Office of Inspector General
Corporation for National and Community Service

Audit of Corporation for National and Community Service Contract Number CNCS 94-005 with RAND Corporation

OIG Audit Report Number 02-06
April 13, 2001

Financial Schedule and Independent Auditors' Report

For the Period
October 1, 1994 to May 28, 1998

Prepared by
Cotton and Company LLP
333 North Fairfax Street
Alexandria, VA 22314

Under Delivery Order Number
S-OPRAQ-99-D-0021-CNS 13

This report was issued to Corporation management on October 30, 2001. Under the laws and regulations governing audit follow up, the Corporation must make final management decisions on the report's findings and recommendations no later than April 30, 2002, and complete its corrective actions by October 30, 2002. Consequently, the reported findings do not necessarily represent the final resolution of the issues presented.

Office of Inspector General
Corporation for National and Community Service

CORPORATION
FOR NATIONAL
SERVICE

Audit of Corporation for National and Community Service
Contract Number CNCS 94-005 with RAND Corporation
OIG Audit Report Number 02-06

The Office of Inspector General engaged Cotton and Company, LLP to audit costs claimed by the RAND Corporation under CNCS contract number CNCS 94-005. The audit covered the contract period October 1, 1994 through May 28, 1998 and included procedures to determine if costs claimed in financial reports prepared by RAND were allowable, internal controls were adequate to safeguard Federal funds, and whether RAND had policies and procedures adequate to ensure compliance with Federal laws, applicable regulations and award conditions.

As a result of the work performed, the auditors are questioning $8,788 of the $2,243,247 costs claimed over the contract period. Six thousand three hundred and two dollars of the questioned costs results from inadequate supporting documentation of other direct costs. The report discusses this condition in detail.

CNS OIG reviewed the report and the work papers supporting its conclusions. We agree with the findings and recommendations presented. Responses from Rand Corporation and the Corporation for National and Community Service to this report are discussed within the report and included in their entirety as Appendices A and B, respectively.

Inspector General
1201 New York Avenue, NW
Washington, DC 20525

Office of Inspector General
Corporation for National and Community Service

Audit of Corporation for National and Community Service Contract Number CNCS 94-005 with RAND Corporation OIG Audit Report Number 02-06

CONTENTS

COTTON & COMPANY LLP

auditors ◆ advisors

DAVID L. COTTON, CPA, CFE, CGFM ◆ CHARLES HAYWARD, CPA, CFE, CISA ◆ MICHAEL W. GILLESPIE, CPA, CFE ◆ CATHERINE L. NOCERA, CPA
MATTHEW H. JOHNSON, CPA, CGFM ● SAM HADLEY, CPA, CGFM ◆ COLETTE Y. WILSON, CPA

April 13, 2001

Inspector General
Corporation for National and Community Service

We audited costs claimed by RAND Corporation to the Corporation for National and Community Service under Contract No. CNCS 94-005 for the period September 26, 1994, through May 28, 1998. The Corporation awarded Contract No. CNCS 94-005 for the period October 1, 1994 to May 28, 1998, including pre-award costs incurred on or after September 26, 1994. Under this cost-plus-fixed-fee contract, RAND performed evaluations of the Learn and Serve America: Higher Education Program.

The audit objectives were to determine if: (1) costs claimed were allowable and incurred for actual contract effort, adequately supported, and charged in accordance with RAND's cost accounting system, contract terms, applicable laws and regulations including the *Federal Acquisition Regulation* (FAR), and applicable cost accounting standards; (2) RAND complied with contract terms and conditions; and (3) RAND's accounting system and system of internal accounting control were adequate for contract purposes.

We performed the audit in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States. These standards require that we plan and perform the audit to obtain reasonable assurance about whether amounts claimed against the contract, as presented in the Schedule of Contract Costs, are free of material misstatement. An audit includes examining, on a test basis, evidence supporting amounts and disclosures in the Schedule. An audit also includes assessing accounting principles used and significant estimates made by the auditee, as well as evaluating overall financial schedule presentation. We believe our audit provides a reasonable basis for our opinion.

RAND's response is in Appendix A, and the Corporation's response is in Appendix B.

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RESULTS IN BRIEF

Costs Claimed

We have identified $8,788 of questioned costs under the contract, as described in the Schedule of Contract Costs:

- $35 for 2 direct labor hours not supported by timesheets.
- $(586) for 24 unbilled direct labor hours.
- $(251) of fringe benefits applicable to questioned direct labor hours.
- $723 for contract salaries not supported by a personal service agreement.
- $2,605 of travel costs not supported by adequate source documentation.
- $52 of travel costs exceeding the daily per diem limit set by the *Federal Travel Regulations*.
- $6,302 of other direct costs not supported by adequate source documentation.
- $(92) of indirect costs applicable to questioned consultant and labor hours.

The Schedule of Contract Costs provides additional information on these questioned costs based on audit results. RAND had costs incurred in excess of costs billed, therefore we are recommending no net questioned costs.

Compliance

The results of our compliance testing disclosed two instances of noncompliance for which we are recommending corrective action. First, RAND claimed travel costs that were unallowable in accordance with contract terms and conditions and the FAR. Second, RAND did not support all claimed costs with adequate source documentation.

Internal Control

We noted a matter involving RAND's internal control structure and its operations that we consider a reportable condition under standards established by the American Institute of Certified Public Accountants. RAND did not provide documentation supporting claimed consultant, travel, and other direct costs billed to the Corporation. RAND did not provide documentation such as original employee timesheets, invoices, or its general ledger for travel and other direct costs billed.

COTTON & COMPANY LLP

By: [signature] CPA for
Sam Hadley, CPA, CGFM

COTTON & COMPANY LLP

auditors • advisors

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April 13, 2001

Inspector General
Corporation for National and Community Service

INDEPENDENT AUDITORS' OPINION

We audited costs claimed by RAND Corporation to the Corporation for National and Community Service under Contract No. CNCS 94-005 for the period September 26, 1994, through May 28, 1998. The Corporation awarded Contract No. CNCS 94-005 for the period October 1, 1994 to May 28, 1998, including pre-award costs incurred on or after September 26, 1994. Costs claimed are summarized in the Schedule of Contract Costs. Costs claimed summarized in this schedule are the responsibility of RAND management. Our responsibility is to express an opinion on costs shown in the schedule based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States. These standards require that we plan and perform the audit to obtain reasonable assurance that the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting amounts and disclosures in the financial schedules. It also includes assessing accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion on costs claimed.

The Schedule of Contract Costs is intended to present allowable costs incurred under the contract in accordance with the FAR and contract terms and conditions. Therefore, it is not intended to be a complete presentation of RAND Corporation's revenues and expenses.

In our opinion, the Schedule of Contract Costs referred to above presents fairly, in all material respects, costs claimed by RAND for the audit period October 1, 1994, through May 28, 1998, including approved pre-award costs incurred on or after September 26, 1994, in conformity with the FAR and contract terms and conditions.

In accordance with *Government Auditing Standards*, we have also issued reports dated April 13, 2001, on our consideration of RAND's internal control structure and on its compliance with laws and regulations.

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This report is intended solely for the information and use of the Office of Inspector General, the Corporation for National and Community Service, and RAND management and should not be used by anyone other than these specified parties.

COTTON & COMPANY LLP

By: ______________, CPA for
Sam Hadley, CPA, CGFM

FINANCIAL SCHEDULE

SCHEDULE OF CONTRACT COSTS

Corporation for National and Community Service Contract with RAND Corporation
Contract No. CNCS 94-005

September 26, 1994, through May 28, 1998

	Claimed Cost	Questioned Costs	Notes
Direct Salaries	$ 514,426	$ (551)	1
Fringe Benefits	233,466	(251)	2
Contract Salaries	115,056	723	3
Travel	61,210	2,657	4
Subcontract	470,251		
Other Direct Costs	98,677	6,302	5
Computing	57,059		
Indirect Costs	711,899	(92)	6
Subtotal	$2,262,044	$8,788	
Less Costs Incurred In Excess of Costs Claimed	(18,797)	(8,788)	
Total Costs Claimed	$2,243,247	$ 0	

NOTES TO THE SCHEDULE OF CONTRACT COSTS

1. We questioned $(551) of claimed direct labor as follows:

   a. RAND billed $35 for 2 direct labor hours not supported by timesheets. RAND billed CNS for 88 hours, and the employee recorded only 86 hours on the timesheet.

   b. RAND did not bill the Corporation for $586 of direct labor costs. RAND claimed 16 hours of direct labor for an employee in one reporting period, however the employee recorded 40 hours on the timesheet.

   We questioned the net of $(551) in accordance with FAR 31.201-2, Determining allowability, which requires that claimed costs be supported by adequate records. We did not expand the number of sample items originally selected, due to the immateriality of audit results.

2. We questioned fringe benefits of $(251) allocable to questioned direct labor costs of $(551), calculated as follows:

Fiscal Year	Questioned Direct Labor	Fringe Benefit Rate	Questioned Fringe Benefits
1996	$ 35	45.151%	$ 16
1998	(586)	45.546	(267)
Total	$(551)		$(251)

3. RAND billed $723 in 1996 for consultant costs claimed not supported by a personal service agreement. In accordance with FAR 31.205-33, Consulting costs, claimed costs must be supported by signed personal service contracts that document the scope of work to be performed and the daily or hourly rate to be paid. In addition, RAND could not provide an invoice or other documentation to support actual hours or days worked.

   We did not expand the number of sample items originally selected for the following reasons:

   - We noted only one occurrence of unsupported costs in our sample. RAND representatives stated that contracted salary agreements are always maintained to support claimed costs, but the agreement for the sampled consultant had been filed in a different box than indicated on its records.

- RAND receives an annual audit in accordance with Office of Management and Budget (OMB) Circular A-133. This audit coverage includes contract costs sampled for allowability, allocability, and proper documentation. We reviewed the Circular A-133 audits performed over the contract period and noted no findings related to unallowable contract costs or inadequate supporting documentation.

4. We questioned $2,605 of travel costs as follows:

   a. RAND could not support 2 airfares ($1,190 in July 1996 and $811 in July 1998). We questioned $2,001 of claimed airfare costs not supported by adequate source documentation, in accordance with FAR 31.201-2, Determining allowability.

   b. We questioned $604 of travel costs claimed from one employee's expense voucher, because RAND could not provide the requested expense voucher or other supporting documentation ($604 in July 1998), in accordance with FAR 31.201-2, Determining allowability.

   We did not expand the number of sample items originally selected for the following reasons:

   - Questioned costs are the result of missing documentation. During our audit, RAND had difficulty retrieving documentation for requested sample items due to the age of the samples and RAND's small staff size. RAND representatives stated that supporting documentation was maintained, but retrieving files was very time consuming, and they could not devote any more staff time to finding the documentation. They selected the larger sample items and retrieved the documentation.

   - As discussed in Note 3, RAND receives an annual OMB Circular A-133 audit, whereby the auditors test allowability and allocability of sampled contract costs.

   Without adequate supporting documentation, we were unable to determine the allowability of costs claimed in accordance with FAR 31.201-2, Determining allowability. In addition, FAR 52.215-2, Audit and Records—Negotiation, Section (f), Availability, states that the contractor is to make available at its office at all reasonable times the records, materials, and other evidence for examination, audit, or reproduction for three years after final payment under a contract.

   c. We questioned $52 of claimed travel costs exceeding the maximum daily limit allowed by the Federal Travel Regulations (FTR). According to FAR 31.205-46 (a), Travel costs, costs incurred for lodging, meals, and incidental expenses will be considered reasonable and allowable only to the extent that they do not exceed on a daily basis the maximum per diem rates in effect at the time of travel as set forth in the FTR.

We selected a sample of 28 travel transactions which totaled $18,380, and noted that three transactions included costs of $52 that exceed the FTR. We did not expand our sample of claimed travel costs due to the immateriality of total claimed travel costs ($61,210). Additional sample items would not result in a material amount of additional questioned costs.

5. We questioned $6,302 of other direct costs. RAND did not provide supporting documentation for 12 of 30 sampled items. We did not expand the number of sample items originally selected for reasons stated in Note 4.

6. We questioned $(92) of claimed indirect costs applicable to questioned direct labor, fringe benefits, and contract salaries as calculated below:

Fiscal Year	**Questioned Direct Costs**	**Overhead Rate**	**Questioned Overhead Costs**
1996	$774	78.576%	$608
1998	(853)	82.001	(700)
Total	$ (79)		$ (92)

INDEPENDENT AUDITORS' REPORTS ON COMPLIANCE AND INTERNAL CONTROL STRUCTURE

COTTON & COMPANY LLP

auditors ◆ advisors

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April 13, 2001

Inspector General
Corporation for National and Community Service

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE

We audited costs claimed by RAND to the Corporation for National and Community Service under Contract No. CNCS 94-005 for the period September 26, 1994, through May 28, 1998, and have issued our report thereon dated April 13, 2001. The Corporation awarded Contract No. CNCS 94-005 for the period October 1, 1994, to May 28, 1998, including approved pre-award costs incurred on or after September 26, 1994.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States. These standards require that we plan and perform the audit to obtain reasonable assurance that financial schedules are free of material misstatement.

Compliance with applicable laws and regulations related to the contract is the responsibility of RAND's management. As part of obtaining reasonable assurance that costs are free of material misstatements, we performed tests of compliance with certain provisions of laws and regulations related to the contract. Our objective was not, however, to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our compliance testing regarding claimed costs disclosed the following nonmaterial instances of noncompliance that are required to be reported under *Government Auditing Standards*:

1. As discussed in the Notes to the Schedule of Contract Costs, RAND claimed direct labor, contract salaries, other direct costs, and travel, not adequately supported in accordance with contract terms and conditions and the FAR. RAND stated it did not provide supporting documentation for all requested sample items, because it has limited staff to retrieve documentation.

   Recommendation: We recommend that the Corporation request RAND to maintain all documentation to support claimed costs and provide documentation upon request.

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RAND's Response: RAND noted that the unsupported items were low-dollar items going back several years. RAND considered the administrative costs of searching for support for these items to be burdensome, and RAND did not provide these items. Its representatives further noted that it will no longer be claiming these costs.

Further, RAND noted that it is subject to four main audits by outside independent entities, including the OMB Circular A-133 audit, incurred cost claim audit, and a Cost Accounting Standards audit. The costs claimed would have been subject to audit in each of the years covered by this audit, and the scope of this audit (allowability, allocability, and proper documentation) would be covered in those audits.

Finally, RAND noted that OMB Circular A-133, Subpart B, Section .215, states that "An audit made in accordance with this part shall be in lieu of any financial audit required under individual Federal awards...Any additional audits shall be planned and performed in such a way as to build upon work performed by other auditors." RAND noted that it has concerns that there was not enough audit coordination between Cotton & Company auditors and its independent auditors; RAND noted that Cotton & Company did request permission to contact the independent auditors toward the end of the audit.

Auditors' Response: The unsupported items do relate to small-dollar items dating back several years. RAND's record retention obligations are not, however, diminished as claimed contract costs age.

Additionally, as noted by RAND, an OMB Circular A-133 audit is to be relied upon to the extent the audit meets a Federal agency's needs. During the planning phase of our audit, we determined that CNS funds had not been selected as a major program in any of the years covered by our audit, and that the nature of programs selected as major programs in those years was not similar in nature to CNS funds. We did incorporate the internal control and compliance work done by other auditors, but could not rely on that audit to meet the needs of CNS.

Finally, RAND is mistaken when noting that Cotton & Company did not request to contact the independent auditors until the end of the audit. Our first step in the planning phase of this audit was to contact the Defense Contract Audit Agency and discuss its audit scope of RAND. It was that auditor who noted that DCAA had never audited CNS funds. In addition, we met with DCAA during our first day of fieldwork in December 2000. During that meeting, DCAA noted that several of the indirect rates applied to the CNS contract are not reviewed by DCAA, because they were not applied in the contracts that were the focus of DCAA's work. Also during our second stage of fieldwork in January 2001, we attempted to contact both independent audit entities with no success. Documentation of our conversations and attempted contacts is included in our workpapers.

Corporation's Response: The Corporation agrees with the costs questioned in accordance with the FAR, but does not agree with the net questioned costs of $0, because RAND had $18,797 of costs incurred in excess of costs claimed, which exceeded questioned costs of $8,788. The Corporation thinks that costs incurred in excess of costs claimed are unallowable per FAR 31.201-2 (a) (4), because RAND is not entitled to reimbursement for costs incurred in excess of the contract terms. Therefore, costs incurred in excess of contract terms cannot be used to offset specifically unallowable costs. The Corporation has discussed the repayment of these costs with RAND.

The Corporation also stated that the audit report does not address whether the claimed indirect cost rates used to calculate claimed costs were based on DCAA-approved indirect rates. The Corporation needs this information to close out the contract.

Auditors' Comments: Costs incurred in excess of costs claimed are otherwise *allowable*, they are simply not claimed. As the Corporation noted, RAND is no longer claiming the expressly unallowable costs; it does, however, still have incurred allowable costs in excess of amounts claimed. All costs incurred were included in the scope of our review, and only \$8,788 was found to be unallowable, leaving \$2,253,256 of allowable costs. RAND should be reimbursed for incurred costs up to the contract ceiling of \$2,243,247. Additionally, because all incurred costs were included in the audit scope, it is possible that some or all of the questioned costs of \$8,788 were not actually claimed, because they were included in the \$18,797 of costs that exceeded the contract ceiling.

The audit report does not typically describe how claimed costs were calculated; rather, it provides discussion on any questioned costs, noncompliance, and internal control weaknesses. RAND applied several indirect cost rates in its claim that were not reviewed by DCAA. For those rates audited by DCAA, we determined that the DCAA-approved rates were used. For those rates not reviewed by DCAA, we determined the nature of the rate, assessed the adequacy and allocability of the rate to the claim, and determined that the application of the rates was proper.

2. RAND claimed travel costs that exceeded Federal Travel Regulations (FTR) limits. RAND's travel policy recognizes the limits imposed by the FTR and complies with them. RAND representatives could not explain why costs that exceeded FTR limits were allowed and recorded as an allowable contract cost. Additionally, we could not determine why the annual OMB Circular A-133 audit did not disclose this noncompliance.

Recommendation: We recommend that the Corporation direct RAND to limit claimed costs to those that are allowable under applicable cost principles and contract provisions.

RAND's Response: RAND noted that the disallowed costs relate to trips that did not involve an overnight stay. To prevent recurrences, RAND management will emphasize training and education for the finance personnel involved with implementing FAR regulations related to this issue.

We considered the above instances of noncompliance in forming our opinion on whether RAND's costs claimed under the contract for the period September 26, 1994, through May 28, 1998, are presented fairly, in all material respects, pursuant to contract terms and conditions and FAR. This nonmaterial instance of noncompliance does not affect our report on claimed costs.

This report is intended solely for the information and use of the Office of Inspector General, the Corporation for National and Community Service, and RAND management and should not be used by anyone other than these specified parties.

COTTON & COMPANY LLP

By: Alan Rosenthal CPA for
Sam A. Hadley, CPA, CGFM

COTTON & COMPANY LLP
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April 13, 2001

Inspector General
Corporation for National and Community Service

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL STRUCTURE

We audited costs claimed by RAND to the Corporation for National and Community Service under Contract No. CNCS 94-005 for the period September 26, 1994, through May 28, 1998, and have issued our report thereon dated April 13, 2001. The Corporation awarded Contract No. CNCS 94-005 for the period October 1, 1994, to May 28, 1998, including approved pre-award costs incurred on or after September 26, 1994.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States. These standards require that we plan and perform the audit to obtain reasonable assurance that financial schedules are free of material misstatement.

RAND's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial schedules in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate, because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit, we obtained an understanding of RAND's internal control structure. We obtained an understanding of the design of relevant policies and procedures and whether they had been placed in operation, and we assessed control risk to determine our auditing procedures for the purpose of expressing an opinion on claimed costs and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

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We noted a matter involving the internal control structure and its operation that we consider a reportable condition under standards established by the American Institute of Certified Public Accountants (AICPA). Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect an organization's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial schedules. The reportable condition is as follows:

1. RAND did not provide documentation supporting all travel, and other direct costs billed to the Corporation. RAND did not provide support, such as invoices, or its general ledger, for travel and other direct costs billed. FAR 52.215-2, Audit and Records—Negotiation, Section (f), Availability, states that the contractor is to make available at its office at all reasonable times the records, materials, and other evidence for examination, audit, or reproduction for three years after final payment under a contract.

   Recommendation: We recommend that the Corporation direct RAND to retain all documentation supporting costs billed in accordance with the FAR.

   RAND's Response: RAND notes that its internal controls were audited by independent agencies for the contract period, and no findings of unallowed costs or inadequate documentation were noted. RAND further notes that it has an extensive set of policies, procedures, and practices designed to provide reasonable assurance that assets are safeguarded, and transactions are executed and recorded properly. RAND considers the combination of these policies and the external audits to be adequate to maintain good internal controls. Finally, RAND stated that it has and will continue to perform independent compliance testing or review functions where it has determined that improvements are appropriate.

   Auditors' Response: We agree that RAND has internal controls to safeguard assets and properly record transactions; we continue to recommend, however, that RAND revise its recordkeeping procedures to provide all necessary supporting documentation in accordance with Federal requirements.

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited occurred and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by AICPA. In our opinion, the condition described above is not a material weakness.

This report is intended solely for the information and use of the Office of Inspector General, the Corporation for National and Community Service, and RAND management and should not be used by anyone other than these specified parties.

COTTON & COMPANY LLP

By: Alan Rosenthal, CPA for

Sam Hadley, CPA, CGFM

APPENDIX A

RAND's RESPONSE

RAND

September 27, 2001

Ms. Luise S. Jordan
Inspector General
Office of Inspector General
1201 New York Avenue, NW
Washington, D.C. 20525

Reference: Audit Report No. 01-29

Dear Ms. Jordan,

Below is RAND's response to the Inspector General's audit findings contained in the above-referenced report.

1. Schedule of Contract Costs

The audit included the substantive testing of low dollar items relating back several years. Because the administrative costs of searching for the final remaining items became burdensome, RAND did not provide these items. Therefore, RAND will not claim them.

RAND is already subject to four main audits by outside independent entities. These include the A-133, incurred cost claim and CAS audits performed by PricewaterhouseCoopers ("PWC") and the Defense Contract Audit Agency ("DCAA"). The costs claimed would have been subject to audit by these entities in each of the years covered by the Inspector General's audit. As noted in the report, the audits' coverage includes contract costs sampled for allowability, allocability, and proper documentation covered under the Corporation for National and Community Service contract period. There were no findings related to unallowable contract costs or inadequate supporting documentation in these audits.

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Pursuant to the Single Audit Act, OMB Circular A-133, Subpart B, section .215 states, "An audit made in accordance with this part shall be in lieu of any financial audit required under individual Federal awards. To the extent this audit meets a Federal Agency's needs, it shall rely upon and use such audits... Any additional audits shall be planned and performed in such a way as to build upon work performed by other auditors." RAND has some concerns that there was not enough coordination between the auditors and PWC or DCAA, which may have expedited some of the audit work. The auditors did request to contact PWC and DCAA towards the end of their audit.

2. Compliance

a. Supporting Documentation

As discussed above, RAND is audited by many outside entities and the audits that were performed at the time the costs were incurred did not find that costs were not adequately supported or that documentation was not provided upon request.

b. Travel Costs

The $52 of disallowed costs relate to reimbursements paid for trips completed in one day that did not involve an overnight stay. RAND management will emphasize training and education of the finance personnel involved with implementing the FAR regulations related to compliance with the questioned travel costs allowed by the Federal Travel Regulations in order to prevent recurrences in this area.

3. Internal Controls

RAND's internal controls were audited by outside independent entities, including PWC and DCAA, for the contract period and no findings of unallowable contract costs or inadequate supporting documentation were noted. RAND has an extensive set of polices, procedures and practices designed to provide reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principals. RAND considers the combination of these policies and procedures and the scope of the external independent audits to be adequate to maintain good internal controls.

RAND

Notwithstanding the above, RAND has and will continue to perform its own independent compliance testing or review of certain functions where RAND has determined that it is appropriate in order to make improvements.

RAND is very appreciative of the opportunity to respond to the draft Inspector General audit report and believes that such a process is in the best interests of the government and of RAND, especially when the exchange can clarify and narrow or eliminate differences of opinion about the matters under audit.

If you have any questions, please do not hesitate to contact me at 310-393-0411, extension 7161.

Sincerely,

Mary Colombo

Mary Colombo
Director, Special Projects and Financial and
Regulatory Reporting

MC:bc

cc: Steve Larson, CNCS
Kathy Leone, IG
Sam Hadley, Cotton and Company
Ken Krug, RAND
Lisa Neufeld, RAND

APPENDIX B

THE CORPORATION'S RESPONSE

CORPORATION

FOR NATIONAL

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RECEIVED
SEP 26 2001
OFFICE OF THE INSPECTOR GENERAL

MEMORANDUM

DATE: September 26, 2001

TO: Luise Jordan, Inspector General

Simon Woodard

THRU: Simon Woodard, Director of Procurement Services

Stephen R. Larson

FROM: Stephen R. Larson, Audit Resolution Manager – OIG Report No. 01-29

SUBJECT: OIG Draft Report No. 01-29 Audit of Contract Number CNCS 94-005 with RAND Corporation.

We have reviewed the draft Office of Inspector General (OIG) audit report of the Corporation's contract with RAND Corporation and have provided comments on our preliminary conclusions on questioned costs, and internal control/compliance issues as discussed below.

Questioned Costs on Contract Number CNCS 94-005: We concur with the overall finding that RAND Corporation did not provide adequate support documentation for $8,788 of questioned labor, applicable indirect costs, travel costs, and other direct costs noted in the audit report. In accordance with FAR 52.215-2 "Audit and Records" the contractor shall maintain and the Contracting Officer or authorized representative shall have the right to examine and audit all records and other evidence sufficient to reflect properly all costs claimed directly or indirectly in performance of this contract." This clause further states that the contractor shall make these records available until 3 years after final payment under this contract. Ms. Mary Colombo, Director Special Projects and Financial Regulatory Reporting, in a September 19, 2001 memorandum stated "that at a certain point in the audit, the administrative costs to RAND outweighed the benefits of searching for the remaining items. Therefore, RAND will not claim them." Based on the audit report findings and contractor's statement above we find the $8,788 of costs to be unallowable in accordance with FAR 31.201-2 "determining allowability."

Contract Modification Number 4 dated September 13, 1996 increased the estimated costs to $2,243,247 and fixed fee to $163,095. The total estimated costs plus fixed fee or ceiling on the contract was increased to $2,406,342. Review of the contractor's Voucher Number 49 Final dated May 21, 1999 showed the contractor's actual cumulative costs incurred to be $2,262,044.13. Further review of this voucher shows that the contractor did not claim $18,797.13 of costs that were in excess of the estimated costs of $2,243,247. These costs of $18,797.13 are not allowable in accordance with FAR 31.201-2(a)(4) "terms of the contract", because the estimated costs of $2,243,247 is a ceiling on reimbursement for allowable costs. The contractor properly did not claim costs in excess of contract terms on their billings to the government. We do not agree with the total questioned costs of $0.00 shown on Page 6 of the audit report, because the $18,797 of excess costs are unallowable per FAR 31.201-2(a)(4), and the contractor is not entitled to reimbursement for costs incurred in excess of the contract terms. The $8,788 of questioned costs shown in the audit report was either not adequately supported or specifically unallowable per FAR clauses. The $18,797 of costs incurred in excess of the contract terms cannot be used to offset specifically unallowable costs of $8,788 with the net questioned costs of $0.00. The correct questioned costs should be $8,788, because these costs are specifically unallowable as addressed in the audit report, and are not challenged by the contractor. We paid the contractor a total of $2,406,432 through Voucher Number 49 consisting of $2,243,247 of costs plus the fixed fee of $163,095. Based on the results of the audit report the contractor is not entitled to $8,788 of costs that were not adequately supported or specifically unallowable, therefore we will request the contractor to repay this amount prior to closing out the contract. We discussed this repayment of unallowable costs with Ms. Mary Colombo on September 26, 2001, and she understands our position that one unallowable cost can not be used to offset another unallowable cost.

The OIG audit report shows $233,466 of fringe benefits, and $711,899 of other indirect costs claimed on our contract. This is a cumulative number and there is no breakdown in the audit report indicating the indirect costs and rate used by fiscal year. There are also no comments in the OIG audit report indicating that the contractor's claimed costs shown on the Schedule of Contract Costs on page 6 are based on the DCAA audit determined indirect rates for fiscal years 1994 - 1998. Based on discussion with Ms. Mary Colombo on September 26, 2001 the detailed breakdown of direct and indirect costs by fiscal year and the DCAA audit determined indirect rates was provided to the Cotton & Company auditor. Therefore, the audit report should be revised to state whether the contractor's claimed indirect costs shown on Final Voucher No. 49 are based on using the DCAA audit determined indirect rates. We need this information prior to closing out the contract.

Internal Control and Compliance Issues: I contacted DCAA to determine the adequacy of relevant accounting billing, timekeeping, and related systems applicable to billing of costs on government contracts. I reviewed the Organization and Systems Section of the Fiscal Year 2000 A-133 (incurred costs) audit report dated June 22, 2001 to determine the current status of relevant internal controls and systems. This review revealed that DCAA has found the Contractor's accounting, labor accounting systems, and Indirect and ODC Systems and related policies and procedures to be inadequate in part based on the system audits performed by DCAA. DCAA is the Cognizant audit agency and is responsible for following up on the discrepancies summarized above. We do not have a current contract with RAND Corporation. Therefore, we do not intend to give RAND Corporation any additional comments on the adequacy of their internal control systems. Before awarding any new contracts to RAND Corporation we will contact DCAA to determine the adequacy of the applicable accounting, timekeeping, and billing systems.

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