [*The Department of Energy's Industrial Carbon Capture and Storage Program Funded by the American Recovery and Reinvestment Act*](#) (OAS-RA-13-15, March 2013). This report found that the Department of Energy (Department) had not always effectively managed the Industrial Carbon Capture and Storage Program and the use of *American Recovery and Reinvestment Act of 2009* (Recovery Act) funds. Specifically, the Department had not adequately documented the approval and rationale to use \$575 million to accelerate existing projects rather than proceeding with new awards as required by Federal and Department policies. In addition, the Department reimbursed recipients approximately \$16.8 million without obtaining and/or reviewing adequate supporting documentation. Furthermore, three recipients were awarded more than \$90 million in Recovery Act funding even though the projects experienced financial and/or technical issues prior to being recommended for selection. Finally, the Department had not ensured that recipient subcontractor or vendor selections for goods and services represented the best value to the Government.

MANAGEMENT COMMENTS



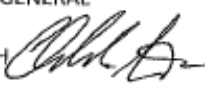
Department of Energy

Washington, DC 20585

November 12, 2015

MEMORANDUM

TO: RICKEY R. HASS
DEPUTY INSPECTOR GENERAL FOR AUDITS AND
INSPECTIONS
OFFICE OF INSPECTOR GENERAL

FROM: CHRISTOPHER A. SMITH 
ASSISTANT SECRETARY
OFFICE OF FOSSIL ENERGY

SUBJECT: Response to Office of Inspector General Draft Audit Report on the "The Office of Fossil Energy's Regional Carbon Sequestration Partnerships Initiative"

The Office of Fossil Energy (FE) appreciates the opportunity to review the Office of Inspector General's (OIG) September 2015 Draft Audit Report entitled, "The Office of Fossil Energy's Regional Carbon Sequestration Partnerships Initiative." FE generally agrees with the findings and recommendations in the report. The following reiterates some of the points of information and clarification made orally to the OIG audit staff with respect to certain findings:

- Both FE and its recipients operated under guidance issued as projects (including carbon sequestration regional partnership projects) transitioned from the Automated Standard Application for Payments (ASAP) system method of reimbursement to the Automated Clearing House (ACH) method.
- Both the requirement to flow down certain terms from the cooperative agreement to sub-contractors and the prime recipient's obligation to provide oversight of its sub-contractors and vendors are designed to facilitate their compliance with laws and financial assistance regulations by all project participants, as DOE lacks privity with sub-contractors and vendors.
- An overall process already exists wherein prior to a new financial assistance award, to any budget period continuation, or to other major action (e.g., budget revision), the Contract Specialist reviews all recent audit information. Any identified findings or material weaknesses are addressed prior to award.
- The Contracting Officer for Indirect Rate Management tracks audit findings in the Departmental Audit Report Tracking System (DARTS). The Cost/Price Team is responsible for updating DARTS for FE programs.
- For recipient accounting system audits, a Cost Price Analyst requests the audit from the Defense Contract Audit Agency or from an independent audit firm based on an identified need. The Cost Price Analyst tracks and reads the report when it arrives. Relevant findings are passed on with recommendations. Actions depend on the recipient, whether NETL is the



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cognizant federal agency, and other factors, such as the audit being identified as a high priority.

We appreciate the review by OIG as we continue to work to improve our Regional Carbon Sequestration Projects. Specific responses to your recommendations are provided below.

OIG Recommendation 1: Direct the Contracting Officer to resolve the identified questioned costs totaling about \$5.1 million.

FE Response: FE concurs with this recommendation. The Contracting Officers will make determinations on all costs questioned. Appropriate steps will be taken regarding any costs determined to be unallowable.

OIG Recommendation 2: Emphasize to the Initiative's financial assistance awardees their responsibility to provide sufficient oversight of costs claimed by and reimbursed to sub-awardees.

FE Response: FE concurs with this recommendation. FE will reinforce the role and duties of the recipients by reminding them in writing and at meetings of their responsibilities for oversight of subawardees' costs. Recently issued financial assistance regulations emphasize the responsibilities of prime recipients for subcontract oversight and management. FE will continue to ensure that oversight requirements are provided to both the recipient's principal investigator and its business manager.

OIG Recommendation 3: Develop an overall process to address and/or consider findings and recommendations from relevant external audit reports in a timely manner to ensure proper controls are in place.

FE Response: FE concurs with this recommendation. The current process has defined responsibilities for Cost Price Analysts with regard to external audit reports. Additional assurance will be gained with the increased emphasis on prime recipients' oversight and management of subcontracts under the new financial assistance regulations and through the following steps:

1. Cost Price Analysts will be directed to issue division-wide e-mails informing Acquisition and Assistance Division personnel when an external audit report is received that contains one or more material weaknesses or material costs exceptions that cast doubt on the financial integrity of the audited entity.
2. Management Decision Letters prepared as the result of an audit of a for-profit recipient will be placed in a common location available to all Acquisition and Assistance Division's staff.

OIG Recommendation 4: Identify other Office of Fossil Energy projects and review costs for issues similar to those we have identified.

FE Response: FE concurs with this recommendation. It will identify other FE projects where this entity is a participant. So far, this entity has been identified as a prime recipient, a sub-awardee or a vendor providing cost share in 16 awards. With respect to reviewing costs for issues similar to those that OIG Identified, FE will: (1) consider the results from Recommendation 1; and (2) allow the Defense Contract Audit Agency to complete its current audit of the entity. Based on those results, FE will develop a plan for investigating the entity's costs under other FE awards.

FEEDBACK

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Office of Inspector General (IG-12)
Department of Energy
Washington, DC 20585

If you want to discuss this report or your comments with a member of the Office of Inspector General staff, please contact our office at (202) 253-2162.