United States Government

Department of Energy

memorandum

DATE: February 9, 2006

Audit Report Number: OAS-L-06-07

REPLY TO ATTN OF: IG-32 (A05OR014)

SUBJECT: Audit of "The Department's Management of United States Enrichment Corporation Site Services"

TO: Manager, Portsmouth/Paducah Project Office

INTRODUCTION AND OBJECTIVE

The Paducah Gaseous Diffusion Plant (Paducah), located in western Kentucky, was constructed by the Department of Energy (Department) in the early 1950s to enrich uranium for use in various military and commercial applications. The Department operated the plant until the Energy Policy Act of 1992 created the United States Enrichment Corporation (USEC) as a Government-owned corporation and directed that Paducah be leased to USEC. USEC operated Paducah as a Government-owned corporation until July 1998, when the Government privatized USEC by selling stock in the corporation to the public. USEC still operates Paducah according to the terms of a 1993 lease with the Department.

The Department's mission at Paducah is primarily related to environmental restoration and legacy waste management. Additionally, the Department retained responsibility for decommissioning the site's uranium enrichment facilities upon final plant shutdown. These activities are managed by the Office of Environmental Management and Bechtel Jacobs Company, LLC (Bechtel Jacobs) is currently performing environmental cleanup activities at Paducah under a cost reimbursable contract.

Exhibit F to the lease, *Memorandum of Agreement between United States Department of Energy and United States Enrichment Corporation for Services*, states that USEC can provide services to the Department at costs to be negotiated for each service. In Fiscal Years (FY) 2002 through 2005, the Department and Bechtel Jacobs purchased about $45.5 million in services from USEC to support its environmental restoration and waste management mission at Paducah. We conducted this audit to determine if the Department managed the cost of services provided by USEC.

CONCLUSIONS AND OBSERVATIONS

We identified instances where the Department and its contractor paid for services provided by USEC, through indirect charges and overhead rates, without assuring that they received the full benefit from such costs. In total, these costs are estimated to be about $922,000, of which about $149,000 recur each year.

Additional costs that USEC charged to Bechtel Jacobs through indirect charges and overhead rates following a February 2003 employee strike at Paducah have not been audited. Federal Acquisition Regulation (FAR) section 22.101.2(c) requires that all costs incurred during strikes be carefully examined to ensure that only those costs necessary for performing the contract in accordance with the Government's essential interest be recognized. In 2004, based on an adjustment of 2003 provisional billing rates, USEC issued an adjustment voucher to Bechtel Jacobs which included, but did not segregate out, additional costs resulting from the 2003 strike. Bechtel Jacobs paid USEC, and the Department provisionally reimbursed Bechtel Jacobs for these additional costs without first ensuring that they benefited the Government. Although the Department was aware that the strike likely increased its costs, it was not aware of the extent of the cost increase. USEC estimated that the strike resulted in an additional $773,000 in charges to the Department but it has yet to supply final 2003 incurred cost data to the Defense Contract Audit Agency (DCAA) for audit.

Also, USEC did not allocate indirect security support costs on a cost beneficial basis. This further increased the Department's share of security costs at Paducah. Although security support costs benefited three separate cost objectives – USEC specific activities (23 percent of the cost), Department specific activities (2 percent of the cost), and common site security support (75 percent of the cost), costs were not allocated between these cost objectives. FAR section 31.201-4 required that costs be allocated to cost objectives on the basis of relative benefits received or other equitable relationships. We concluded that security support costs should have been allocated between the Department and USEC on a more equitable basis even though these costs benefited all activities at the site. At our request, USEC prepared an estimate of the impact of its current allocation methodology on the Department's costs. Based on calendar year 2004 provisional billing rates, USEC estimated that not allocating security support pool costs between cost objectives resulted in about $149,000 in additional charges to the Department each year.

The Department believed that purchasing services under the 1993 lease was beneficial since fee was not paid on services provided by USEC under the lease. Additionally, the Department is using DCAA to review USEC's cost accounting standards disclosure statement, indirect billing rates, and incurred cost submissions in an effort to strengthen administrative controls over the acquisition of services. While we acknowledge the Department's attempt at lowering the cost of services purchased from USEC and its use of DCAA's services, we suggest that the Manager, Portsmouth/Paducah Project Office, notify DCAA of the cost allocation issues discussed in this report and determine the allowability of additional costs associated with the 2003 strike and security support costs.

SCOPE AND METHODOLOGY

The audit was performed from May through November 2005, at the Department's Oak Ridge Office in Oak Ridge, Tennessee; the Paducah Gaseous Diffusion Plant near Paducah, Kentucky; and, the Portsmouth Gaseous Diffusion Plant near Piketon, Ohio. The audit scope was limited to services provided by USEC in FY 2002 through 2005. To accomplish the audit objective, we analyzed the 1993 lease agreement between USEC and the Department, the USEC Privatization Act, work authorization documents, and invoices for services provided by USEC.

The audit was performed in accordance with generally accepted Government auditing standards for performance audits and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the audit objective. Accordingly, we assessed the Department's compliance with the Government Performance and Results Act of 1993 and found that the Department had not established performance measures for the acquisition of services from USEC. 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. We did not rely on computer-processed data to accomplish the audit objective, and therefore did not conduct a data reliability assessment.

The Manager, Portsmouth/Paducah Project Office, waived the exit conference. Because no formal recommendations are being made in this letter report, a formal response is not required.

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