



**AUDIT OF THE OFFICE OF JUSTICE PROGRAMS
NATIONAL INSTITUTE OF JUSTICE
COOPERATIVE AGREEMENT AWARDED TO
EPSILON LAMBDA ELECTRONICS CORPORATION
WEST CHICAGO, ILLINOIS**

U.S. Department of Justice
Office of the Inspector General
Audit Division

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EXECUTIVE SUMMARY

The Office of the Inspector General, Audit Division, has completed an audit of an Office of Justice Programs (OJP), National Institute of Justice (NIJ), cooperative agreement awarded to Epsilon Lambda Electronics Corporation (Epsilon).¹ Epsilon is located in West Chicago, Illinois, about 30 miles west of Chicago, Illinois, and is a privately held, for-profit corporation. Epsilon was awarded \$963,580 under grant number 2007-RG-CX-K181 for a research and development project. The purpose of the project was to research and develop a sensor and surveillance technology for detecting concealed weapons at a safe distance and to collect radar images of a wide range of threat and benign objects. With funding from the agreement, Epsilon planned to demonstrate a compact, low-cost prototype concealed weapons detection sensor.

The objective of our audit was to review performance in the following areas: (1) internal control environment; (2) drawdowns; (3) grant expenditures, including personnel costs; (4) budget management and control; (5) matching costs; (6) accountable property; (7) indirect costs; (8) program income; (9) financial status and progress reports, (10) grant requirements; (11) program performance and accomplishments; and (12) monitoring of sub-grantees and contractors. We determined that matching costs, accountable property, indirect costs, program income, and monitoring of sub-grantees were not applicable to this grant.

As of May 19, 2010, the grantee had drawn down the entire award amount of \$963,580 in grant funds and had recorded costs totaling \$968,037 on its separately maintained spreadsheet for requesting reimbursement. We examined Epsilon's accounting records, financial status and progress reports, and operating policies and procedures. In total, we found \$178,917 in questioned costs and

¹ We use the term "cooperative agreement" interchangeably with "grant" throughout this report.

identified internal control, accounting, reporting, and contractor monitoring deficiencies. Specifically, we found:

- Epsilon was not in compliance with the requirement to have a financial and compliance audit conducted for fiscal years 2008 and 2009. The most recent audit was conducted for the fiscal year ended December 31, 1998.
- Although Epsilon has written procurement, receiving, and payroll policies, personnel stated that the policies were not being followed because they were no longer relevant to Epsilon's operations and that there was not a current, formal process for purchasing and receiving. At the audit close out meeting, Epsilon's President informed us that Epsilon has a dedicated purchasing agent and that there is a formal procurement process. In addition, we identified a lack of adequate segregation of financial duties. Further, Epsilon was not using its official accounting system to record all grant-related expenditures, and all of Epsilon's financial information was maintained on a stand-alone laptop computer, which was typically kept at the Comptroller's home.
- Epsilon was unable to fully support all grant-related costs. Specifically, Epsilon submitted drawdown requests that included \$2,230 in unidentified costs for which Epsilon could not provide supporting documentation. Moreover, Epsilon was reimbursed \$622 for non-personnel and non-contract expenditures for which Epsilon could not provide supporting documentation. Therefore, we are questioning \$2,852 in unsupported costs.
- Epsilon was reimbursed for personnel costs related to employees who were not included in the approved budget as well as costs in excess of approved budget amounts. Based upon these deficiencies, we are questioning \$124,577 in unallowable direct labor and fringe benefit costs reimbursed by the grant.
- Epsilon was reimbursed \$5,805 for unsupported contract expenditures. In addition, Epsilon was reimbursed \$45,683 for services provided by contractors not included in the approved budget or for services charged to the grant at an overstated rate. Based upon these

deficiencies, we are questioning \$51,488 of the contract expenditures reimbursed by the grant.

- Four of the ten required financial status reports were submitted between 2 and 40 days late. Additionally, the reports were not prepared from the accounting records but instead from the drawdown requests. As a result, the financial status reports do not match expenditures as recorded in Epsilon's official accounting records.
- Epsilon did not maintain adequate documentation to assess a primary contractor's performance under the grant.
- Although an NIJ official reported that Epsilon made progress in the ongoing research of millimeter wave-based sensors, Epsilon did not accomplish the objectives of the grant, which were to develop and demonstrate a radar sensor prototype and to collect signatures of a wide range of threat and benign objects. Instead, Epsilon changed the design approach and only provided NIJ with a design for a sensor. We did not locate a Grant Adjustment Notice approving a change to the project as required by the terms and conditions of the grant.

Our report contains eight recommendations to address the preceding issues, which are discussed in detail in the Findings and Recommendations section of the report. Our audit objectives, scope, and methodology are discussed in Appendix I of the report.

TABLE OF CONTENTS

INTRODUCTION	1
Background.....	2
Our Audit Approach.....	2
FINDINGS AND RECOMMENDATIONS	4
Accounting and Internal Controls	4
Grant Drawdowns	7
Grant Expenditures	8
Budget Management and Control	15
Grant Reporting.....	15
Compliance with Cooperative Agreement Requirements	17
Program Performance and Accomplishments	18
Monitoring Contractors	20
Views of Responsible Officials	21
Recommendations	21
APPENDIX I: OBJECTIVES, SCOPE, AND METHODOLOGY	23
APPENDIX II: SCHEDULE OF DOLLAR-RELATED FINDINGS ...	25
APPENDIX III: AUDITEE RESPONSE	26
APPENDIX IV: OFFICE OF JUSTICE PROGRAMS RESPONSE ...	29
APPENDIX V: OFFICE OF THE INSPECTOR GENERAL ANALYSIS AND SUMMARY OF ACTIONS NECESSARY TO CLOSE THE REPORT	32

INTRODUCTION

The Department of Justice (DOJ) Office of the Inspector General, Audit Division, has completed an audit of an Office of Justice Programs (OJP), National Institute of Justice (NIJ) cooperative agreement awarded to Epsilon Lambda Electronics Corporation (Epsilon), located in West Chicago, Illinois. Epsilon was awarded \$963,580 (including one supplement) under grant number 2007-RG-CX-K181 to fund the research and development of a sensor and surveillance technology for detecting concealed weapons at a safe distance.² Specifically, the objectives were to develop and demonstrate a radar sensor prototype with anti-terrorism technology capable of remotely detecting suicide bomb belts and to collect extensive radar images of a wide range of threat and benign objects.

As shown in the following table, Epsilon was awarded a total of \$963,580 to research and develop this project.

TABLE 1. OFFICE OF JUSTICE PROGRAMS GRANT TO EPSILON LAMBDA ELECTRONICS CORPORATION

AWARD NUMBER	PROJECT START DATE	PROJECT END DATE	AWARD AMOUNT	OBJECTIVE
2007-RG-CX-K181	10/01/2007	01/31/2009	\$496,972	To demonstrate system technology in a test bed environment and collect extensive radar images of a wide range of threat and benign objects.
Supplement	10/01/2007	03/31/2010	466,608	To implement a sensor prototype that incorporates threat assessment algorithms for the reliable identification of threat objects.
Total:			\$963,580	

Source: Office of Justice Programs

The purpose of this audit was to determine whether reimbursements claimed for costs under the agreement were allowable, supported, and in accordance with applicable laws, regulations, guidelines, and terms and conditions of the agreement, and to determine program performance and accomplishments. The objective of our audit was to review performance in the following areas: (1) internal control environment; (2) drawdowns;

² We use the term “cooperative agreement” interchangeably with “grant” throughout this report.

(3) grant expenditures, including personnel costs; (4) budget management and control; (5) matching costs; (6) accountable property; (7) indirect costs; (8) program income; (9) financial status and progress reports; (10) grant requirements; (11) program performance and accomplishments; and (12) monitoring of sub-grantees and contractors. We determined that matching costs, accountable property, indirect costs, program income, and monitoring of sub-grantees were not applicable to this grant.

Background

Since 1984, OJP has provided federal leadership in developing the nation's capacity to prevent and control crime, improve the criminal and juvenile justice systems, increase knowledge about crime and related issues, and assist crime victims. NIJ was created in 1969 and is the research, development, and evaluation agency of DOJ. NIJ's overall goals are to: (1) foster science-based criminal justice practice, (2) translate knowledge to practice, (3) advance technology, (4) work across disciplines, and (5) adopt a global perspective.

Epsilon is an engineering research and development company located in West Chicago, Illinois, about 30 miles west of Chicago, Illinois. According to its website, Epsilon has been working in the millimeter and microwave industry for over 36 years, focusing on millimeter wave integrated circuit technology, subsystems, and systems. Further, Epsilon's product and technology applications are for low-cost, short-range radar and wideband communication systems. Epsilon is a privately held, for-profit corporation whose President is the majority stockholder and also the grant Project Director. Epsilon employs five staff members (three engineers, a Production Manager, and a Comptroller).

Our Audit Approach

We tested compliance with what we consider to be the most important conditions of the agreement. Unless otherwise stated in our report, the criteria we audit against are contained in the *OJP Financial Guide*, the Code of Federal Regulations, Office of Management and Budget (OMB) Circulars, and the award documents. We tested Epsilon's:

- **Accounting and Internal Controls** to determine whether the grantee had sufficient accounting and internal controls in place for the processing and payment of funds and controls were adequate to safeguard grant funds and ensure compliance with the terms and conditions of the grant;

- **Grant Drawdowns** to determine whether grant drawdowns were adequately supported and if the grantee was managing grant receipts in accordance with federal requirements;
- **Grant Expenditures** to determine the accuracy and allowability of costs charged to the grant;
- **Budget Management and Control** to examine the amounts budgeted and the actual costs for each approved cost category and determine if the grantee deviated from the approved budget, and if so, if the grantee received the necessary approval;
- **Financial Status Reports and Progress Reports** to determine whether the required reports were submitted on time and accurately reflected grant activity;
- **Accomplishment of Grant Requirements and Objectives** to determine if the grantee met or is capable of meeting the grant's objectives and whether the grantee collected data and developed performance measures to assess accomplishment of the intended objectives; and
- **Monitoring of Contractors** to determine if the grantee adequately monitored the work of contractors to ensure the work was completed as agreed upon in the contracts.

We also performed limited work and confirmed that Epsilon was not required to contribute any local matching funds, did not receive reimbursement for accountable property or indirect costs, did not generate any program income, and did not sub-award DOJ grant funds to sub-grantees. Therefore, we did not perform testing in these areas.

FINDINGS AND RECOMMENDATIONS

We determined that Epsilon researched the development of a concealed weapons detector. However, we found that Epsilon did not fully accomplish the objective of the cooperative agreement, which was to develop a prototype concealed weapons detector. Additionally, we identified weaknesses in Epsilon's internal controls as well as accounting and reporting deficiencies. For instance, we found insufficient documentation to support personnel, contract, non-personnel, and non-contract expenditures reimbursed by the grant. We found Epsilon charged the grant for employees who were not included in the approved budget and at higher salary and fringe benefit rates than included in the approved budget. We also found that Epsilon requested and received reimbursement for personnel expenditures in excess of maximum allowable amounts included in the approved budget. Further, the grantee's financial status reports were not based upon grant accounting records, and 4 of the 10 required financial status reports were filed late. As a result, we questioned \$178,917 in unsupported or unallowable expenditures.

We performed audit work at Epsilon in West Chicago, Illinois, where we obtained an understanding of the accounting system and reviewed a sample of grant expenditures. We reviewed the criteria governing grant activities, including the *OJP Financial Guide*, relevant OMB Circulars, and the Code of Federal Regulations. In addition, we reviewed grant documents, including the application, award, budgets, and financial status and progress reports. We also interviewed key personnel at Epsilon.

Accounting and Internal Controls

According to the *OJP Financial Guide*, grant recipients are required to establish and maintain accounting and internal control systems to account accurately for funds awarded to them. Further, the accounting system should ensure, among other things, the identification and accounting for receipt and disposition of all funds, funds applied to each budget category included in the approved award, expenditures governed by any special and general provisions, and non-federal matching contributions.

We interviewed key Epsilon personnel, including the President, Chief Engineer, Comptroller, and Production Manager, regarding Epsilon's financial management system, record keeping practices, and methods for ensuring adherence to the terms and conditions of the award. We also reviewed

Epsilon's policies, procedures, and accounting records to assess Epsilon's risk of non-compliance with laws, regulations, guidelines, and terms and conditions of the award.

Financial Management System

The *OJP Financial Guide* requires grantees to establish and maintain a system of accounting and internal controls that adequately identifies and classifies grant costs. The system must include controls to ensure that funds and other resources are used optimally and expenditures of funds are in conformance with the general and special conditions applicable to the recipient. Further, the *OJP Financial Guide* states that grantees should establish and maintain program accounts that will enable, on an individual basis, the separate identification and accounting of the receipt and disposition of all funds and the application of all funds to each budget category included within the approved award.

We did not test the overall financial management system for Epsilon as a whole, but conducted a limited review and performed testing in areas related to the NIJ award. We also interviewed staff and management to further assess risk. The grantee has a Quality Control Manual for all aspects of internal controls. However, based on our interviews with key Epsilon personnel, the procedures and processes included in the manual were no longer current and were not being followed by Epsilon employees. Specifically, during fieldwork Epsilon personnel stated that there is no current, formal process for purchasing or receiving. According to the Comptroller, the organization has evolved from a manufacturing company to primarily a research and development organization, and the number of employees has also decreased over time. As a result, the procedures established in the Quality Control Manual have become less relevant to Epsilon's operations. At the audit close out meeting, Epsilon's President advised that Epsilon has an employee who is the dedicated purchasing agent and that there is a formal procurement process.

Our review of Epsilon's financial management system also indicated that the internal controls over the accounting system were weak due to a lack of segregation of duties. Specifically, the Comptroller performs all accounting functions, including recording orders, receipts, and disbursements. The Production Manager explained that due to the very small size of the company, every employee knows what every other employee is doing. Therefore, the Comptroller is aware of all the purchases made by other employees and would also know if an order was not received. In the same manner, the Comptroller would know if the items or services had been received prior to paying an invoice.

In addition, the Comptroller told us that Epsilon uses a commercial off-the-shelf business accounting software for maintaining its accounting records. According to the Comptroller, the software is installed on a stand-alone laptop computer, and the data is backed up to a flash drive every 3 months. Moreover, the laptop computer is generally stored in a locked desk at the Comptroller's home because the Comptroller typically works from home. The Comptroller also stated that the laptop computer only contains the basic software password; there is no additional security password.

We also found that the Comptroller was not aware of the method to record certain transactions by job code using Epsilon's accounting software. Instead, the Comptroller manually calculated the allocation of fringe benefits and rent and utilities related to the award and recorded that information on a separate record of expenditures. As a result, Epsilon's general ledger does not show a complete, separate accounting of all grant-related expenses.

Given the issues identified with Epsilon's financial management system, we believe that Epsilon should strengthen its internal controls.

Audit

According to the special conditions of the agreement, the *OJP Financial Guide*, and OMB Circular A-133, commercial, for-profit organizations that expend \$500,000 or more in federal funds in the organization's fiscal year are required to have independent financial and compliance audits conducted, usually every year. As shown in the following table, Epsilon's expenditures of federal funds exceeded \$500,000 in fiscal years (FY) 2008 and 2009.³

**TABLE 2. EPSILON'S EXPENDITURES OF FEDERAL FUNDS
FISCAL YEARS 2007 THROUGH 2009**

Fiscal Year	2007	2008	2009
Total Federal Expenditures	\$247,447	\$912,983	\$863,602

Source: Epsilon Lambda Electronics Corporation.

Although Epsilon's expenditures of federal funds exceeded \$500,000 for FYs 2008 and 2009, the most recent audit of Epsilon's financial statements was conducted for FY 1998.

In addition to the issues discussed above, we noted several other internal control weaknesses, which are discussed in the Grant Drawdowns,

³ Epsilon's fiscal year is from January 1 to December 31.

Grant Expenditures, Grant Reporting, and Monitoring Contractors sections of this report. The weaknesses include unsupported drawdowns as a result of not recording all expenditures in its general ledger, receiving reimbursement for personnel costs in excess of maximum costs allowed in the approved budget and for employees not listed in the approved budget and at higher rates than approved in the budget, filing reports in an untimely manner, and a lack of documentation to support the grantee's monitoring of contractor performance. We believe that Epsilon's current internal control environment needs significant improvement. As a result, we believe that OJP should ensure that Epsilon implements proper internal controls prior to awarding any additional funding to this grantee.

Grant Drawdowns

We reviewed Epsilon's process for requesting OJP reimbursement for grant-related costs to ensure that reimbursement requests were supported adequately by official accounting records and were in accordance with federal requirements. Epsilon's Comptroller stated that drawdowns were based on actual expenditures and that the drawdown requests were prepared on a monthly or semi-monthly basis depending on Epsilon's cash requirements and when there was time available to prepare the drawdown requests. However, through our analysis of Epsilon's general ledger and grant drawdowns, we determined that Epsilon's reimbursement requests were not based on costs recorded in its general ledger. Instead, Epsilon requested reimbursement based upon a separate spreadsheet maintained by the Comptroller. As mentioned, the Comptroller manually calculated grant-related fringe benefits and rent and utilities costs and recorded those amounts on a separate record of expenditures because the Comptroller was uncertain how to record and allocate these expenditures using Epsilon's accounting software. The Comptroller also included all other grant-related costs on this separate record of expenditures, which was then used for submitting reimbursement requests.

We used the Comptroller's spreadsheets to compare grant-related expenditures to the actual drawdown amounts. As shown in the following table, the grantee had drawn down \$963,580 (the total award amount), although the Comptroller's spreadsheets totaled \$968,037 in grant-related expenses. Through our comparison, we identified errors in Epsilon's drawdown requests. Specifically, on two occasions Epsilon computed its grant-related expenditures using the wrong time period and as a result, submitted its reimbursement request for the incorrect amount. Further, on one occasion, Epsilon inadvertently failed to include some grant-related expenditures in the reimbursement request, while on another occasion Epsilon requested reimbursement for a non-grant related cost. We found,

however, that Epsilon adjusted future drawdown requests to correct these errors.

TABLE 3. COMPARISON OF DRAWDOWNS TO EPSILON’S RECORD OF EXPENDITURES

DATE OF DRAWDOWN PER OJP	AMOUNT DRAWN DOWN PER OJP	GRANT EXPENDITURES PER ACCOUNTING RECORDS FOR DRAWDOWN PERIOD	CUMULATIVE DRAWDOWNS PER OJP	CUMULATIVE EXPENDITURES PER EPSILON’S RECORDS	CUMULATIVE EXPENDITURES LESS CUMULATIVE DRAWDOWNS
12/21/2007	\$39,310.36	\$39,310.36	\$39,310.36	\$39,310.36	\$0.00
01/07/2008	7,395.84	7,395.84	46,706.20	46,706.20	0.00
01/15/2008	10,528.44	10,528.44	57,234.64	57,234.64	0.00
02/01/2008	10,680.88	10,680.88	67,915.52	67,915.51	(0.01)
03/03/2008	24,617.12	24,617.12	92,532.64	92,532.64	0.00
04/01/2008	16,047.92	16,047.92	108,580.56	108,580.56	0.00
04/15/2008	34,934.38	24,951.94	143,514.94	133,532.50	(9,982.44)
05/15/2008	41,112.88	41,112.88	184,627.82	174,645.38	(9,982.44)
06/16/2008	52,483.54	62,465.98	237,111.36	237,111.36	0.00
07/15/2008	56,562.25	56,562.25	293,673.61	293,673.61	0.00
08/20/2008	49,966.02	49,966.02	343,639.63	343,639.64	0.01
09/23/2008	99,286.51	99,286.51	442,926.14	442,926.14	0.00
10/16/2008	29,572.11	32,898.51	472,498.25	475,824.65	3,326.40
12/22/2008	21,000.00	99,884.35	493,498.25	575,709.00	82,210.75
01/06/2009	85,685.38	5,195.29	579,183.63	580,904.29	1,720.66
01/14/2009	(3,473.75)	0.00	575,709.88	580,904.29	5,194.41
02/19/2009	34,786.87	29,591.58	610,496.75	610,495.87	(0.88)
04/01/2009	71,085.78	71,085.78	681,582.53	681,581.65	(0.88)
05/01/2009	40,265.28	29,673.42	721,847.81	711,255.07	(10,592.74)
06/08/2009	48,939.27	31,431.93	770,787.08	742,687.00	(28,100.08)
07/16/2009	38,393.31	66,492.51	809,180.39	809,179.51	(.88)
09/01/2009	76,859.69	76,859.69	886,040.08	886,039.20	(.88)
10/16/2009	30,786.46	30,786.46	916,826.54	916,825.66	(.88)
12/01/2009	6,894.46	32,106.36	923,721.00	948,932.02	25,211.02
01/25/2010	25,211.90	7,567.87	948,932.90	956,499.89	7,566.99
05/19/2010	14,647.10	11,537.21	963,580.00	\$968,037.10	4,457.10
TOTAL	\$963,580.00	\$968,037.10	\$963,580.00	\$968,037.10	\$4,457.10

Source: Office of Justice Programs and Epsilon Lambda Electronics Corporation.

As a result of the discrepancies discussed above, we performed additional analysis of Epsilon’s drawdown requests. Through our testing, we found \$2,230 in unsupported drawdowns for which Epsilon received reimbursement. The Comptroller did not provide support for these drawdown requests and was uncertain as to what the costs entailed. Therefore, we are questioning the \$2,230 as unsupported costs.

Grant Expenditures

The *OJP Financial Guide* serves as a primary manual to assist grantees in fulfilling their fiduciary responsibility to safeguard grant funds and ensure

funds are used for the purposes for which they were awarded. It also serves as a day-to-day management tool for award recipients in administering grant programs.

To determine the accuracy and allowability of costs charged to the grant, we reviewed a sample of personnel, contractor, and other direct expenditures. According to Epsilon’s records, total grant-related expenditures were \$968,037, and Epsilon had been reimbursed for \$963,580 (the entire amount of the award).⁴ We tested \$60,753 of personnel costs from 6 pay periods and 42 non-personnel expenditures totaling \$225,397.

TABLE 4. EPSILON’S APPROVED GRANT BUDGET AMOUNTS AND DESCRIPTION OF COSTS

COST CATEGORY	APPROVED BUDGET	DESCRIPTION OF PLANNED EXPENDITURES
Personnel	\$327,244	Epsilon staff involved in the concealed weapons detector project
Fringe Benefits	52,628	Epsilon staff involved in the concealed weapons detector project
Travel	7,012	Epsilon staff members attending kick-off meeting and final progress report meeting
Supplies	74,954	Commercial off-the-shelf items and raw materials for fabrication of radar
Contract/Consultant	467,957	Signal processing expertise and capability to bring the technology into a usable platform for local law enforcement applications
Other	33,785	Rent, utilities, and equipment calibration
Equipment	0	None planned
Construction	0	None planned
Indirect Costs	0	None planned
FEDERAL FUNDS	\$963,580	
LOCAL MATCH	\$0	
TOTAL PROJECT Cost	\$963,580	

Source: Office of Justice Programs and Epsilon Lambda Electronics Corporation.

⁴ After submitting its final request for reimbursement, Epsilon determined that the total project costs incurred were \$1,039,888. The total costs incurred were based on actual salary rates paid rather than approved budget salary rates and included salary expenditures in excess of maximum allowable salary expenditures. Epsilon also estimated grant-related fringe benefit and rent expenditures based upon certain percentages of total salary expenditures. Further, the \$1,039,888 amount included subcontractor, component, and travel expenditures for which Epsilon did not request or receive reimbursement from OJP.

Personnel Expenditures

To determine the accuracy and allowability of personnel costs charged to the award, we selected and reviewed a sample of six pay periods during the award period. We compared the names, positions, and salaries included in the OJP-approved budgets to the employees who were paid with grant funds. We also tested the accuracy of the supporting time records and reports and recalculated the allocation of salary costs charged to the grant to verify whether the costs were computed correctly, properly authorized, accurately recorded, and properly allocated to the grant. We tested \$53,919 of the total \$412,721 in salary costs reimbursed by OJP.

We found that Epsilon requested and received reimbursement for employees who were not included in the approved budget and for costs calculated at salary rates in excess of the rates included in the approved budget. Based upon the issues identified, we performed further analysis of Epsilon's requests for reimbursement of salary expenditures beyond the initially selected six pay periods. From this analysis, we found that during Phase I of the project, Epsilon had requested and received reimbursement for three employees' salary costs that were calculated at salary rates greater than the rates included in the approved budget. For example, the OJP-approved budget stated that the Comptroller's allowable salary rate was \$80,000 during Phase I of the project. However, during the time period of February 25, 2008, through November 10, 2008, Epsilon charged the grant for the Comptroller's time spent on grant-related activities using a salary rate of \$108,000. As a result, Epsilon was reimbursed \$4,833 more than allowed by the approved budget. In addition to using a higher salary rate than was approved when computing the grant-related salary costs, we found that during Phase I, Epsilon requested and received reimbursement for salary costs of four employees that exceeded the maximum salary costs included in the approved budget. For example, the OJP-approved budget stated that Epsilon was allowed to charge 45 percent of the Principal Investigator's \$150,000 salary (or \$67,500) to the grant. However, Epsilon requested and received \$86,383 in reimbursement for the Principal Investigator's salary during Phase I of the project, which was \$18,883 more than allowed by the approved budget. We also determined that during Phase I, Epsilon had requested and received reimbursement for the salary costs of an engineer who was not specified in the approved budget.

During our analysis of salary costs incurred during Phase II of the project, we identified similar issues to what we found during our examination of Phase I salary costs. Specifically, we found that Epsilon had requested and received reimbursement for one employee's salary costs that was calculated at a salary rate greater than the rate included in the approved

budget. We also determined that during Phase II of the project, Epsilon requested and received reimbursement for three employees' salary costs that exceeded the maximum salary costs included in the approved budget. Further, we determined that Epsilon had requested and received reimbursement for the salary costs of two engineers who were not specified in the approved budget. In total, we found that Epsilon was reimbursed \$114,579 for unallowable salary expenditures as summarized in the following table.

TABLE 5. TOTAL REIMBURSED PERSONNEL COSTS IN EXCESS OF ACTUAL ALLOWABLE AMOUNTS BY PROJECT YEAR AND POSITION⁵

Position	Allowable Salary ⁶	Reimbursement for Salary Expenditures	Reimbursements Over Allowable
First Project Year (Phase I)			
Principal Investigator	\$67,500.00	\$86,383.09	\$18,883.09
Chief Engineer	48,000.00	56,783.21	8,783.21
Manufacturing Technician	26,250.00	45,941.47	19,691.47
Quality Control and Technical Writing	19,035.05	23,867.81	4,832.76
Engineer	0	4,297.31	4,297.31
First Project Year Total	\$160,785.05	\$217,272.88	\$56,487.82
Second Project Year (Phase II)			
Principal Investigator	47,813.02	47,813.02	0
Chief Engineer	50,000.00	65,624.14	15,624.14
Manufacturing Technician	24,192.00	50,685.94	26,493.94
Quality Control and Technical Writing	7,490.20	7,490.20	0
Engineer	7,862.40	16,661.89	8,799.49
Engineer	0	5,232.56	5,232.56
Engineer	0	1,940.82	1,940.82
Second Project Year Total	\$137,357.62	\$195,448.56	\$58,090.94
TOTAL	\$298,142.67	\$412,721.43	\$114,578.76

Source: Office of Justice Programs and Epsilon Lambda Electronics Corporation

We identified similar concerns during our analysis of the fringe benefits charged to the grant. We tested \$6,834 of the total \$56,973 in fringe benefit costs reimbursed by OJP. We considered whether the fringe benefit costs were consistent with charges for other employees, included in the approved budgets, and computed correctly using the approved fringe benefit rate and appropriate formula. We found that during Phase I of the project, Epsilon had requested and received reimbursement for fringe benefit costs for one employee who was not included in the approved budget. We also found that during Phase I, Epsilon requested and received reimbursement for fringe benefit costs of two employees that exceeded the maximum fringe

⁵ The sum of the individual salary amounts by position for each project year may be greater or less than the totals shown due to rounding.

⁶ Allowable salary amounts were calculated based on the actual percent of time employees worked on the concealed weapon detector project and the salary rates included in the approved budget.

benefit costs included in the approved budget. During the second phase of the project, Epsilon requested and received reimbursement for fringe benefit costs for two employees who were not included in the approved budget. Further, during the second year of the project, Epsilon requested and received reimbursement for three employees at a higher workmen's compensation rate than was stipulated in the approved budget. We also found that Epsilon had requested and received reimbursement for two employees at health insurance rates that were less than the health insurance rates included in the approved budget.

Through our analysis, we found that Epsilon had requested and received reimbursement for \$9,998 in unallowable fringe benefit expenditures as summarized in the following table.

TABLE 6. TOTAL REIMBURSED FRINGE BENEFIT COSTS IN EXCESS OF ACTUAL ALLOWABLE AMOUNTS BY PROJECT YEAR AND POSITION⁷

Position	Allowable Fringe Benefits ⁸	Reimbursement for Fringe Benefit Expenditures	Reimbursements Over Allowable Amount
First Project Year			
Principal Investigator	\$8,133.75	\$8,439.63	\$305.88
Chief Engineer	8,292.60	7,989.40	(303.20)
Manufacturing Technician	5,613.00	7,130.12	1,517.12
Quality Control and Technical Writing Engineer	3,047.62	1,895.10	(1,152.52)
Not Individually Reimbursed ⁹	0	403.79	403.79
		7,695.00	7,695.00
First Project Year Total	\$25,086.97	\$33,553.03	\$8,466.06
Second Project Year			
Principal Investigator	5,780.02	4,671.33	(1,108.68)
Chief Engineer	9,174.00	9,233.32	59.32
Manufacturing Technician	5,112.16	7,866.46	2,754.30
Quality Control and Technical Writing Engineer	1,821.35	594.72	(1,226.63)
Engineer	0	353.23	353.23
Engineer	0	511.22	511.22
Engineer	0	189.62	189.62
Second Project Year Total	\$21,887.52	\$23,419.90	\$1,532.38
TOTAL	\$46,974.49	\$56,972.93	\$9,998.43

Source: Office of Justice Programs and Epsilon Lambda Electronics Corporation

⁷ The sum of the individual fringe benefit amounts by position for each project year may be greater or less than the totals shown due to rounding.

⁸ Allowable fringe benefit amounts were calculated based on the actual percent of time employees worked on the concealed weapon detector project and the fringe benefit rates included in the approved budget.

⁹ For the reimbursement period ending June 10, 2008, the comptroller requested reimbursement for the total estimated first year unemployment insurance expenditures. We considered the allowable unemployment insurance expenditures for each reimbursement period in our determination of reimbursements over allowable amounts. As a result, we did not include a separate amount under the Allowable Fringe Benefits column for this line item.

In sum, we are questioning \$124,577 in personnel costs. This consists of \$114,579 in salary expenditures and \$9,998 in fringe benefits expenditures that were deemed unallowable as detailed above.

Contract Expenditures

We judgmentally selected 24 transactions recorded in Epsilon's general ledger as contract expenditures associated with the project to determine whether the costs were accurate, supported, allowable, and allocable to the grant under federal rules, regulations, and guidelines. The selected transactions totaled \$133,925 of the total \$416,381 in grant-related contract expenditures. However, Epsilon only requested and received reimbursement for 13 of the 24 transactions; the 13 transactions totaled \$102,803. Based upon our testing, we are questioning \$51,488 in unsupported and unallowable costs as follows:

- \$4,000 in unsupported costs for contract expenditures that were supported only by memoranda signed by Epsilon's President with instructions to process the checks and to charge the expenditures to the grant.¹⁰ Epsilon was unable to provide: (1) a copy of a contract, purchase order, or agreement that identified and authorized the grant-related services; (2) supporting documentation that identified what grant-related services were provided; (3) a copy of an invoice from the contractor; or (4) evidence that the receipt of the grant-related services had been verified.
- \$1,805 in unsupported costs for a contract expenditure that was supported only by a handwritten note. The note included check numbers and amounts, as well as cumulative totals and amounts that corresponded to entries in the general ledger, along with an annotation "originals lost." Epsilon could not provide: (1) a copy of a contract, purchase order, or agreement that identified and authorized the grant-related services; (2) supporting documentation that identified what grant-related services were provided; (3) a copy of an invoice from the contractor; or (4) evidence that the receipt of grant-related services had been verified. Therefore, we determined this transaction was not properly authorized and supported.

¹⁰ We identified three transactions totaling \$6,000 for which the costs were only supported by simple memoranda. However, Epsilon did not request or receive reimbursement for one of the transactions totaling \$2,000. Therefore, we are only questioning the \$4,000 that was reimbursed.

- \$37,710 in unallowable costs for contract expenditures that were not included in the grant-approved budget.¹¹ The grant-approved budget authorized Epsilon to procure contract services and specifically named contractors that would be utilized. However, three of the six contractors included in our sample were not identified in the grant-approved budget.

Based on these issues, we conducted further testing of Epsilon's contract expenditures and found that Epsilon received cost savings that it did not pass on to OJP. Epsilon entered into a research services agreement with a contractor that would assist Epsilon on multiple projects, not just the OJP grant-funded project. Epsilon agreed to pay the contractor \$49,139 and estimated the contractor would provide 1,300 hours of service on all projects. Based upon our review of the contractor's timesheets, we found that the contractor actually worked a total of 1,952 hours. Although the contractor worked more hours than originally estimated, Epsilon only paid the contractor the original cost of the agreement – \$49,139. According to the contractor's timesheets, the contractor spent 1,220 of the total 1,952 hours (or 62.5 percent) on the OJP grant-funded project. However, Epsilon requested and received reimbursement for \$38,685, which equated to 79 percent of the total cost of the agreement. We believe that Epsilon should have only charged the grant \$30,712, which was based upon the original cost of the agreement (\$49,139) multiplied by the percentage of time spent on the OJP grant-funded project (62.5 percent). Therefore, we are questioning the difference of \$7,973 as unallowable costs.

In sum, we are questioning \$51,488 in contract costs. This consists of \$5,805 (\$4,000 plus \$1,805) in unsupported expenditures and \$45,683 (\$37,710 plus \$7,973) in unallowable expenditures as detailed above.

Non-personnel and Non-contract Expenditures

To determine the accuracy and allowability of non-personnel and non-contract costs charged to the grant, we reviewed a sample of 18 transactions, consisting of travel and supplies expenditures, totaling

¹¹ We identified 16 transactions totaling \$46,918 for grant-related services provided by unapproved contractors. However, Epsilon did not request or receive reimbursement for nine of the transactions totaling \$9,208. Therefore, we are only questioning the seven that were reimbursed, totaling \$37,710.

\$91,472. We found \$622 in unsupported costs.¹² We also identified a few non-dollar related recordkeeping issues. Specifically, we found that one transaction was inaccurately recorded in the general ledger as a travel expenditure instead of as a contract expenditure. We also identified two transactions for which Epsilon had recorded the wrong dates in its general ledger. All of the remaining transactions were properly authorized, accurately recorded in the general ledger, and adequately supported.

Budget Management and Control

According to the *OJP Financial Guide*, a grantee may transfer funds between approved budget categories without OJP approval if the total transfers are 10 percent or less than the award amount. Requests for transfers of funds between budget categories of over 10 percent must be submitted to OJP for approval. We compared the amounts charged in each of the budget categories to the approved budget amount for each budget category. Although we observed the movement of dollars between budget categories, none of the amounts exceeded 10 percent of the total budget amount. Therefore, Epsilon was not required to obtain prior approval from OJP for these transfers.

Grant Reporting

The *OJP Financial Guide* states that two types of reports are to be submitted by the grantee. Financial Status Reports (FSR) provide information on monies spent and the unobligated amounts remaining in the grant. Program progress reports provide information on the status of grant-funded activities and other pertinent information.

Financial Status Reports

According to the *OJP Financial Guide*, prior to October 1, 2009, FSRs were to be submitted within 45 days of the end of the calendar quarter. Beginning with the reporting period October 2009 through December 2009, grantees are required to submit quarterly Federal Financial Reports within 30 days of the end of the calendar quarter.¹³ The final FSR must be submitted no later than 90 days following the end of the grant period. Funds or future awards may be withheld if reports are not submitted or if

¹² We identified three transactions totaling \$969 that were not properly supported with original receipts or other documentation. However, Epsilon did not request or receive reimbursement for one of the transactions totaling \$347. Therefore, we are only questioning the \$622 that was reimbursed.

¹³ For consistency purposes, we use the term "FSR" to refer to both types of reports.

reports are submitted late. We reviewed all 10 of the FSRs submitted during the award. As shown in Table 7, Epsilon submitted 4 of the 10 reports from 2 to 40 days late.

TABLE 7. TIMELINESS OF FINANCIAL STATUS REPORTS

RPT No.	REPORT PERIOD	DUE DATE	DATE SUBMITTED	DAYS LATE
1	10/01/07 – 12/31/07	02/14/08	12/18/07	0
2	01/01/08 – 03/31/08	05/15/08	05/19/08	4
3	04/01/08 – 06-30/08	08/14/08	07/18/08	0
4	07/01/08 - 09/30/08	11/14/08	11/24/08	10
5	10/01/08 – 12/31/08	02/14/09	02/11/09	0
6	01/01/09 – 03/31/09	05/15/09	04/29/09	0
7	04/01/09 – 06/30/09	08/14/09	08/14/09	0
8	07/01/09 – 09/30/09	11/14/09	11/16/09	2
9	10/01/09 – 12/31/09	01/30/10	03/11/10	40
10	01/01/10 – 03/31/10	06/29/10	04/12/10	0

Source: Office of Justice Programs

We also compared the grant-related expenditures reflected on the FSRs to Epsilon’s accounting records. Through our review of Epsilon’s records, we determined that Epsilon’s general ledger included grant-related expenditures for which Epsilon did not request or receive reimbursement. Further, the general ledger did not include any grant-related fringe benefit or rent and utilities expenditures. Therefore, the FSRs did not accurately reflect grant-related expenditures as recorded in Epsilon’s official accounting system. Instead, we determined that Epsilon prepared the FSRs based on the separately maintained spreadsheet used for submitting its drawdown requests. The following table shows the grant-related expenditures as reported on Epsilon’s FSRs, official accounting records, and separately maintained spreadsheet.

TABLE 8. ACCURACY OF FINANCIAL STATUS REPORTS

FSR No.	FSR REPORT PERIOD END DATE	EXPENSES PER FSR	EXPENDITURES PER DRAWDOWN REQUESTS	EXPENDITURES PER GENERAL LEDGER
1	12/31/2007	\$39,310.36	\$46,706.20	\$50,255.02
2	03/31/2008	69,270.20	61,874.36	59,421.71
3	06/30/2008	168,890.44	168,890.45	139,817.08
4	09/30/2008	198,353.65	198,353.64	158,187.05
5	12/31/2008	105,079.64	105,079.64	128,889.60
6	03/31/2009	100,677.36	100,677.36	112,092.97
7	06/30/2009	117,189.30	117,189.30	87,556.12
8	09/30/2009	118,054.70	118,054.70	132,928.48
9	12/31/2009	39,674.23	39,674.23	55,010.64
10	03/31/2010	7,080.12	7,080.12	15,921.39
not reimbursed due to award maximum			4,457.09	
Total		\$963,580.00	\$968,037.09	\$940,080.06

Source: Office of Justice Programs and Epsilon Lambda Electronics Corporation

Progress Reports

According to the *OJP Financial Guide*, Categorical Assistance Progress Reports are due semiannually on January 30 and July 30 for the life of the award. We reviewed the six progress reports submitted during the award and found that two of the reports were not submitted by OJP's established deadline. However, we are not taking issue with the timeliness of these report submissions because the reports were only 1 day late.

As for the content of the progress reporting, we found that the reports did not include a comparison of actual accomplishments to the objectives established for the period. Instead, the reports included detailed, cumulative technical results of work performed during the reporting period. In our judgment, the reports provided adequate information to determine the status of the tasks planned for the period. The progress reports did identify circumstances that resulted in Epsilon's decision to change the design approach. However, no documentation was available to show that Epsilon formally requested OJP's approval to change the design approach.

Compliance with Cooperative Agreement Requirements

We reviewed the special conditions of the grant award and identified several key requirements, such as the grantee's agreement to: (1) have an independent financial and compliance audit performed, (2) act jointly with

NIJ in determining research design, and (3) submit progress reports and FSRs in a timely manner. As previously mentioned, the grantee did not have the required independent audit performed. We also found that Epsilon did not act jointly with NIJ in the determination of changing the research design. Moreover, we found the grantee submitted the required progress reports and FSRs, although four FSRs were submitted late. All of these matters are discussed in detail in the appropriate sections of this report.

Program Performance and Accomplishments

According to the award documentation, the goal of the award was to develop an anti-terrorism technology capable of remotely detecting concealed weapons, such as handguns and knives, as well as explosive devices such as suicide bomb belts. Epsilon had previously conducted experiments utilizing three-dimensional 77 GHz radars that demonstrated the ability of millimeter wave radars to detect objects concealed on human subjects. However, the experiments also demonstrated that the radar images of the detected objects would require much improvement to reliably classify objects as weapons or as non-threatening objects. Therefore, Epsilon proposed to develop a radar sensor at 94 GHz to achieve the very high resolution necessary to realize the grant objectives. Epsilon proposed to partner with Northrop Grumman to develop the very sophisticated signal processing methods necessary to complete the concealed weapons detection sensor.

The system was to be developed in two phases. During Phase I, Epsilon was supposed to demonstrate the system technology in a test bed environment and develop an extensive collection of radar images. During Phase II, Epsilon was to implement the technology in a prototype sensor that met NIJ's objectives that incorporated threat assessment algorithms to reliably identify threat objects. Through our review of Epsilon's progress reports and interviews with Epsilon officials, we determined that Epsilon did not accomplish the objectives of developing and demonstrating a radar sensor prototype or collecting extensive object signatures. We noted that Epsilon changed the design approach mid-way through the project and provided only a design, not a prototype, for a sensor.

The award documentation reported that substantial federal involvement in the project was contemplated and identified various methods for NIJ to monitor the technical elements of the project, including periodic telephone contacts, review of interim reports, and site visits. The award documentation specified that NIJ would conduct a review of Epsilon's activities at least monthly. However, according to the terms and conditions

of the agreement, NIJ's monitoring of Epsilon was expected to occur several times a month.

Due to the highly technical nature of the project, we requested the NIJ Program Manager to provide us with the results of NIJ's oversight and monitoring of the technical elements of the project. In response, the NIJ Program Manager reported having telephone conversations with Epsilon on several occasions. The Program Manager also advised us that Epsilon had presented its research and responded to subsequent questions at a technology working group meeting. However, NIJ did not maintain any documentation supporting its oversight of Epsilon.

The NIJ Program Manager agreed that Epsilon did not meet the program objectives but also opined that not meeting program objectives is often the nature of research. The NIJ Program Manager also stated that Epsilon's progress reports had been received and approved. As previously mentioned, Epsilon did submit its progress reports that explained it was changing its design approach. However, we found that OJP was often untimely in its review of the progress reports – ranging from 23 to 357 days to approve the reports.

In response to another inquiry, an NIJ official provided further insight into the grantee's attempt to meet the program objectives. Specifically, this official explained that millimeter wave-based sensors afford one of the most promising approaches to being able to detect at a safe distance weapons concealed under clothing. The official further stated that success has been achieved in developing such sensors to function with short-range distances but the ongoing challenge is to develop these types of sensors that are able to detect concealed weapons at longer distances. According to this official, Epsilon made progress in this ongoing area of research that will prove valuable in future endeavors to develop long-range millimeter wave-based sensors.

Regardless of the reported progress by Epsilon in the ongoing research of millimeter wave-based sensors, there is a notable difference between delivering an actual prototype and developing only a design. We are concerned that Epsilon did not receive official, documented NIJ approval prior to this deviation from the project design approach. We are also concerned about the lack of evidence to support NIJ's project oversight and the untimely review of the submitted progress reports that discussed the revised project design.

Monitoring Contractors

According to the *OJP Financial Guide*, direct recipients of federal awards should ensure that monitoring of organizations under contract to them is performed in a manner that will ensure compliance with their overall financial management requirements.

Epsilon contracted with individuals and organizations to obtain professional services, supplies, and the system technology necessary to develop the concealed weapons detection sensor. The largest portion of the contract expenditures was for the system technology development. Epsilon's principal contractor performed this work at its own facility and periodically reported its results and progress to Epsilon. The remaining professional services were performed at Epsilon's facility and the work was directed and supervised by Epsilon's Program Manager and Chief Engineer. Epsilon also obtained consulting services from an individual through a purchase order. The remaining contracts were for components necessary for performing tests related to the development of a radar sensor.

According to the Program Manager, Epsilon relied on the reputation of its principal contractor for the system technology development as being a major corporation and a predominant government contractor, which provided assurance to Epsilon that the contractor's financial management system and processes and procedures for administering and adhering to the terms and conditions of the contract were adequate. The Program Manager stated that he and the Chief Engineer conducted bi-monthly teleconferences with the principal contractor to discuss the principal contractor's results and progress and to ensure the terms and conditions of the contract were being met. However, the Program Manager told us there was no documentation of these verbal reviews of the principal contractor's performance.

Although the monitoring was unstructured, Epsilon's principal contractor was required to submit semi-annual reports detailing the work performed and results achieved. We requested copies of these reports. However, Epsilon was not able to provide copies of the contractor's semi-annual report for the reporting period ending December 31, 2009 or the contractor's final report for the period ending March 31, 2010. Because Epsilon could not provide all of the contractor's semi-annual reports, we cannot completely assess the effectiveness of Epsilon's monitoring of this contractor.

We believe that Epsilon did not maintain adequate documentation, such as reported progress on accomplishments, to assess its principal contractor's performance under the award. Further, the contractor's reports

we reviewed did not include any cost information or comparison of accomplishments to project goals. In addition, we do not believe that Epsilon's monitoring of the principal contractor's performance as documented in the progress reports submitted to OJP is adequate for evaluating contractor performance.

Based on our review of the timesheets provided by Epsilon for its other contractors, we determined the services were provided in a timely manner and approved by Epsilon's President. Because Epsilon monitored these contractors' performance through direct supervision by Epsilon's Chief Engineer and Program Manager, we determined that it was not necessary to perform additional testing of the effectiveness of Epsilon's monitoring of the contractors.

Views of Responsible Officials

We discussed the results of our review with grantee officials throughout the audit and at a formal exit conference, and we have included their comments as appropriate.

Recommendations

We recommend that OJP:

1. Ensure that Epsilon undergoes the required, independent financial and compliance audits for FY 2008 and FY 2009.
2. Ensure that Epsilon implements proper internal controls, including the development of revised financial policies before the grantee receives any additional funds.
3. Remedy the \$2,852 in unsupported questioned costs related to Epsilon's inability to support its drawdown requests of \$2,230 and the reimbursement of non-personnel and non-contract expenditures for which Epsilon could not provide supporting documentation totaling \$622.
4. Remedy the \$124,577 in unallowable questioned costs that were used to pay the salary (\$114,579) and fringe benefit costs (\$9,998) of unapproved personnel or the higher than allowed salary and fringe benefit costs of authorized personnel.

5. Remedy the \$5,805 in unsupported questioned costs that were used to procure contract services for which Epsilon could not produce adequate documentation.
6. Remedy the \$45,683 in unallowable questioned costs that were used to procure contract services from contractors that were not included in the approved budget (\$37,710) and for contract cost savings that were not passed on to OJP (\$7,973).
7. Ensure that Epsilon submits a revised, final Federal Financial Report that accurately reflects grant-related expenditures as recorded in Epsilon's official accounting system.
8. Review Epsilon's submitted progress reports related to the project design changes and ensure that the grant file contains the necessary approvals for the changes in project scope.

OBJECTIVES, SCOPE, AND METHODOLOGY

The purpose of this audit was to determine whether reimbursements claimed for costs under the cooperative agreement were allowable, supported, and in accordance with applicable laws, regulations, guidelines, and terms and conditions of the cooperative agreement, and to determine program performance and accomplishments.

We conducted this performance audit in accordance with generally accepted government auditing standards and included such tests as were considered necessary to accomplish our objectives. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Our audit concentrated on, but was not limited to, the inception of the agreement on October 1, 2007, through March 31, 2010. This was an audit of NIJ grant number 2007-RG-CX-K181, for which Epsilon was awarded a total of \$963,580. In conducting our audit, we reviewed FSRs and progress reports as well as performed sample testing in award expenditures, including salary and fringe benefit costs. Our testing was conducted by judgmentally selecting a sample of expenditures, along with a review of internal controls and procedures for the grant that we audited. Judgmental sampling design was applied to obtain broad exposure to numerous facets of the grant reviewed, such as dollar amounts, expenditure category, or risk. This non-statistical sample design does not allow for projection of the test results to all grant expenditures or internal controls and procedures. In total, Epsilon had drawn down \$963,580 and recorded grant-related costs totaling \$968,037 as of May 19, 2010. We tested 42 invoices, which totaled \$225,397. In addition, we tested \$53,919 out of a total of \$412,721 in salary costs and \$6,834 out of \$56,973 in total fringe benefits costs.

We tested compliance with what we consider to be the most important conditions of the cooperative agreement. Unless otherwise stated in our report, the criteria we audit against are contained in the *OJP Financial Guide* and the award documents. We reviewed Epsilon's grant activities and performance in the following areas: (1) internal control environment; (2) drawdowns; (3) grant expenditures, including personnel costs; (4) budget management and control; (5) financial status and progress reports; (6) grant requirements; (7) program performance and accomplishments; and (8) monitoring of contractors. We determined that matching costs, accountable property, indirect costs, program income, and

monitoring of sub-grantees were not applicable to this grant. Although Epsilon had expended more than \$500,000 in federal funds during 2008 and 2009, it did not have a financial and compliance audit conducted during those years. We performed limited testing of source documents to assess the timeliness and accuracy of FSRs, reimbursement requests, expenditures, and progress reports; evaluated performance to grant objectives; and reviewed the grant-related internal controls over the financial management system. We tested invoices associated with transactions shown in Epsilon's general ledger as of October 19, 2010. However, we did not test the reliability of the financial management system as a whole and reliance on computer-based data was not significant to our objectives.

SCHEDULE OF DOLLAR-RELATED FINDINGS

	AMOUNT	PAGE
QUESTIONED COSTS:		
Unsupported		
Drawdown Requests	\$2,230	8
Contract Expenditures	5,805	14
Non-Personnel and Non-Contract Expenditures	622	15
<i>Total Unsupported</i>	<i>\$8,657</i>	
Unallowable		
Personnel Expenditures	\$124,577	13
Contract Expenditures	45,683	14
<i>Total Unallowable</i>	<i>\$170,260</i>	
TOTAL NET DOLLAR-RELATED FINDINGS	\$178,917	

Questioned Costs are expenditures that do not comply with legal, regulatory, or contractual requirements; are not supported by adequate documentation at the time of the audit; or are unnecessary or unreasonable.

AUDITEE RESPONSE



Carol S. Taraszka
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 Chicago Regional Audit Office
 Office of the Inspector General
 U.S. Department of Justice
 500 West Madison Street, Suite 1121
 Chicago, IL 60661
Carol.S.Taraszka@usdoj.gov

CC: Linda J. Taylor, Lead Auditor
Linda.Taylor2@usdoj.gov
 Fax: 202-353-2524

This letter is in response to the draft audit report dated September 30, 2011, regarding NIJ grant 2007-RG-CX-K181. The draft audit report contained 8 recommendations and \$178,917 in questioned costs, which are addressed below.

As summary of Epsilon Lambda's position in regards to the contract and subsequent review, the company concurs that certain actions were not taken over the contract period due to an incomplete understanding of contract terms, and the company recommends two main actions to correct these oversights and close out the referenced grant, as well as two other actions to be undertaken before any additional grant funds are awarded to grantee Epsilon Lambda Electronics. These actions will address all 8 of the draft audit report recommendations.

The two current and immediate actions the company recommends be taken are:

- The company prepare and submit for OJP approval, one or more Grant Adjustment Notice(s), along with related revised budgets, sufficient to detail the change in scope, technical approach, and direction of financial resources to the contract.
- The company prepare and submit for OJP approval, a final Federal Financial report that reflects the above reference Grand Adjustment Notice(s) and the company official accounting system.

In addition to the above current and immediate actions to be taken, the company recommends the following two actions be undertaken as conditions to the company receiving any additional NIJ grant funds:

- The company complete and submit an independent financial review for the most recent appropriate fiscal year, prior to any new grant funds being awarded by NIJ to grantee Epsilon Lambda Electronics.
- The company demonstrate, and OJP ensure, that all proper internal controls, including revised financial policies, are implemented prior to any new grant funds be awarded by NIJ to grantee Epsilon Lambda Electronics.

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The two immediate actions, and two conditional actions, will address the 8 draft audit recommendations in detail as follows:

- Recommendation 1 – The company recommends that OJP accept and approve that the audit undertaken by the Office of the Inspector General as completed, and that this audit will act as a sufficient replacement for a post-financial review of the 2008-2009 years. The company recommends that any subsequent grant funds be conditional upon a complete independent review of the company's most recent applicable fiscal year be undertaken and submitted to OJP.
- Recommendation 2 – The company concurs that prior to any additional grant funds being provided to Epsilon Lambda Electronics, the company must demonstrate that all proper internal controls, including revised financial policies, are implemented.
- Recommendation 3 – The company recommends that the company submit, and OJP approve, one or more Grant Adjustment Notice(s), and related grant budgets, sufficient to detail the change in scope, technical approach, and direction of financial resources to the contract. The amount \$2,852 in unsupported costs will be withdrawn, and offset with supported costs that previously exceeded the contract. See foot note #4, that indicates the company incurred total costs of \$1,039,888., an amount sufficient to withdraw the unsupported costs, and still be within the contract limits.
- Recommendation 4 - The company recommends that the company submit for OJP approval, one or more Grant Adjustment Notice(s), and related grant budgets, sufficient to detail the change in scope, technical approach, and direction of financial resources to the contract. The GAN and related budget will detail how the amount \$124,577 was spent in different cost categories than those original proposed in the grant budget, and why these movements in expense categories were required to meet the technical approach.
- Recommendation 5 – The company recommends that the company submit for OJP approval, one or more Grant Adjustment Notice(s), and related grant budgets, sufficient to detail the change in scope, technical approach, and direction of financial resources to the contract. The \$5,805 in unsupported costs will be withdrawn, and offset with previously supported costs in amount that exceeded the contract. See foot note #4, that indicates the company incurred total costs of \$1,039,888, an amount sufficient to withdraw the unsupported costs and still be within the contract limits.
- Recommendation 6 - The company recommends that the company submit for OJP approval, one or more Grant Adjustment Notice(s), and related grant budgets, sufficient to detail the change in scope, technical approach, and direction of financial resources to the contract. The GAN and budget will detail how the amount \$45,683 was spent in different cost categories, and under different subcontracts, than those original proposed in the grant budget, and why these movements in expense categories and subcontracts were required to meet the technical approach.
- Recommendation 7 - The company concurs that Epsilon Lambda should submit for OJP approval, a final Federal Financial report that reflects the above referenced Grand Adjustment Notice(s) and related budget changes, and modifications to the company official accounting system.

- Recommendation 8 - The company recommends that the company submit for OJP approval, one or more Grant Adjustment Notice(s), and related grant budgets, sufficient to detail the change in scope, technical approach, and direction of financial resources to the contract. OJP would confirm that these GAN's are consistent with the company's submitted progress reports.

Respectively Submitted

Robert M Knox

Robert M. Knox,
President, Epsilon Lambda Electronics

October 19, 2011

OFFICE OF JUSTICE PROGRAMS RESPONSE



U.S. Department of Justice

Office of Justice Programs

*Office of Audit, Assessment, and Management**Washington, D.C. 20531*

OCT 28 2011

MEMORANDUM TO: Carol S. Taraszka
Regional Audit Manager
Chicago Regional Audit Office
Office of the Inspector General

FROM: Maureen A. Henneberg
Director *Maureen A. Henneberg*

SUBJECT: Response to the Draft Audit Report, *Office of Justice Programs, National Institute of Justice, Cooperative Agreement Awarded to Epsilon Lambda Electronics Corporation, West Chicago, Illinois*

This memorandum is in response to your correspondence, dated September 30, 2011, transmitting the subject draft audit report for the Epsilon Lambda Electronics Corporation (Epsilon). We consider the subject report resolved and request written acceptance of this action from your office.

The report contains eight recommendations and \$178,917 in questioned costs. The following is the Office of Justice Programs' (OJP) analysis of the draft audit report recommendations. For ease of review, the recommendations are restated in bold and are followed by our response.

1. **Ensure that Epsilon undergoes the required, independent financial and compliance audits for fiscal year 2008 and fiscal year 2009.**

We agree with the recommendation. We will coordinate with Epsilon to obtain a copy of fiscal year 2008 and 2009 audit reports, once completed. In addition, we will request that Epsilon provide a copy of procedures, developed and implemented, to ensure that all required future audits are performed in a timely manner.

2. **Ensure that Epsilon implements proper internal controls, including the development of revised financial policies before the grantee receives any additional funds.**

We agree with the recommendation. We will coordinate with Epsilon to obtain a copy of procedures, developed and implemented, to ensure that Epsilon maintains internal controls which are adequate to administer Federal grant funds.

3. **Remedy the \$2,852 in unsupported questioned costs related to Epsilon's inability to support its drawdown requests of \$2,230 and the reimbursement of non-personnel and non-contract expenditures for which Epsilon could not provide supporting documentation totaling \$622.**

We agree with the recommendation. We will coordinate with Epsilon to remedy the \$2,852 in unapproved questioned costs related to drawdown requests totaling \$2,230, and non-personnel and non-contract expenditures totaling \$622, charged to cooperative agreement number 2007-RG-CX-K181. If adequate documentation cannot be provided, we will request that Epsilon return the funds to the U.S. Department of Justice (DOJ), and submit a revised final Federal Financial Report (FFR) for the agreement.

4. **Remedy the \$124,577 in unallowable questioned costs that were used to pay the salary (\$114,579) and fringe benefit costs (\$9,998) of unapproved personnel or the higher than allowed salary and fringe benefit costs of authorized personnel.**

We agree with the recommendation. We will coordinate with Epsilon to remedy the \$124,577 in unallowable questioned costs related to unallowable salary totaling \$114,579, and fringe benefits costs totaling \$9,998, charged to cooperative agreement number 2007-RG-CX-K181. If adequate documentation cannot be provided, we will request that Epsilon return the funds to the DOJ, and submit a revised final FFR for the agreement.

5. **Remedy the \$5,805 in unsupported questioned costs that were used to procure contract services for which Epsilon could not produce adequate documentation.**

We agree with the recommendation. We will coordinate with Epsilon to remedy the \$5,805 in unsupported questioned costs related to contract services charged to cooperative agreement number 2007-RG-CX-K181. If adequate documentation cannot be provided, we will request that Epsilon return the funds to the DOJ, and submit a revised final FFR for the agreement.

6. **Remedy the \$45,683 in unallowable questioned costs that were used to procure contract services from contractors that were not included the approved budget (\$37,710) and for contract cost savings that were not passed on to OJP (\$7,973).**

We agree with the recommendation. We will coordinate with Epsilon to remedy the \$45,683 in unallowable questioned contract services expenditures, and will request a final determination from the National Institute of Justice (NIJ) regarding the allowability of contractor services not approved by NIJ. If the expenditures are determined to be unallowable, we will request that Epsilon return the funds to the DOJ, and submit a revised final FFR for the agreement.

7. **Ensure that Epsilon submits a revised, final Federal Financial Report that accurately reflects grant-related expenditures as recorded in Epsilon's official accounting system.**

We agree with the recommendation. We will coordinate with Epsilon to obtain a copy of a revised final FFR for cooperative agreement number 2007-RG-CX-K181, which accurately reflects total cumulative Federal grant expenditures recorded in Epsilon's accounting system for the agreement.

8. **Review Epsilon's submitted progress reports related to the project design changes and ensure that the grant file contains the necessary approvals for the changes in project scope.**

We agree with the recommendation. We will coordinate with Epsilon to ensure that the necessary approvals from the NIJ, related to changes in the project scope for cooperative agreement number 2007-RG-CX-K181, are properly documented in OJP's Grants Management System for the agreement.

We appreciate the opportunity to review and comment on the draft audit report. If you have any questions or require additional information, please contact Jeffery A. Haley, Deputy Director, Audit and Review Division, on (202) 616-2936.

cc: Jeffery A. Haley
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OJP Executive Secretariat
Control Number 20111743

**OFFICE OF THE INSPECTOR GENERAL
ANALYSIS AND SUMMARY OF ACTIONS
NECESSARY TO CLOSE THE REPORT**

The OIG provided a draft of this audit report to Epsilon Lambda Electronics Corporation (Epsilon) and the Office of Justice Programs (OJP). Epsilon's response is incorporated in Appendix III of this final report, and OJP's response is incorporated in Appendix IV of this final report. The following provides the OIG analysis of the responses and summary of actions necessary to close the report.

Recommendation Number:

1. **Resolved.** OJP concurred with our recommendation to ensure that Epsilon undergoes the required, independent financial and compliance audits for FY 2008 and FY 2009. Epsilon responded by proposing that this audit be considered sufficient in lieu of the independent financial and compliance audits for FY 2008 and FY 2009 and that an independent financial and compliance audit be completed on the most recent fiscal year prior to the awarding of any subsequent grant funds. Because this OIG audit only focused on one grant awarded to Epsilon and did not thoroughly examine all of Epsilon's financial activities, we do not believe using our report in lieu of the requirement of having independent financial and compliance audits conducted for FY 2008 and FY 2009 is appropriate. In its response, OJP stated that it will coordinate with Epsilon to obtain a copy of the FY 2008 and FY 2009 audit reports, once completed, as well as request a copy of Epsilon's procedures to ensure that all required future audits are performed in a timely manner.

This recommendation can be closed when we receive a copy of the completed independent financial and compliance audits for FY 2008 and FY 2009, as well as Epsilon's procedures, once approved by OJP, for ensuring all required future audits are completed in a timely manner.

2. **Resolved.** Both Epsilon and OJP concurred with our recommendation to ensure that Epsilon implements proper internal controls, including the development of revised financial policies, before the grantee receives any additional funds. OJP stated in its response that it will coordinate with Epsilon to obtain a copy of procedures, developed and implemented, to ensure that Epsilon maintains internal controls that are adequate to administer federal grant funds.

This recommendation can be closed when we receive a copy of the implemented procedures, once approved by OJP, that ensure Epsilon maintains proper internal controls, including revised financial policies that are adequate to administer federal grant funds.

3. **Resolved.** Both Epsilon and OJP concurred with our recommendation to remedy the \$2,852 in unsupported questioned costs related to Epsilon's inability to support its drawdown requests of \$2,230 and the reimbursement of non-personnel and non-contract expenditures for which Epsilon could not provide supporting documentation totaling \$622. OJP stated in its response that it will coordinate with Epsilon to remedy the \$2,852. OJP further stated that if adequate documentation cannot be provided, OJP will request that Epsilon return the funds to DOJ and submit a revised final Federal Financial Report.

This recommendation can be closed when we receive evidence that the \$2,852 in questioned costs have been appropriately remedied.

4. **Resolved.** Both Epsilon and OJP concurred with our recommendation to remedy the \$124,577 in unallowable questioned costs that were used to pay the salary (\$114,579) and fringe benefit costs (\$9,998) of unapproved personnel or the higher than allowed salary and fringe benefit costs of authorized personnel. OJP stated in its response that it will coordinate with Epsilon to remedy the \$124,577 in unallowable questioned costs. OJP further stated that if adequate documentation cannot be provided, OJP will request that Epsilon return the funds to DOJ and submit a revised final Federal Financial Report.

This recommendation can be closed when we receive evidence that the \$124,577 in questioned costs have been appropriately remedied.

5. **Resolved.** Both Epsilon and OJP concurred with our recommendation to remedy the \$5,805 in unsupported questioned costs that were used to procure contract services for which Epsilon could not produce adequate documentation. OJP stated in its response that it will coordinate with Epsilon to remedy the \$5,805 in unsupported questioned costs. OJP further stated that if adequate documentation cannot be provided, OJP will request that Epsilon return the funds to DOJ and submit a revised final Federal Financial Report.

This recommendation can be closed when we receive evidence that the \$5,805 in questioned costs have been appropriately remedied.

6. **Resolved.** Both Epsilon and OJP concurred with our recommendation to remedy the \$45,683 in unallowable questioned costs that were used to procure contract services from contractors that were not included in the approved budget (\$37,710) and for contract cost savings that were not passed on to OJP (\$7,973). OJP stated in its response that it will coordinate with Epsilon to remedy the \$45,683 in unallowable questioned contract services expenditures. OJP further stated that it will request a final determination from the National Institute of Justice (NIJ) regarding the allowability of the contractor services not included in the approved budget. OJP stated that if the expenditures are determined to be unallowable, OJP will request that Epsilon return the funds to DOJ and submit a revised final Federal Financial Report.

This recommendation can be closed when we receive evidence that the \$45,683 in questioned costs have been appropriately remedied.

7. **Resolved.** Both Epsilon and OJP concurred with our recommendation to ensure that Epsilon submits a revised, final Federal Financial report that accurately reflects grant-related expenditures as recorded in Epsilon's official accounting system. OJP stated in its response that it will coordinate with Epsilon to obtain a copy of a revised, final Federal Financial Report, which accurately reflects total cumulative federal grant expenditures recorded in Epsilon's accounting system for the grant under review.

This recommendation can be closed when we receive a copy of the revised, final Federal Financial Report that accurately reflects grant-related expenditures as recorded in Epsilon's official accounting system.

8. **Resolved.** Both Epsilon and OJP concurred with our recommendation to review Epsilon's submitted progress reports related to the project design changes and ensure that the grant file contains the necessary approvals for the changes in project scope. OJP stated in its response that it will coordinate with Epsilon to ensure that the necessary approvals from NIJ for the changes in project scope are properly documented in OJP's Grants Management System.

This recommendation can be closed when we receive evidence of the necessary approvals from NIJ for the changes in project scope and that those approvals are contained in the grant file.