ADVISORY

OFFICE OF
INSPECTOR GENERAL
U.S.DEPARTMENT OF THE INTERIOR

ISSUES IDENTIFIED DURING OUR AUDIT OF INTERIM COSTS CLAIMED BY COASTAL ENVIRONMENTAL GROUP, UNDER CONTRACT NOS. INF13PC00214 AND INF13PC00195 WITH THE U.S. FISH AND WILDLIFE SERVICE

Report No.: X-CX-FWS-0003-2014

May 2016

Memorandum **MAY 0 4 2016**

To: Daniel M. Ashe
Director, U.S. Fish and Wildlife Service

From: Kimberly Elmore Kimberly Elmore
Assistant Inspector General for Audits, Inspections, and Evaluations

Subject: Management Advisory – Issues Identified During Our Audit of Interim Costs Claimed by Coastal Environmental Group, Under Contract Nos. INF13PC00214 and INF13PC00195 With the U.S. Fish and Wildlife Service
Report No. X-CX-FWS-0003-2014

The Office of Inspector General (OIG) has completed an audit of the interim costs claimed by Coastal Environmental Group (CEG) on two contracts between September 2013 and July 2014.[1] These contracts were awarded to CEG in September 2013 from the U.S. Fish and Wildlife Service's (FWS) Super Storm Sandy funds to support debris removal and disposal efforts at two wildlife refuges. In our audit, we identified $564,750 in unsupported costs for the Long Island National Wildlife Refuge in New York (Contract No. INF13PC00214) and $1,444,286 in unsupported costs for the Edwin B. Forsythe National Wildlife Refuge in New Jersey (Contract No. INF13PC00195), for a total of $2,009,036 in questioned costs.[2] FWS has responded separately to our cost audit report. This management advisory highlights management issues identified during the cost audit.

During our audit, we found that FWS should have used a more effective process to select the contractor and to monitor performance throughout the contract. As a result, FWS did not prevent or detect numerous problems, including severe financial capability problems, poor internal controls, nonpayment of vendors and subcontractors, labor violations, past performance problems, issues with related parties, and no or deficient Federal contract experience. In this management advisory, we detail our concerns surrounding FWS' contractor selection process, the inadequate documentation FWS relied on when paying the contractor, and FWS' insufficient contract monitoring. We make two recommendations to FWS to improve its contracting practices.

---

[1] OIG Report No. X-CX-FWS-0002-2014, "Interim Costs Claimed by Coastal Environmental Group, Under Contract Nos. INF13PC00214 and INF13PC00195 With the U.S. Fish and Wildlife Service," March 2016.
[2] See Attachment 1 for the risk attributes we considered when deciding to audit CEG.

Improving FWS' Pre-Award Process

Pre-award assessments are essential to reducing risk when awarding contracts. An assessment helps ensure that the potential contractor has adequate financial management systems. It also enables FWS to decide whether to award the contract and whether to add conditions to it, and allows management to plan the appropriate level of contractor oversight. The contractor's capability to account for funds should be evaluated prior to awarding a contract.[3]

During our audit, we found many potential fraud indicators pertaining to CEG and subcontractors DS3 Enterprises and GSI Disaster Services LLC (GSI). These included past performance issues, related-party transactions, potential violations of the Prompt Payment Act (31 U.S.C. §§ 3901-3905), cash flow problems, and even past bankruptcies.

Many of these indicators should have been identified before the FWS contracts were awarded. If FWS had identified some of these issues, it likely would not have contracted with CEG, thereby avoiding the numerous problems that occurred on these contracts.

CEG Past Performance Issues

We discovered past performance issues that FWS should have uncovered during the pre-award assessment of CEG. During our background research, we determined that CEG and one of its subcontractors (DS3 Enterprises, or DS3) had prior issues with a similar Super Storm Sandy debris cleanup contract with the U.S. Army Corps of Engineers (USACE). We found news articles[4] that included the following quotes:

- "Investigators from the U.S. Department of Labor visited the site last week when workers and advocates alleged that subcontractors DS3 Enterprises and Coastal Environmental Group underpaid or failed to pay some of the 400 workers hired to remove 9,000 tons of debris from the island."
- "Workers hired as part of a U.S. Army Corps of Engineers project to clean up post-Sandy storm debris on Fire Island say they are not being paid the wages they were promised when the job was advertised."

These articles were published in March and April 2013, months before FWS awarded the contracts to CEG in September.

To learn more about the allegations, we contacted the contracting officer (CO) at USACE. When we asked about the investigation of CEG and DS3 by the U.S. Department of Labor (DOL), the CO confirmed that labor charges were withheld from the prime contractor for restitution of incorrect payments.

---

[3] See Attachment 2 for guidance on an effective process for pre-award assessments.
[4] Specifically: (1) Fuller, Nicole, "Probe sought into Fire Island cleanup pay," *Newsday*, April 1, 2013: A.26; and (2) Ruud, Candice, "Workers allege wage issues in Fire Island cleanup," *Newsday*, March 26, 2013: A.22.

CEG Related-Party Transactions

We confirmed that the [redacted]. In addition, [redacted]. These relationships raise the possibility of related-party transactions that may affect financial practices.

CEG Financial and Cash Flow Problems, and Prompt Payment Act Violations

During our initial site visit we obtained and reviewed CEG's financial statements. We identified some issues in those statements that raised potential red flags, including those outlined in Figure 1.

Problems Identified in CEG's Financial Statements

1. [redacted]
2. [redacted]
3. [redacted]
4. [redacted]
5. [redacted]

Figure 1. Overview of problems found during OIG review of CEG's financial statements.

We performed an audit of FWS' contracts with CEG, including examination of invoices and supporting documentation from subcontractors DS3 and GSI. We had a conference call with FWS contracting staff and shared our findings and concerns, which included articles on the USACE contract and the timeline of events and what we learned during our interview with the USACE CO.

We also noted similar concerns about GSI, a very small business with no Federal contract experience that did not have any identifiable place of business, [redacted]. FWS staff indicated that there had been problems with CEG making timely payments to GSI; however, the problems seemed to be resolved, at least for the time being.

All these red flags point to significant cash flow problems and the inability to meet obligations such as debt, bills, and subcontractor invoices. The types of issues that can result from cash flow problems in contractors and subcontractors are described in Figure 2.

Types of Issues Typical for Contractors With Cash Flow Problems

1. Complaints of nonpayment or slow payments by vendors and subcontractors—such as missing payroll.
2. Labor issues and violations.
3. Releasing or firing employees.
4. Unsupported costs—without proper documentation, potentially using money to fund operating costs or other contracts.

Figure 2. Issues often found with contractors and subcontractors that have cash flow problems.

We also obtained and reviewed CEG's Dun & Bradstreet[5] business credit report, known as the Comprehensive Insight Plus Report. The scoring and credibility assessment provided in that report for CEG were very telling of what was happening and may continue to happen on these contracts. CEG received the [redacted] scores [redacted] for the credit score and the financial stress score, [redacted] (on a scale where 1 is best and 5 is worst). These scores mean that CEG is at high risk for—

- discontinuing operations and bankruptcy;
- very slow payment to vendors; and
- nonpayment to vendors.

Considering the red flags and potential fraud indicators we discovered, it appears that FWS' process for conducting pre-award assessments of potential contractors should be improved. FWS should have identified CEG as high risk and perhaps would have awarded the Super Storm Sandy contracts elsewhere, or at least added more contract monitoring.

According to FWS, when the contract money had been spent at the Edwin B. Forsythe National Wildlife Refuge, more work remained to be done, but FWS did not feel satisfied with CEG's work and decided to send out a new requisition. CEG did not win the follow-up contract because of the issues stated above.

Improving FWS' Post-Award Monitoring

Post-award monitoring, including the timely receipt of financial records and reports from contractors, is important for effectively managing contracts. Ineffective contract monitoring increases the risk of improper payments and untimely expenditures. Agencies have addressed this issue through on-site reviews and development of systems that make financial information readily available to staff.

[5] Dun & Bradstreet (D&B) provides current and historical business information. The U.S. Government has widely adopted use of D&B's business identification system (D-U-N-S Number) and related data analysis to support vendor tracking and decision making for intragovernmental transactions, grants management, and transparency reporting.

FWS Had Inadequate Supporting Documentation

During our audit, CEG's [redacted] acknowledged being only vaguely familiar with the Federal Acquisition Regulation (FAR) that governs the acquisition process, especially analysis of costs to determine reasonableness, allocability, and allowability. The [redacted] was new to this job and Government contracting and had only been in the position for [redacted] at the start of these contracts, and was no longer with CEG at the time of our second site visit. The [redacted] inexperience with the FAR could have contributed to the insufficient supporting documentation for costs incurred on both contracts. CEG's accountants did not have adequate support for the costs claimed by CEG.

In our audit report, we detailed the unsupported costs associated with the two CEG contracts. Below, we discuss additional problems that we noted during our audit work related to insufficient supporting documentation—missing payroll and other nonpayments, labor issues and violations, and improper firing. With better oversight, FWS would have identified and prevented many of these issues from continuing.

Complaints for Nonpayment and Slow Payments by Vendors and Subcontractors

We interviewed vendors and subcontractors and determined that many of them were not being paid by CEG. Also, one of the subcontractors had not been paid the most recent payroll. We informed the FWS CO, and the CO sent a notification of concern to CEG advising that any future complaints regarding payments would be directed to the surety company for resolution. One of the subcontractors concurrently sent OIG and the CO a letter that stated: "Coastal's payment of invoices still does not comply with our contract terms. Further, Coastal is still not meeting its obligation to the USFWS to promptly pay subcontractors, nor has Coastal complied with notice requirements of the Prompt Payment law."

In addition, GSI told us that it was owed [redacted] by CEG as of July 29, 2014, and was suing CEG's bond insurance. On March 9, 2015, we received an email from On Point Risk Solutions, Inc., stating that it had been retained by CEG's surety, Aegis Security Insurance Company, to provide claim management assistance because GSI had filed a payment claim.

Labor Issues and Violations

During our audit we obtained the previously mentioned DOL investigative report on CEG and DS3 for alleged violations on the USACE contract. That report states: "This case was directed and part of the Northeast Hurricane Sandy Clean-up National Initiative. In addition, complaints were being received quite frequently during the months of March and April 2013 primarily dealing with shorted hours worked, health and welfare, misclassification and nonpayment. Everything but misclassification was substantiated throughout the investigative period. Violations stemmed from the fact that Coastal, typically [redacted] employees, now had to contend with a payroll of over [redacted] employees in a short time span."

The DOL investigation determined that CEG owed [redacted] employees back wages of [redacted] and that DS3 owed [redacted] employees back wages of [redacted] The DOL case file also noted that there were four additional compliance actions in just the prior 3 years against these companies. Three of those four cases resulted in back wages due, totaling over $110,000.

In our review of the FWS debris cleanup contracts, we discovered several violations of the McNamara-O'Hara Service Contract Act (41 U.S.C. §§ 6701-6707) by CEG and sent a "Referral of Possible Violations of the Service Contract Act" to a senior investigator at DOL. For example, for one position the company paid a rate of [redacted] per hour, but we determined the rate should have been [redacted] per hour.

<u>Improper Release of Employee</u>

During the planning stage for our second site visit, CEG's [redacted] The [redacted] alleged that the [redacted], asked the [redacted] to "cook the books" (fraudulently alter facts or figures) for the bank loan. CEG needed a favorable audit to ensure that the bank would renew its line of credit. The [redacted] said that CEG had a cash flow problem and needed the line of credit to keep running the business. The [redacted] explained that the external auditors wanted some deferred revenue to be kept off the financial statement, which the [redacted] agreed with, thinking that including the amounts would be unethical and fraudulent. When the [redacted] brought the issue to the [redacted] the [redacted] the [redacted] that day. When OIG called to confirm a planned meeting with the [redacted] during the site visit, we found that the [redacted] was no longer with CEG. The [redacted] claimed that CEG also did not fully pay for prior hours worked.

FWS' Contract Oversight Was Deficient

FWS did not have effective monitoring procedures in place over the contractor's invoice and payment process. In our audit report, we explained that CEG did not provide most of the supporting documentation needed to support the total costs it billed to the two contracts. We also determined that FWS did not properly verify the calculations on the invoices. Some invoices had math errors, double billings for subcontractor work, and labor rates inconsistent with the contract. Employees should have worked at only one of the two refuge sites, but some employees (for example, [redacted]) billed for work at both the New Jersey and the Long Island sites. FWS did not verify that these employees were not billing the same time at each jobsite. One cause for these errors may have been that FWS had different contracting officer's representatives (CORs) for each contract, who failed to verify with each other that the same employees were not charging time on both contracts.

FWS and CEG could not provide adequate data on how profit was calculated. One COR—who approved the invoices—could not explain how the profit was calculated. CEG claimed profit on third-party invoices in different amounts, ranging from 18.43 percent to 21.80 percent on the Long Island National Wildlife Refuge contract and from 18.80 percent to 24.11 percent on the Edwin B. Forsythe National Wildlife Refuge contract.

Also, FWS did not receive any supporting documentation on the travel allowance from the contractor. CEG charged the Government for lodging and meals without having the proper documentation required by the FAR, specifically 48 C.F.R. § 31.205-46(a)(7), "Travel Costs."

Costs are allowable only if the contractor documents the following: date and place, purpose of the trip, and name and title of the person taking the trip.

In addition, FWS could not identify the pieces of equipment onsite with a serial number or identifying number associated with each piece of equipment. There was no way to verify which equipment was owned by CEG and which equipment was rented by a third party. CEG charged the Government for equipment expenses without proper documentation required by the FAR, specifically 48 C.F.R. § 31.201-2(d), “Determining Allowability.” CEG could not provide a master list of equipment that included serial numbers and invoices from subcontractors to support the equipment charges. CEG also could not provide documentation that identified equipment as assets for the contractor or subcontractor.

FWS did not verify the bonding company invoices within CEG’s invoices. CEG only provided the dollar amount on these invoices with no supporting documentation. For example, on the Long Island National Wildlife Refuge contract, in a period of less than a year, there were two bonding company charges, with no invoices. FWS could not verify the bonding period within the invoice or the specifications on the bond.

FWS did not verify the payroll hours for CEG employees and subcontractors from the crew’s timesheets and daily logs against the FWS invoice to make sure the correct hours were billed for each contract. Employees did not sign in or sign out at the jobsite. CEG had no internal controls over policies and procedures on payroll, position descriptions, and accounts payable, which would have provided checks and balances on time worked on the contract.

FWS should have had more effective monitoring procedures in place over the whole invoice process. In our audit report, we explained that CEG did not provide most of the supporting documentation for costs it billed to the contracts.

Recommendations

We recommend that FWS contracting officials take the following actions to ensure effective oversight of future contracts:

1. Develop and implement an improved process for conducting pre-award assessments of potential contractors.

2. Strengthen internal controls over post-award monitoring, particularly the monitoring and record-keeping of a contract’s supporting documentation, such as invoices, equipment lists, and timesheets.

Information contained in this management advisory will be included in our semiannual report to Congress and posted on our website. Please contact me at 202-208-5747 if you have any questions.

Response Required

Please provide us with your written response to this management advisory within 30 days. The response should provide information on actions taken or planned to address the recommendations, as well as target dates and title(s) of the official(s) responsible for implementation. Please send your response to aie_reports@doioig.gov.

cc: Kristin Young, Procurement Chief, U.S. Fish and Wildlife Services
Debra Sonderman, Director, Office of Acquisition and Property Management

Attachments (2)

Why We Chose To Audit Coastal Environmental Group

Our approach to contract audits is to complete risk profiles or assessments and select for review the contractors that we identify as higher risk. Our decision to audit the Coastal Environmental Group (CEG) was based on our background research and the following risk attributes:

1. *Contractor and Subcontractor Experience.* CEG personnel had little prior Federal contract experience. Contractors with little or no experience usually do not understand Federal contract rules and regulations (e.g., the Federal Acquisition Regulation) and may not be able to segregate costs, determine indirect rates, or handle contract administration. CEG's key personnel had less than 6 months' experience with Federal contracts. In addition, subcontractor DS3 Enterprises was selected and had additional labor issues. Another subcontractor, GSI Disaster Services LLC (GSI), was a very small business with no Federal contract experience that did not have any identifiable place of business; and [redacted], [redacted].

2. *Past Performance.* CEG and DS3 had prior issues with a similar Super Storm Sandy debris cleanup contract with the U.S. Army Corps of Engineers (USACE), on which they were prime subcontractors to the Environmental Chemical Corporation (ECC). There were alleged labor issues, including underpaying or failing to pay some of the 400 workers. Also, during our interview with the USACE [redacted], he stated that CEG was not paying its subcontractors, the [redacted] was not trustworthy, CEG was being sued by ECC, and his advice was to never contract with CEG.

3. *Cost-Type Contract.* Unlike firm-fixed-price contracts, cost-type contracts shift the burden to the Federal Government for ensuring that all costs are reasonable, allowable, and allocable. As a result, contracting staff take on increased oversight responsibilities, such as reviewing timesheets, contractor invoices, and other administrative items during an already hectic time period. One type of cost-type contract—the time and materials contract—is considered especially high risk due to the increased amount of monitoring needed to verify the contractor's time and performance.

4. *Time and Materials Contract.* As noted above, this type of contract is very high risk for the Government and requires careful monitoring. Most of the charges to the FWS debris cleanup contracts were labor costs for contractor and subcontractor labor. Tracking time can be complicated when employees are qualified to do different work under the contract at different labor rates. Contractors need to have a good timesheet policy and procedure to track the time of their employees and subcontractors, and the Government needs to provide thorough oversight and review of the timesheets.

5. *High-Dollar Contract.* These are high-dollar cost-type contracts, totaling over $6.4 million.

6. *Related Parties*. We confirmed that the [redacted]. In addition, [redacted]. These relationships raise the possibility of related-party transactions that may affect financial practices.

7. *Equipment Rental*. Some of the charges to the FWS contracts were for equipment rental. These contracts included very high-dollar transactions, which add a significant incentive for fraud. Just a small change to an invoice can add thousands—even tens of thousands—of dollars to the billings.

   In our experience, equipment rental is a high-risk area. Contractors or subcontractors can profit from excessive charges in many ways, including—

   a. charging equipment at daily rates that grossly exceed the industry standard;
   b. charging hourly or daily rates when weekly or monthly rates should have been charged;
   c. charging daily rates that exceed the cost of the pieces of equipment—in many cases exceeding the cost by multiple times;
   d. charging unreasonable cost-recovery rates;
   e. buying equipment with Federal contract money and making future profits by retaining the equipment for use on future projects; and
   f. using equipment on multiple contracts (Federal or private sector) and charging cost-recovery rates that could far exceed the cost of the equipment.

8. *Disaster*. The fact that these were emergency contracts means that they encompass many of the risk elements identified above, including a shorter period of performance, award without competitive bidding, and potential for decreased oversight by contracting staff.

Guidance for Pre-Award Assessments

Pre-award assessments are essential to reducing risk when awarding contracts. An ideal process for conducting pre-award assessments of potential contractors could include the following steps:

1. Administer an internal control questionnaire that evaluates knowledge of the Federal Acquisition Regulation, internal controls, and segregation of duties.

2. Take additional steps to evaluate financial capabilities, including a review of the contractor’s financial statements and Dun & Bradstreet report.

3. Perform basic Web searches on the contractor and known subcontractors to identify past performance issues, including issues related to the principals of the companies.

4. Contact other agencies that have and had contracts with these companies, including contacting the U.S. Department of Labor for past investigations for labor issues such as noncompliance with the Davis-Bacon and Related Acts.

5. Review the Financial and Business Management System and Federal Procurement Data System to assess the level of experience the contractor and known subcontractors have with the U.S. Department of the Interior and other Federal agencies.

Report Fraud, Waste, and Mismanagement

Fraud, waste, and mismanagement in Government concern everyone: Office of Inspector General staff, departmental employees, and the general public. We actively solicit allegations of any inefficient and wasteful practices, fraud, and mismanagement related to departmental or Insular Area programs and operations. You can report allegations to us in several ways.

By Internet: www.doi.gov/oig/index.cfm

By Phone:
24-Hour Toll Free: 800-424-5081
Washington Metro Area: 202-208-5300

By Fax: 703-487-5402

By Mail:
U.S. Department of the Interior
Office of Inspector General
Mail Stop 4428 MIB
1849 C Street, NW.
Washington, DC 20240