



OFFICE OF INSPECTOR GENERAL

U.S. Department of Energy

ASSESSMENT REPORT

DOE-OIG-18-03

October 2017

**AUDIT COVERAGE OF
COST ALLOWABILITY FOR
UT-BATTELLE, LLC
DURING FISCAL YEAR 2015
UNDER DEPARTMENT OF ENERGY
CONTRACT NO. DE-AC05-00OR22725**



Department of Energy
Washington, DC 20585

October 19, 2017

MEMORANDUM FOR THE MANAGER, OAK RIDGE NATIONAL LABORATORY
SITE OFFICE

A handwritten signature in black ink, appearing to read "Debra K. Solmonson".

FROM: Debra K. Solmonson
Deputy Assistant Inspector General
for Audits and Inspections
Office of Inspector General

SUBJECT: INFORMATION: Assessment Report on "Audit Coverage of Cost Allowability for UT-Battelle, LLC During Fiscal Year 2015 Under Department of Energy Contract No. DE-AC05-00OR22725"

BACKGROUND

Since 2000, UT-Battelle, LLC (UT-Battelle) has managed and operated the Oak Ridge National Laboratory under contract with the Department of Energy. Oak Ridge National Laboratory is the Department's largest science and energy laboratory and through its activities in neutron science, high-performance computing, materials research, and nuclear technology, Oak Ridge National Laboratory supports the Department's national missions of scientific discovery, clean energy, and security. During fiscal year (FY) 2015, UT-Battelle incurred and claimed costs totaling \$1,415,425,695.

As an integrated management and operating contractor, UT-Battelle'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. UT-Battelle 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.

The Department's Office of Inspector General, Office of Acquisition Management, integrated management and operating contractors, and other select contractors have implemented a Cooperative Audit Strategy to make efficient use of available audit resources while ensuring that the Department's contractors claim only allowable costs. This strategy places reliance on the contractors' internal audit function (Internal Audit) to provide audit coverage of the allowability of incurred costs claimed by contractors. Consistent with the Cooperative Audit Strategy, UT-Battelle is required by its contract to maintain an Internal Audit activity with the responsibility for conducting audits, including audits of the allowability of incurred costs. In addition, UT-Battelle 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.

To help ensure that audit coverage of cost allowability was adequate for FY 2015, the objectives of our assessment were to determine whether:

- UT-Battelle Internal Audit conducted cost allowability audits that complied with professional standards and could be relied upon;
- UT-Battelle 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 impacting allowable costs that were identified in prior audits and reviews have been adequately resolved.

RESULTS OF ASSESSMENT

Based on our assessment, nothing came to our attention to indicate that the allowable cost-related audit work performed by UT-Battelle's Internal Audit could not be relied upon. We did not identify any material internal control weaknesses with the allowable cost reviews Internal Audit conducted, which generally met the Institute of Internal Auditors International Standards for the Professional Practice of Internal Auditing. In audits performed since our last assessment, Internal Audit questioned \$44,171 in costs, which had all been resolved. Additionally, we found that UT-Battelle conducted or arranged for audits of subcontractors when costs incurred were a factor in determining the amount payable to a subcontractor, and had resolved all costs questioned in those audits.

Other Matters

While it did not impact our reliance on its work, we noted that as part of Internal Audit's risk-based planning approach, as approved by the Contracting Officer, Internal Audit did not review FY 2015 costs in each of UT-Battelle's four major disbursement categories. Beginning with its FY 2013 allowable cost reviews, Internal Audit had determined that the risk of unallowable costs only warranted testing on a rotational basis and alternated auditing UT-Battelle's major disbursement categories, auditing procurement and travel costs one year, and then non-procurement and payroll costs the next. Accordingly, Internal Audit conducted allowable cost audits on FY 2015 procurement and travel costs, but did not conduct audits on payroll and non-procurement costs. Despite this change in approach, we noted that Internal Audit had relied on the same sampling approach it had used when it was performing annual audits of major disbursement categories. In particular, for FY 2015 costs, Internal Audit had selected and tested approximately 50 transactions in each disbursement category, as it had done with costs incurred since FY 2007 when it was performing annual audits in each category.

We acknowledge that the Cooperative Audit Strategy guidance allows Internal Audit discretion in selecting and conducting its audits, and that the Contracting Officer had approved this approach. Further, we noted that for those major categories excluded from allowable cost audits, Internal Audit had included limited transaction testing on those types of costs in other audits. As the risk of unallowable costs may change from year to year, we suggest that Internal Audit, in coordination with the Contracting Officer, continue to assess and validate whether the rotational transaction testing strategy provides for adequate audit coverage of incurred costs.

SCOPE AND METHODOLOGY

This assessment was performed from September 2016 to October 2017, at the Oak Ridge National Laboratory, located in Oak Ridge, Tennessee. The assessment was limited to UT-Battelle's Internal Audit activities, subcontract audits, and resolution of questioned costs and internal control weaknesses that affect costs claimed by UT-Battelle on its Statement of Costs Incurred and Claimed for FY 2015. The assessment was conducted under Office of Inspector General project number A16OR062. To accomplish our objectives, we:

- Assessed allowable cost audit work conducted by Internal Audit that included a review of allowable cost audit reports, work papers, auditor qualifications, independence, audit planning (including risk assessments and overall internal audit strategy), and compliance with applicable professional auditing standards;
- Reviewed policies, procedures, and practices for identifying subcontracts that require audit and arranging such audits;
- Assessed subcontract audit status; and
- Evaluated resolution of questioned costs and internal control weaknesses affecting cost allowability that were identified in prior audits and reviews conducted by the Office of Inspector General, UT-Battelle's Internal Audit, and other organizations.

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 our conclusions based on our objectives. A review is substantially less in scope than an examination or audit where the objective is an expression of opinion on the subject matter and accordingly, for this review, no such opinion is expressed. Additionally, 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 a limited amount of computer-processed data to accomplish our assessment objectives. Based on a recent review of Oak Ridge National Laboratory information technology controls performed by KPMG LLP, on behalf of the Office of Inspector General, we determined that data was sufficiently reliable for the purposes of this review.

Management waived an exit conference on September 14, 2017.

This report is intended for the use of the 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

PRIOR REPORT

Assessment Report on [*Audit Coverage of Cost Allowability for UT-Battelle LLC During Fiscal Year 2014 Under Department of Energy Contract No. DE-AC05-00OR22725*](#) (OAI-V-16-11; July 2016). Based on our assessment, nothing came to our attention to indicate that the allowable cost-related audit work performed by UT-Battelle, LLC's internal audit function 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 year 2014 audits, UT-Battelle, LLC's internal audit function identified questioned costs totaling \$602, all of which had been resolved. Thus, we did not question any costs associated with those audits. In addition, the contracting officer determined that UT-Battelle, LLC had generally addressed subcontract audit strategy concerns and had resolved costs previously determined to be questionable or pending audit for years prior to fiscal year 2014. However, we identified a total of \$134,106,144 in subcontract costs incurred through fiscal year 2014 that we considered unresolved pending audit.

FEEDBACK

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