



OFFICE OF INSPECTOR GENERAL

U.S. Department of Energy

ASSESSMENT REPORT

DOE-OIG-20-18

December 2019

**AUDIT COVERAGE OF COST
ALLOWABILITY FOR
HONEYWELL FEDERAL
MANUFACTURING & TECHNOLOGIES,
LLC FROM OCTOBER 1, 2014,
TO SEPTEMBER 30, 2015,
UNDER DEPARTMENT OF ENERGY
CONTRACT NO. DE-NA0000622,
AND FROM OCTOBER 1, 2015,
TO SEPTEMBER 30, 2017,
UNDER DEPARTMENT OF ENERGY
CONTRACT NO. DE-NA0002839**



Department of Energy
Washington, DC 20585

December 19, 2019

MEMORANDUM FOR THE MANAGER, KANSAS CITY FIELD OFFICE

A handwritten signature in black ink, appearing to read "John E. McCoy II".

FROM: John E. McCoy II
Deputy Assistant Inspector General
for Audits and Inspections, West
Office of Inspector General

SUBJECT: INFORMATION: Assessment Report on “Audit Coverage of Cost Allowability for Honeywell Federal Manufacturing & Technologies, LLC from October 1, 2014, to September 30, 2015, Under Department of Energy Contract No. DE-NA0000622, and from October 1, 2015, to September 30, 2017, Under Department of Energy Contract No. DE-NA0002839”

BACKGROUND

Since November 2000, Honeywell Federal Manufacturing & Technologies, LLC (Honeywell) managed and operated the National Security Campus, formerly known as the Kansas City Plant, under contract with the Department of Energy’s National Nuclear Security Administration. The National Security Campus manufactures and procures nonnuclear weapon components including electronic, mechanical, and engineered parts that support the national laboratories, universities, and U.S. industry. The National Security Campus was managed under cost-reimbursement management and operating contracts employing performance incentives which ran from October 1, 2010, through September 30, 2015, under contract number DE-NA0000622, and was extended from October 1, 2015, through September 30, 2020, under contract number DE-NA0002839. From October 1, 2014, through September 30, 2017, Honeywell incurred and claimed costs totaling approximately \$2.3 billion.

As an integrated management and operating contractor, Honeywell’s financial accounts are integrated with those of the Department, and the results of transactions are reported monthly according to a uniform set of accounts. Honeywell is required by its contract to account for all funds advanced by the Department annually on its Statement of Costs Incurred and Claimed, to safeguard assets in its care, and to claim only allowable costs. Allowable costs are incurred costs that are reasonable, allocable, and allowable in accordance with the terms of the contract, applicable cost principles, laws, and regulations.

To help ensure only allowable costs were claimed by the Department's integrated contractors and to make efficient use of available audit resources, the Office of Inspector General, the Department's Office of Acquisition Management, and the integrated management and operating contractors and other select contractors implemented a Cooperative Audit Strategy. This strategy places reliance on the contractors' internal audit function to provide audit coverage of the allowability of incurred costs claimed by contractors. The Cooperative Audit Strategy also requires that audits performed internally must, at a minimum, meet the standards prescribed by the Institute of Internal Auditors. Consistent with the Cooperative Audit Strategy, Honeywell is required by its contract to maintain an internal audit activity with responsibility for conducting audits, including audits of the allowability of incurred costs. In addition, Honeywell is required to conduct or arrange for audits of its subcontractors when costs incurred are a factor in determining the amount payable to a subcontractor.

The objectives of our assessment for October 1, 2014, through September 30, 2017, were to determine, based on our limited sampling, whether:

- Honeywell's Internal Audit (Internal Audit) conducted cost allowability audits that complied with professional standards and could be relied upon;
- Honeywell conducted or arranged for audits of its subcontractors when costs incurred were a factor in determining the amount payable to a subcontractor; and
- Questioned costs and internal control weaknesses affecting allowable costs that were identified in prior audits and reviews have been resolved.

RESULTS OF ASSESSMENT

During our assessment, nothing came to our attention to indicate that the allowable cost-related audit work performed by Honeywell's Internal Audit from October 1, 2014, through September 30, 2017, could not be relied upon. We conducted our assessment as a review attestation. A review is substantially less in scope than an examination or audit. Our review was limited and would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our review. Based on our limited sampling, we did not identify any material internal control weaknesses with cost allowability audits, which generally met the Institute of Internal Auditors International Standards for the Professional Practice of Internal Auditing. We observed that Honeywell's Internal Audit identified approximately \$193,760 in questioned costs, which have been resolved and reimbursement has been made to the Department. We did, however, identify issues that need to be addressed to ensure that only allowable costs are claimed and reimbursed to the contractor. Specifically:

- Approximately \$2,957 in questioned costs related to meals and refreshments, late fee costs, and employee educational expenses were not questioned by Internal Audit;
- A Time and Material subcontract with incurred costs totaling approximately \$1,545,078 required an audit but had not been audited;

- Inaccurate listings of subcontracts requiring audit; and
- Sufficient documentation was not always included in the TeamMate workpaper files to support workpaper conclusions.

Questioned and Unresolved Costs

Our retesting of Internal Audit's cost allowability audit work disclosed additional questioned costs. Specifically, we found additional questioned costs totaling approximately \$2,957 that included meals and refreshments, late fees, and employee educational expenses.

Meals and Refreshments

We questioned approximately \$927 for an award luncheon and another approximately \$398 for other meals and refreshment costs. According to the Federal Acquisition Regulation (FAR) 31.205-14, *Entertainment Costs*, the cost of social activities, such as meals, are generally unallowable. Internal Audit stated that it did not question the costs for an award luncheon that celebrated employees for their technical achievements because the prime contract allows for expenses related to rewards and recognition acknowledgement. Although Honeywell's contract clause, Light Refreshments, stated that reasonable expenditures for refreshments such as pastries, coffee, and soft drinks are specifically allowable as part of recognition ceremonies, it did not specifically identify meals as an allowable expense. Additionally, Internal Audit did not question other meals and refreshment costs (e.g., breakfast for supplier diversity event and dinner with students) even though the claimed costs lacked supporting documentation and did not provide an explanation for the nature and purpose of the events. During the course of our assessment, Internal Audit did not provide additional documentation or an explanation to support other meals and refreshment costs referenced above. Honeywell determined that the costs were unallowable and agreed to reimburse the Department for this amount. We requested that the Kansas City Field Office's Contracting Officer make a cost allowability determination on the award luncheon cost, and the Contracting Officer concluded that the cost was unallowable. Honeywell already took action and reimbursed the Department for questioned costs totaling approximately \$1,068 (approximately \$927 plus approximately \$141 in burdened indirect costs).

We also questioned approximately \$1,504 for meal expenses related to pre-employment interviews because the supporting documentation did not contain information necessary to make a determination as to whether or not the costs were allowable. For example, the supporting evidence we reviewed did not always include information such as attendance records, travel status of applicants, or agendas demonstrating that the meals were necessary to the recruitment process. Recruitment costs, including travel costs for applicant interviews, are allowable under FAR 31.205-34, *Recruitment Costs*. In addition, in November 2011, the Department issued Acquisition Letter AL 2012-05, *Meal Costs in Management and Operating Contracts*, which provided additional guidance to Contracting Officers on determining whether meal costs would be allowable under the FAR. The Acquisition Letter states that meals for the applicants are an allowable cost, as a per diem charge, if an applicant is in valid travel status. If an applicant is not in travel status, the cost of the meal would be unallowable unless a justification is provided that demonstrates the meals are necessary for the recruitment process. Internal Audit stated that it did

not question the costs based on the prime contract clause that states that recruitment costs such as participation in corporate recruiting activities are allowable, and that applicants who are requested by the Contractor to report for a pre-employment interview shall be allowed reasonable actual costs of lodging not to exceed per diem, and meal and incidental expenses. During the course of our assessment, Internal Audit provided additional documentation and explanation to support the approximately \$1,504 in pre-employment related meal expenses. Although the Contracting Officer determined the costs to be allowable, the Contracting Officer agreed that supporting documentation could be improved. In addition, the Contracting Officer stated that he would followup with Honeywell to conduct an in-depth review of guides and work instructions to determine which updates and controls have been implemented to ensure clarity and consistency of documentation needed to determine allowability of costs incurred.

Other Questioned Costs

In addition, we questioned costs totaling approximately \$128 that included \$75 in late fees and employee educational expenses totaling approximately \$53. According to FAR 31.205-15, *Fines, Penalties, and Mischarging Costs*, costs of fines and penalties resulting from violations of, or failure of the contractor to comply with, Federal, State, local, or foreign laws and regulations, are unallowable. Furthermore, FAR 31.205-44, *Training and Education Costs*, stated that the educational costs related to the field in which the employee is working are allowable, less financial assistance received from other sources. During our retesting, we found an instance where an employee received an approximately \$53 scholarship from a non-Honeywell source, but the employee did not reduce the educational expenses by the amount of scholarship received. Honeywell agreed with our findings and reimbursed the Department for the unallowable costs totaling approximately \$135, which included approximately \$7 in burdened indirect costs.

Subcontract Not Audited as Required

We found that Honeywell generally conducted or arranged for audits of subcontractors when costs incurred were a factor in determining the amount payable to a subcontractor. However, we identified an approximately \$1,545,078 Time and Material subcontract requiring an audit that had been closed but not audited as required.

Honeywell's subcontract audit process requires Honeywell to hire an external audit firm to conduct closeout audits of Time and Material subcontracts if the subcontract is greater than \$500,000 and if the subcontract is identified as being in need of audit during the risk assessment process. According to a contractor official, Honeywell submitted an approval for a closeout audit in May 2015 to the former Contracting Officer, but the request was not communicated to the incoming Contracting Officer. As a result, a closeout audit was not performed. The Honeywell official is currently following up with the Kansas City Field Office for a path forward. As a result, we consider these subcontract costs, totaling approximately \$1,545,078, as unresolved.

Subcontract Listings Inaccurate

Honeywell did not maintain an accurate listing of subcontract awards. Honeywell maintained a spreadsheet to track cost-type subcontracts and associated audits. However, the spreadsheet did not list every cost-type subcontract that was active from October 1, 2014, through September 30, 2017. Specifically, when we noted a discrepancy while comparing the spreadsheet to the information contained in Honeywell's Supplier Contracts Management system, a Honeywell official discovered that the spreadsheet did not include one subcontract with costs totaling approximately \$2,103,086. According to the Honeywell official, the subcontract was erroneously omitted from the spreadsheet. The official stated that Honeywell has since reviewed its subcontract listing for additional omissions in the spreadsheet.

In addition, we found other discrepancies between the spreadsheet and the information entered into the Supplier Contracts Management system. For example, we found that subcontract totals did not always match between the two. According to the Honeywell official, this occurred because the responsible individuals did not always update the spreadsheet when subcontract modifications were made. The same official stated that Honeywell plans to revise its checklist for monitoring subcontracts so that it includes updating subcontract totals when changes occur.

Furthermore, Honeywell self-identified that there were cost-type subcontracts in the spreadsheet that appear in the Supplier Contracts Management system as fixed-price. The Honeywell official attributed the discrepancies to the methodology used to classify subcontracts in the system. Specifically, the official explained that Honeywell classified its subcontracts based on the majority value of the subcontract. For example, a fixed-price contract with a reimbursable provision is classified as fixed-price if the majority of the subcontract value was awarded on a fixed-price basis. The official stated that in the future, subcontracts with a reimbursable provision will be classified as cost-type contracts.

Audit Documentation Not Sufficient to Support Conclusions

We found that Internal Audit's workpapers did not always include sufficient documentation to support its conclusions. According to Honeywell's Internal Audit Manual, all workpapers related to internal audits are prepared or included in the TeamMate files. However, during our review of Internal Audit's workpaper files, we did not always find sufficient documentation in TeamMate that would allow us to reach the same conclusions as Internal Audit. Internal Audit has since provided additional documentation and explanations that supported its conclusions. As required by the standards prescribed by the Institute of Internal Auditors, sufficient documentation is necessary to support the engagement's results and conclusions. Furthermore, the current Internal Audit Manual states that sufficient documentation should be included in TeamMate so that a cold reader could review the documentation that was used to reach audit conclusions.

RECOMMENDATIONS

We recommend that the Manager, Kansas City Field Office, direct the Field Office Contracting Officer to ensure that:

1. Costs determined to be unallowable, in this report, are recovered;
2. Honeywell performs or arranges for an audit of the identified Time and Material subcontract;
3. Honeywell's listing of subcontracts requiring audit is accurate and complete; and
4. Internal Audit maintains sufficient documentation in its workpapers to support conclusions reached in completed audits.

MANAGEMENT RESPONSE AND AUDITOR COMMENTS

Management concurred with the recommendations to recover costs determined to be unallowable, improve the subcontract audit process, and maintain Internal Audit supporting documentation. Management concurred in principle with the recommendation to perform or arrange for an audit of the Time and Material subcontract that met the general requirement for an audit; however, Honeywell requested that the Contracting Officer consider an audit waiver for the subcontract due to the age of the purchase order and other technical factors. The Contracting Officer is reviewing Honeywell's request.

Further, management stated that Honeywell is in the process of implementing several controls to ensure that the list of subcontracts requiring audit is accurate and complete, and updating the Internal Audit Department Manual to clarify audit requirements. Management's actions are estimated to be completed by November 30, 2019. We consider management's planned actions to be responsive to our recommendations.

Management's comments are included in Attachment 3.

SCOPE AND METHODOLOGY

This assessment was performed from January 2019 to July 2019 at the National Security Campus offices located in Kansas City, Missouri. The assessment was limited to Internal Audit's activities, subcontract audits, and resolution of questioned costs and internal control weaknesses that affect costs claimed by Honeywell on its Statement of Costs Incurred and Claimed from October 1, 2014, through September 30, 2017. The assessment was conducted under the Office of Inspector General project number A19LV007. To accomplish our objectives, we:

- Assessed allowable cost audit work conducted by Internal Audit which included a review of audit reports, workpapers, auditor qualifications, independence, audit planning (including risk assessments and overall Internal Audit strategy), and compliance with applicable professional auditing standards;
- Interviewed Kansas City Field Office and Honeywell officials;
- Reviewed policies and procedures, and practices for identifying subcontracts that require audit and arranging for such audits;

- Evaluated the resolution of questioned costs and control weaknesses affecting cost allowability that were identified in prior audits and reviews conducted by the Office of Inspector General, Internal Audit, and other organizations; and
- Judgmentally selected 10 of 42 Sundry account transactions and randomly selected 10 of 30 Educational Assistance account transactions that Internal Audit tested in its fiscal year 2017 Allowable Cost Audit for retesting. Based on the result, we expanded our testing of Sundry account transactions related to meals and refreshments. Because the sample selections were not statistical, the results and overall conclusions are limited to the transactions tested and cannot be projected to the entire population.

We conducted our assessment in accordance with generally accepted government auditing standards for attestation engagements. Those standards require that we plan and perform the review to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our objectives. We believe that the evidence obtained provides a reasonable basis for conclusions based on our objectives. A review is substantially less in scope than an examination or audit where the objective is an expression of an opinion on the subject matter and accordingly, for this review, no such opinion is expressed. Also, because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our review. We relied on computer-processed data to accomplish our objectives and determined that the computer-processed data was sufficiently reliable for the purposes of the review.

We held an exit conference on July 15, 2019.

This report is intended for the use of Department contracting officers and field offices in the management of their contracts and is not intended to be and should not be used by anyone other than these specified parties.

Attachments

**SUMMARY OF QUESTIONED/UNAUDITED COSTS FOR HONEYWELL FEDERAL
MANUFACTURING & TECHNOLOGIES, LLC**

Table 1: Questioned Costs

Category	Questioned Costs	Resolved¹	Unresolved
Celebratory Meals	\$927	\$1,068	\$0
Other Meals and Refreshments	\$398	\$398	\$0
Pre-Employment Interview Meals	\$1,504	\$1,504	\$0
Late Fees	\$75	\$82	\$0
Educational Assistance	\$53	\$53	\$0
Total Questioned Costs	\$2,957²	\$3,105²	\$0

Table 2: Unaudited Costs

Category	Unaudited Costs	Resolved	Unresolved
Unaudited Subcontract Costs	\$1,545,078	\$0	\$1,545,078
Total Unaudited Costs	\$1,545,078	\$0	\$1,545,078

¹ The amount includes (if applicable) burdened indirect costs.

² Line item questioned and unaudited subcontract costs were rounded to the nearest dollar. As such, rounding errors have a cumulative effect on the column totals that are either overstated or understated by less than 1 dollar.

PRIOR REPORT

Assessment Report on [*Audit Coverage of Cost Allowability for Honeywell Federal Manufacturing & Technologies, LLC During Fiscal Years 2012 Through 2014 Under Department of Energy Contract No. DE NA0000622*](#) (OAI-V-16-13, September 2016). Based on our assessment, nothing came to our attention to indicate that the allowable cost-related audit work performed by Honeywell Federal Manufacturing & Technologies, LLC's Internal Audit for fiscal years 2012 through 2014 could not be relied upon. We did not identify any material internal control weaknesses with the cost allowability audits, which generally met the Institute of Internal Auditors International Standards for the Professional Practice of Internal Auditing. During its fiscal years 2012 through 2014 audits of cost allowability, Internal Audit identified \$289,110 in questioned costs, all of which had been resolved. Further, we found that Internal Audit had conducted 12 audits of subcontractors totaling \$830,929 and identified \$7,070 in questioned costs, all of which had been resolved.

MANAGEMENT COMMENTS



Department of Energy
Under Secretary for Nuclear Security
Administrator, National Nuclear Security Administration
Washington, DC 20585



September 23, 2019

MEMORANDUM FOR TERI L. DONALDSON
INSPECTOR GENERAL

FROM: LISA E. GORDON-HAGERTY

SUBJECT: Response to the Office of Inspector General Draft Report *Audit Coverage of Cost Allowability for Honeywell Federal Manufacturing & Technologies, LLC, from October 1, 2014, to September 30, 2015, Under Department of Energy Contract No. DE-NA0000622, and from October 1, 2015, to September 30, 2017, Under Department of Energy Contract No. DE-NA0002839 (A19LV007)*

Thank you for the opportunity to review and comment on the subject draft report. We appreciate the auditors' validation of Honeywell Federal Manufacturing & Technologies, LLC's internal audit work. The National Nuclear Security Administration (NNSA) concurs with the Office of Inspector General's recommendations to recover costs determined to be unallowable and to improve the subcontract audit process and audit documentation.

The attachment to this memorandum details actions planned to be taken by NNSA. NNSA subject matter experts have also provided technical comments to your audit team under separate cover. If you have any questions regarding this response, please contact Mr. Dean Childs, Director, Audits and Internal Affairs, at (301) 903-1341.

Attachment



Attachment

NATIONAL NUCLEAR SECURITY ADMINISTRATION**Management Decision**

Audit Coverage of Cost Allowability for Honeywell Federal Manufacturing & Technologies, LLC, from October 1, 2014, to September 30, 2015, Under Department of Energy Contract No. DE-NA0000622, and from October 1, 2015, to September 30, 2017, Under Department of Energy Contract No. DE-NA0002839 (A19LV007)

The Office of Inspector General (OIG) recommended that:

Recommendation 1: The Manager, Kansas City Field Office directs the Contracting Officer to ensure that costs determined to be unallowable in this report are recovered.

Management Response: Concur. The contracting officer will recover costs determined to be unallowable in this report. Estimated Completion Date: November 30, 2019.

Recommendation 2: The Manager, Kansas City Field Office directs the Contracting Officer to ensure that Honeywell performs or arranges for an audit of the identified Time and Material subcontract.

Management Response: Concur in principle. We agree the contract meets the general requirement for audit. Honeywell, however, has requested that the Contracting Officer consider an audit waiver due to the age of the purchase order and other technical factors. The Contracting Officer is currently reviewing and will make a final determination on the request and, if necessary, the file will be sent for audit by November 30, 2019.

Recommendation 3: The Manager, Kansas City Field Office directs the Contracting Officer to ensure that Honeywell's listing of subcontracts requiring audit is accurate and complete.

Management Response: Concur. Honeywell is in the process of implementing several controls to ensure that the list of subcontracts requiring audit is accurate and complete. The enterprise resource planning system will be updated to include additional variable cost contract description options to ensure that all contracts with variable cost components are properly identified in the system. The Buyer Checklist will be revised to require checks for variable cost contracts to ensure they have been properly recorded in the enterprise resource planning system and listed on the spreadsheet, including updates for subsequent price changes. Monthly reports will also be reviewed to identify variable cost contracts and compared to the spreadsheet to ensure that new contracts are added to the spreadsheet in a timely manner. Estimated Completion Date: November 30, 2019.

Recommendation 4: The Manager, Kansas City Field Office directs the Contracting Officer to ensure that Internal Audit maintains sufficient documentation in its workpapers to support conclusions reached in completed audits.

Management Response: Concur. The Internal Audit Department Manual has been updated to clarify requirements and has been reviewed with all auditors. The revision will be approved by the Contracting Office by November 30, 2019.

FEEDBACK

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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) 586-1818. For media-related inquiries, please call (202) 586-7406.