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

Audit Report

Central Office Expenses for the Thomas Jefferson National Accelerator Facility

DOE/IG-0629

December 2003

Department of Energy
Washington, DC 20585

December 8, 2003

MEMORANDUM FOR THE SECRETARY

FROM: Greg Friedman
Gregory H. Friedman
Inspector General

SUBJECT: INFORMATION: Audit Report on "Central Office Expenses for the Thomas Jefferson National Accelerator Facility"

BACKGROUND

The Department of Energy's Thomas Jefferson National Accelerator Facility (Jefferson Lab), located in Newport News, Virginia, is a national user facility for scientific research using continuous beams of high-energy electrons. The Laboratory's primary mission is to probe the nucleus of the atom through the operation of its principal experimental facility, the Continuous Electron Beam Accelerator Facility. In addition, Jefferson Lab participates in the Spallation Neutron Source Project in Oak Ridge, Tennessee, and operates a Free-Electron Laser. Southeastern Universities Research Association, a non-profit consortium of 60 colleges and universities, has been the contractor for the construction and operation of the Laboratory since 1984.

Effective November 1999, Jefferson Lab's contract was modified to permit reimbursement of the contractor's central office expenses. The amount of reimbursable expenses was to be based on contract terms and cost principles established by the Office of Management and Budget for non-profit organizations. Based on issues identified during a periodic audit of Laboratory costs, we initiated this audit to determine whether the Department reimbursed Southeastern Universities Research Association for expenses that exceeded central office charges permitted under Federal cost principles and the terms of the Department's contract.

RESULTS OF AUDIT

As a result of our audit, we questioned about \$4.6 of the \$4.8 million claimed by and paid to the contractor for central office expenses from November 1999 to September 2002. This included central office expenses that were specifically not allowable as well as expenses that were not adequately supported or documented. Specifically:

- Expenses of \$1.7 million that were not allowed by the contract or cost principles, including charges for items such as investment portfolio management, entertainment, alcoholic beverages, and costs incurred in support of unrelated business segments; and,

- Salary and benefit reimbursements of $2.9 million that were supported only by management prepared affidavits completed up to 29 months after the actual work was performed.

We were concerned that the payments to the contractor for unallowable and unsupported expenses were not identified on a "real time" basis by the Department's contract administrator, the Oak Ridge Operations Office. Simply put, we found that Oak Ridge had not provided adequate financial oversight of the contractor's operations. In particular, the contractor was allowed to avoid preparing detailed cost proposals, which are essential elements of an effective contract administration regime. Further, the contractor's delay in submitting required expenditure reports went essentially unchallenged for more than a year. When the reports were eventually submitted, they were insufficiently detailed, and Oak Ridge and its Jefferson Lab Site Office did not require the contractor to provide amplifying information necessary to determine the propriety of specific charges.

Lack of attention by Federal administrators to contractor claims, in our judgment, created an atmosphere in which the contractor sought and received reimbursement for unallowable and inadequately documented home office costs. The Federal funds used to pay these claims should have been employed directly for advancing the scientific mission of the Jefferson Lab.

We recommended that the Contracting Officer make a formal determination regarding the allowability of questioned costs and recover overpayments as appropriate. We also made recommendations designed to enhance financial contract administration activities at the Laboratory.

MANAGEMENT REACTION

Management concurred with our recommendations and agreed to take appropriate corrective action.

Attachment

cc: Deputy Secretary
Under Secretary for Energy, Science and Environment
Director, Office of Science
Director, Office of Management, Budget and Evaluation/Chief Financial Officer
Manager, Oak Ridge Operations Office

CENTRAL OFFICE EXPENSES FOR THE THOMAS JEFFERSON NATIONAL ACCELERATOR FACILITY

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CENTRAL OFFICE EXPENSES

Claimed and Reimbursed Costs

The Southeastern Universities Research Association is the Department of Energy's (Department) contractor for the operation of the Thomas Jefferson National Accelerator Facility (Jefferson Lab). The Jefferson Lab contract provided for reimbursement of central office expenses that are allowed by the cost principles contained in Office of Management and Budget Circular A-122, *Cost Principles for Non-Profit Organizations*. In general, central office expenses are general and administrative expenses incurred by a contractor. Among other things, for a cost to be allowable it must be reasonable, allocable, conform to limitations and exclusions set forth in the principles and in the contract, and be adequately documented. We observed, however, that the Department reimbursed the contractor for a number of costs that were unallowable or not adequately supported. Specifically, in Fiscal Years (FY) 2000, 2001, and 2002, the Department reimbursed the contractor for central office expenses that were prohibited by the contract or cost principles or were not allocable to Jefferson Lab. We also noted other costs for salaries, employee benefits, and administrative expenses that were not adequately supported.

Over a 35-month period, the Department reimbursed the contractor for expenses that were prohibited by the contract and cost principles. These expenses included items such as operating deficits from a residence facility, investment management costs, expenses associated with the contractor's non-Jefferson Lab business segments, and entertainment related costs. For example, the contractor was reimbursed for items such as:

- Expenses of $215,000 for deficits incurred in the operation of the contractor's residence facility even though such costs were specifically prohibited by the contract;
- Costs of $322,000 associated with management of the contractor's investment portfolio, an expense identified by cost principles as unallowable;
- Charges of $203,000 attributable to the contractor's non-Jefferson Lab business segments; and,
- Other expenses for items such as alcoholic beverages, employee commuting expenses, local meals for employees who were not in travel status, contributions, public relations costs, and entertainment expenses including receptions and holiday parties.

We also observed that salary, benefit, and administrative expense reimbursements made by the Department were not properly supported. While the contractor charged expenses based on the percentage of effort that each central office employee devoted to Jefferson Lab contract activities, the only supporting records provided were affidavits that were not timely, sufficient, nor always signed by employees. For example, the affidavits did not adequately support the amount of employee effort devoted to the contract because they were not prepared until 5 to 29 months after completion of work, were prepared to support an entire year of effort, and were frequently not prepared or signed by the employee performing the work. Instead, the affidavits were signed by three senior contractor officials.

Department Oversight

Payments to the contractor for unallowable and unsupported expenses were not identified and corrected because the Oak Ridge Operations Office (Oak Ridge) did not provide adequate financial oversight of the contractor. Prior to November 1999, the contractor was not required to provide Oak Ridge with details of its actual central office expenses because expenses were covered by a fixed management allowance. After the contract was modified, however, Oak Ridge did not increase its financial reviews to ensure that claimed expenses were allowable and properly supported. The lack of financial reviews or close attention to charging methods prevented Oak Ridge from identifying the fact that the contractor did not have a supportable method for charging salaries, employee benefits, and certain administrative costs to the contract.

For example, Oak Ridge did not require the contractor to submit details of its central office expenses, even though the requirement for detailed expense information was spelled out in the contract. The contractor was required to submit annual proposals, 60 days before the start of each fiscal year, to provide details of its central office expenses and certify that the proposals contained no unallowable expenses. Oak Ridge was to use these proposals to determine the amount that it would pay the contractor for central office expenses during the coming year. However, for the three fiscal years we reviewed, Oak Ridge agreed to pay the contractor about $4.9 million without obtaining detailed certified proposals.

In addition, the contract required the contractor to report its actual central office expenses within 120 days after the end of each fiscal year. Oak Ridge, however, did not enforce this provision and continued to reimburse the contractor even though the expense report for FY 2000 was not submitted until March 2002. Besides not being timely, this report and reports for FY 2001 and FY 2002 did not provide sufficient detail for Oak Ridge to determine whether it contained unallowable costs. Neither Oak Ridge nor its Jefferson Lab Site Office took action to obtain clarifying or supporting information regarding claimed central office expenses.

Operational Impacts

Lack of attention to contractor claims may have reduced the general effectiveness of Jefferson Lab by depriving it of funds that could have been used to satisfy operational needs, and substantially increased the risk that unallowable costs would be incurred and not be detected. Funds used to reimburse the contractor for unallowable costs could have been used to address budgetary shortfalls or enhance operations or quality of science at this important national user facility. Without changes, the Department could continue to significantly overpay the contractor for central office expenses while receiving minimal assurance that the amounts claimed are equitable and reasonable.

RECOMMENDATIONS

We recommend that the Manager, Oak Ridge Operations Office:

1. Make a final determination regarding the allowability of the contractor's home office expenses and recover all overpayments;

2. Enhance financial oversight to ensure that future payments only cover allowable expenses;

3. Enforce contractual reporting and certification requirements; and,

4. Ensure that the contractor develops a supportable method for determining the expenses that are to be reimbursed.

MANAGEMENT REACTION

Management concurred with our recommendations and agreed to take action regarding the questioned costs. Management also agreed to enhance financial oversight to ensure that future payments only cover allowable expenses and that the contractor develops a supportable method for determining expenses that are to be reimbursed. Management indicated that it will enforce contractual reporting and certification requirements by requiring the contractor to submit sufficiently detailed reports and certifications within the timeframes established by the contract. Management's comments are included as Appendix 2.

AUDITOR COMMENTS

Management's comments are responsive to our recommendations.

Appendix 1

OBJECTIVE

The objective of this audit was to determine whether the Department paid for only those central office expenses that were allowed by the cost principles and the contract.

SCOPE

The audit was performed as part of our audit of costs claimed for Jefferson Lab under contract DE-AC05-84ER40150 for FYs 2000, 2001, and 2002. The audit was performed at Jefferson Lab in Newport News, Virginia, and at the contractor's office in Washington, D.C., from April to September 2003. The audit scope was limited to Jefferson Lab costs, central office expenses, and fees claimed for FYs 2000, 2001, and 2002. In this report, we are presenting a summary of our findings regarding central office expenses. Details of central office expenses questioned and the result of our audit of Jefferson Lab costs were provided to Oak Ridge in a separate audit report.

METHODOLOGY

To accomplish the audit objective, we:

- Researched applicable laws, regulations, and contract terms relevant to reimbursement of central office expenses;
- Reviewed contractors' expense reports submitted to the Department;
- Tested expense transactions by tracing them to books of original entry and supporting records and documentation;
- Evaluated the contractor's method of computing the amount of central office expenses that were charged to the contract; and,
- Reviewed Oak Ridge's and the Jefferson Lab Site Office's oversight of central office expenses.

The audit was performed in accordance with generally accepted Government auditing standards that applied to this financial-related audit. Criteria used in evaluating the claimed costs included the terms of the contract and applicable cost principles. We obtained a sufficient understanding of the contractor's central office cost accounting system and internal controls to plan the audit and to determine the nature, timing, and extent of tests to be performed. Our purpose was not to form an opinion on the cost accounting systems and internal controls. We relied on computer-processed data to accomplish our audit objective. We conducted limited tests to ensure reliability of the data.

Management waived the exit conference.

DOE F 1325.8
(4/93)

United States Government Department of Energy

Memorandum

DATE: November 10, 2003

REPLY TO
ATTN TO: FM-733:Miller/LM-13:Skinner

SUBJECT: **DRAFT REPORT "CENTRAL OFFICE EXPENSES FOR THE THOMAS JEFFERSON NATIONAL ACCELERATOR FACILITY"**

TO: Rickey R. Hass, Director, Science, Energy, Technology and Financial Audits, Office of Audit Services, Office of Inspector General, IG-34/FORS

This is in response to your October 16, 2003, memorandum, with attached draft report, subject as above. Your memorandum requested that ORO review the information in the draft report and provide written comments within 15 working days on the facts presented and conclusions reached, as well as alternative recommendations in solving the problems discussed in the report.

ORO concurs in the report recommendations, and our comments are attached. Please feel free to contact me at 865-576-4446 if you wish to discuss this further.

Judith M. Penry
Judith M. Penry
Chief Financial Officer

Attachments

cc:
M. D. Johnson, SC-3/FORS
D. G. Kovar, SC-90/GTN
J. J. Fowler, CC-10
J. M. Penry, FM-70
G. J. Malosh, LM-1
J. A. Turi, TJNAF
R. J. France, IG-221/FORS
W. S. Maharay, IG-30/FORS

Attachment 1

OAK RIDGE OPERATIONS OFFICE COMMENTS ON DRAFT INSPECTOR GENERAL REPORT ENTITLED "CENTRAL OFFICE EXPENSES FOR THE THOMAS JEFFERSON NATIONAL ACCELERATOR FACILITY"

<u>RESPONSE TO RECOMMENDATIONS</u>:

1. **That the Manager, Oak Ridge Operations Office make a final determination regarding the allowability of costs incurred by SURA for home office expenses and recover all overpayments.**

   Response: Concur.

   ORO will make a determination regarding the allowability of cost within 90 days after resolution of the False Claims Act (FCA) action or as otherwise directed by the OIG concerning questioned costs appropriate for administrative disposition by DOE and not included in the FCA action.

2. **That the Manager, Oak Ridge Operations Office enhance financial oversight to ensure that future payments are only for allowable expenses.**

   Response: Concur. DOE is in the final year (fiscal year 2004) of its performance-based management contract with SURA, and SURA submitted a cost proposal on September 15, 2003, for the estimated allocable portion of Central Office Expenses for fiscal year 2004 which is based on a revised allocation methodology for Central Office Expenses. At that time, SURA submitted a revised allocation methodology for Cost Accounting Standards Board Disclosure Statement, Part VIII – Home Office Expenses, describing its proposed Central Office Expenses allocation methodology. ORO will review the proposal for compliance with applicable cost principles and determine if the SURA financial system can adequately support the proposed methodology. If both conditions are met, ORO will, by January 31, 2004, after giving SURA the appropriate amount of time to prepare a cost impact statement for the proposed revised allocation methodology, make a determination as to whether the change is desirable and not detrimental to the Government and complete negotiations with SURA on the predetermined fiscal year 2004 Central Office Expenses.

   As it relates to the yearend actual allowable incurred costs report (for fiscal years 2003 and 2004), ORO will direct SURA to provide sufficient amplifying information in its Central Office Expenses reports of actual allowable incurred costs, due within 120 days after the end of each fiscal year, in sufficient detail to allow DOE to determine the propriety of specific charges. Within 30 days of receipt of the fiscal years 2003 and 2004 reports to DOE, the Oak Ridge Financial Service Center will review the SURA reports and provide a recommendation to the DOE Contracting Officer on the adequacy of the report for negotiating the allocable portion of SURA's Central Office Expenses in accordance with cost principles contained in OMB Circular A-122.

As it relates to any follow-on contract for the management and operation of Jefferson Lab, ORO will re-evaluate the Central Office Expenses contractual provision H.29 in light of the contractor's allocation methodology and the issues outlined by the OIG.

3. **That the Manager, Oak Ridge Operations Office enforce contractual reporting and certification requirements.**

   Response: Concur. ORO will require SURA to submit sufficiently detailed reports and certifications within the timeframes established by the contract. As we move forward, we will evaluate the fiscal years 2003 and 2004 yearend Central Office Expenses reports of actual allowable incurred costs, as well as the September 15, 2003, cost proposal for the estimated allocable portion of Central Office Expenses for fiscal year 2004 in light of the legal/contractual requirements, the Department's authority and the issues being addressed by SURA.

4. **That the Manager, Oak Ridge Operations Office ensure that the contractor develops a supportable method for determining the expenses that are to be reimbursed.**

   Response: Concur. On September 15, 2003, SURA submitted its cost proposal for the estimated allocable portion of Central Office Expenses for fiscal year 2004 which is based on a revised allocation methodology for Central Office Expenses. At that time, SURA also submitted a revised Cost Accounting Standards Board Disclosure Statement, Part VIII – Home Office Expenses, describing its proposed Central Office Expenses allocation methodology. ORO will review the proposal for compliance with applicable cost principles and determine if the SURA financial system can adequately support the proposed methodology. If both conditions are met, ORO will, by January 31, 2004, after giving SURA the appropriate amount of time to prepare a cost impact statement of the proposed revised allocation methodology, make a determination as to whether the change is desirable and not detrimental to the Government, and complete negotiations with SURA on the predetermined fiscal year 2004 Central Office Expenses. Of course, the final determination of allowability will be pending the routine OIG Cost Incurred Audits for questionable costs for those respective years and the Contracting Officer's determination of cost allowability.

IG Report No.: DOE/IG-0629

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1. What additional background information about the selection, scheduling, scope, or procedures of the audit would have been helpful to the reader in understanding this report?

2. What additional information related to findings and recommendations could have been included in this report to assist management in implementing corrective actions?

3. What format, stylistic, or organizational changes might have made this report's overall message more clear to the reader?

4. What additional actions could the Office of Inspector General have taken on the issues discussed in this report which would have been helpful?

Please include your name and telephone number so that we may contact you should we have any questions about your comments.

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