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**Office of the Inspector General  
Corporation for National and Community Service**

**Audit of  
Corporation for National and Community Service  
Contract No. 95-743-1009  
With Biospherics, Inc.**

**Report Number 99-09  
May 6, 1999**

*Prepared by:*

Cotton & Company, LLP  
333 North Fairfax Street, Suite 401  
Alexandria, Virginia 22314

Under CNS OIG MOU # 94-0468-1027  
With the Department of State  
Contract # S-OPRAQ-94C-0468-18

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**This report was issued to Corporation management on May 6, 1999. 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 November 2, 1999, and complete its corrective actions by May 6, 2000. Consequently, the reported findings do not necessarily represent the final resolution of the issues presented.**

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**Office of the Inspector General  
Corporation for National and Community Service**

CORPORATION  
FOR NATIONAL  
SERVICE

**Audit of Corporation for National and Community Service  
Contract No. 95-743-1009  
With Biospherics, Inc.**

Cotton & Company,LLP, under contract to the Office of the Inspector General, audited the amounts claimed by Biospherics, Inc. under Contract 95-743-1009. The audit covered the costs (\$4,475,214) claimed during the period from June 22, 1995 through October 31, 1998, and included tests to determine whether costs reported to the Corporation were documented and allowable in accordance with the terms and conditions of the contract. We have reviewed the report and work papers supporting its conclusions and agree with the findings and recommendations presented.

The auditors found that Biospherics, Inc.:

- Claimed costs for work performed by employees at labor rates not included in the contract or contract modifications;
- Claimed other direct costs as “standard costs” based on unsupported standard rates, in lieu of billing other direct costs based on actual costs as required by the contract; and
- Claimed costs for direct mailing services under a subcontract that was not approved by the contracting officer, as required by the contract.

As a result, we are questioning \$739,458 (17 percent) in costs claimed under the contract. Additional information on the questioned costs as well other compliance and internal control findings are discussed in detail in this report.

The Corporation’s response to a draft of this report is included as an Appendix. In its response, the Corporation stated that it had reviewed the draft but did not have specific comments at this time and plans to address the findings and recommendations as part of the audit resolution process.

Biospherics, Inc. did not respond within the comment period. Instead, Biospherics sent a letter by facsimile five days after the due date in which it disagreed with the questioned costs.

**OFFICE OF INSPECTOR GENERAL  
CORPORATION FOR NATIONAL AND COMMUNITY SERVICE  
AUDIT REPORT NUMBER 99-09**

**AUDIT OF  
CORPORATION FOR NATIONAL AND COMMUNITY SERVICE  
CONTRACT NO. 95-743-1009 WITH  
BIOSPHERICS, INC.**

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# COTTON & COMPANY

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March 1, 1999

Inspector General  
Corporation for National and Community Service

We audited costs claimed by Biospherics, Inc., to the Corporation for National and Community Service under Contract No. 95-743-1009 for the period from June 22, 1995, through October 31, 1998, the contract award period. Under this time-and-materials contract, Biospherics provided public access to toll-free and fulfillment services on behalf of the AmeriCorps recruitment group.

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

We performed the audit in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 the amounts and disclosures in the Schedule. An audit also includes assessing the accounting principles used and significant estimates made by the auditee, as well as evaluating the overall financial schedule presentation. We believe our audit provides a reasonable basis for our opinion.

The Corporation's response to the draft report is included as an Appendix. In its response, the Corporation stated that it reviewed the draft report and did not have specific comments, but will address the findings and recommendations in the final management decision.

Biospherics did not respond within the comment period. Instead Biospherics sent a letter by facsimile 5 days after the due date in which it disagreed with the questioned costs.

## ***RESULTS IN BRIEF***

### **Costs Claimed**

We questioned \$739,458, or approximately 17 percent of the \$4,475,214 claimed under the contract. The majority of these costs, \$406,711 (approximately 9 percent), was questioned because Biospherics claimed labor costs for work performed by employees at labor rates that did not agree with the rates in the contract or contract modifications. The contract specifies the allowable labor categories and unit prices. Biospherics' contract administrator stated that the Corporation's contracting officer instructed them verbally to use the new labor categories and unit prices that it billed the Corporation. The contracting officer did not process modifications or send a letter adding these labor categories and unit prices.

We also questioned other direct costs of \$324,832 claimed under the contract. Biospherics billed other direct costs as "standard costs," but did not have support for the rates billed. It based the rates on unsupported amounts and did not calculate actual costs on an annual basis.

Biospherics billed the Corporation for \$7,915 [\$6,377 plus \$1,020 of general and administrative (G&A) expense and \$518 profit] for direct mailing services subcontracted to another firm. The subcontract was not approved by the contracting officer. Accordingly, we questioned \$7,915.

The Schedule of Contract Costs provides additional information on these questioned costs based on the results of our audit.

### **Compliance**

The results of our tests of compliance regarding claimed costs disclosed that Biospherics claimed labor, subcontract, and other direct costs based on standard costs that were unallowable and unallocable in accordance with contract terms and conditions and the *Federal Acquisition Regulation*, as discussed above and in detail in the Notes to the Schedule of Contract Costs.

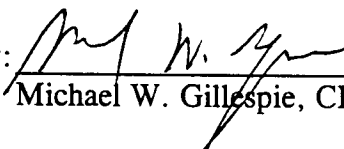
### **Accounting and Internal Control Systems**

We noted two matters involving Biospherics' internal control structure and its operations that we consider reportable conditions under standards established by the American Institute of Certified Public Accountants. We believe that the first matter is a material weakness.

First, Biospherics billed the Corporation at rates based on "standard costs" for some direct costs. It based the rates on unsupported amounts, and did not calculate actual costs on an annual basis or document its procedures for calculating the standard rates. The contract requires Biospherics to bill actual costs.

Second, Biospherics does not have adequate timekeeping procedures. Employees used correction fluid to alter timesheets, and supervisors and employees did not initial all changes. Sound internal controls dictate that, at a minimum, employees and their supervisors mark through and initial timesheet changes.

COTTON & COMPANY, LLP

By:   
Michael W. Gillespie, CPA

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March 1, 1999

Inspector General  
Corporation for National and Community Service

## INDEPENDENT AUDITORS' OPINION

We audited costs claimed by Biospherics, Inc., to the Corporation for National and Community Service under Contract No. 95-743-1009 for the period from June 22, 1995, through October 31, 1998, the contract award period. Costs claimed are summarized in the Schedule of Contract Costs. Costs claimed summarized in the schedule are the responsibility of Biospherics 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 schedule is free of material misstatement. An audit includes examining, on a test basis, evidence supporting amounts and disclosures in the financial schedule. 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.

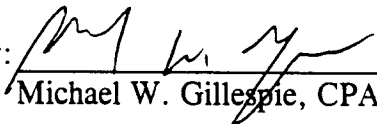
This schedule is intended to present allowable costs incurred under the contract in accordance with the *Federal Acquisition Regulation* and contract terms and conditions. Therefore, it is not intended to be a complete presentation of Biospherics' revenues and expenses.

In our opinion, except for questioned costs in the Schedule of Contract Costs, the financial schedule referred to above presents fairly, in all material respects, costs claimed by Biospherics as these costs relate to the contract for the audit period from June 22, 1995, through October 31, 1998, in conformity with the *Federal Acquisition Regulation* and contract terms and conditions.

In accordance with *Government Auditing Standards*, we have also issued reports dated March 1, 1999, on our consideration of Biospherics' internal control structure and on its compliance with laws and regulations.

This report is intended for the use of the Inspector General and Corporation management. This report is a matter of public record, and its distribution is not limited.

COTTON & COMPANY, LLP

By:   
Michael W. Gillespie, CPA



## **FINANCIAL SCHEDULE**

## SCHEDULE OF CONTRACT COSTS

**Corporation For National and Community Service Contract With  
Biospherics, Inc.**

**Contract No. 95-743-1009  
June 22, 1995 through October 31, 1998**

	Claimed Costs	Questioned Costs	Notes
Salaries and Wages	\$3,151,234	\$406,711	1. a, b
Postage	707,850		
Computer	82,000	82,000	2
Telephone Instruments	29,700	29,700	2
Telephone, Local Service	29,465		
Voice Mail	107,785	107,785	2
Warehouse Space	32,200		
Supplies	94,876		
Reproduction	96,347	96,347	2
Local Travel	11,061	9,000	2
G&A	57,690		
Mail Services Subcontract	7,915	7,915	3
Equipment, Cubix Server	<u>67,091</u>	<u>          </u>	
Total	<u>\$4,475,214</u>	<u>\$739,458</u>	

## NOTES TO SCHEDULE OF CONTRACT COSTS

1. We questioned \$406,711 of salaries and wages as follows:
  - a. We questioned \$38,589 billed to the Corporation, which was calculated at labor rates that exceeded rates in the contract or contract modifications. Contract Section B.3, specifies labor categories and unit prices allowable under the contract. Biospherics' contract administrator stated that he increased the rates based on discussions with the Corporation's contracting officer. He stated that the increase reflected increased costs resulting from the 1996 "government shutdown," higher-than-expected costs for its subcontractor, Quality Support, Incorporated (QSI), and overtime paid to some employees. The contracting officer did not, however, process contract modifications for these rate changes. We questioned the following:

Labor Category	Contract Rates			Difference	Hours	Total
	Billed Rate	Option Year 1 (10/95-09/96)	Option Year 2 (10/96-09/97)			
Project Director	\$52.23	\$49.12		\$ 3.11	28.00	\$ 87
Project Manager	40.06	37.68		2.38	1,164.50	2,772
Line Supervisor (QSI)	31.68	28.33		3.35	1,239.00	4,151
Line Supervisor (QSI) Overtime	47.52	28.33		19.19	52.50	1,007
Line Supervisor (QSI) Overtime	49.67		\$33.11	16.56	21.50	356
Information Specialist	20.50	19.23		1.27	10,461.25	13,286
Information Specialist Overtime	30.75	19.23		11.52	56.75	654
Information Specialist Overtime	31.70		21.13	10.57	35.75	378
General Clerk (QSI)	20.68	18.50		2.18	3,792.50	8,268
General Clerk (QSI) Overtime	30.34	18.50		11.84	94.00	1,113
General Clerk (QSI) Overtime	32.45		21.63	10.82	46.00	498
General Clerk	20.50	18.50		2.00	1,694.50	3,389
Systems Analyst	61.86	58.18		3.68	580.50	2,136
Telecomm. Specialist	34.84	32.77		2.07	49.00	101
Courier	17.98	16.91		1.07	<u>367.75</u>	<u>393</u>
<b>Total</b>					<u>19,683.50</u>	<u>\$38,589</u>

- b. We questioned \$368,122 billed for work performed by individuals employed by temporary employment agencies. Contract Section H.2 states that prior written approval of the contracting officer is required before utilizing the services of any consultant. According to Biospherics representatives, they did not inform anyone at the Corporation that temporary employees were being used on the contract. Biospherics' contract administrator stated that he considered these individuals to be the same as Biospherics employees in terms of the contract, because they worked in Biospherics' offices, and the contract did not define "employee." He also stated that, because the work was performed at Biospherics' offices, some overhead costs were associated with these consultants. The actual amount paid to the temporary employment agencies for these individuals was \$270,601. The \$97,521 difference between the amount paid to the temporary agencies and the amount claimed under the contract represents additional profit to Biospherics. Because Biospherics did not have written contracting officer approval to utilize consultants, we questioned the entire \$368,122 as follows:

Labor Category	Consultant Hours	Amount Billed	Questioned in Note 1a, above	Questioned Costs	Amount Paid to Agencies
Systems Analyst	3,067	\$196,263	\$ 519	\$195,744	\$183,679
Information Specialist	4,311	92,731	884	91,847	42,567
General Clerks	3,776	<u>82,325</u>	<u>1,794</u>	<u>80,531</u>	<u>44,355</u>
Total		<u>\$371,319</u>	<u>\$3,197</u>	<u>\$368,122</u>	<u>\$270,601</u>

2. Biospherics billed the Corporation for some types of costs at "standard costs." However, it did not document in writing the calculation of the standard costs or support the reasonableness of the rates used by periodic comparisons to actual costs. Contract Section B.3 states that other direct costs "shall be billed at actual cost." Further, *Federal Acquisition Regulation* (FAR) 31.201-1, Composition of Total Costs, states that costs include standard costs properly adjusted for applicable variances. Cost Accounting Standard (CAS) 407 provides guidance on the use of standard cost accounting systems for government contracts. CAS 407 states that standard costs may be used only when the contractor enters standard costs into the books of account, accounts for standard costs and related variances, and states in writing its practices with regard to the setting and revising of standards and disposition of variances. FAR 31.201-2(d), Determining Allowability, states that the contractor is responsible for accounting for costs appropriately and for maintaining adequate supporting documentation.

Biospherics' contract administrator stated that Biospherics has no documentation for actual rates, but they consider the rates reasonable and disclosed them in Biospherics' cost proposals submitted to the Corporation. Because these costs are not supported, we questioned \$324,832 as follows:

- \$82,000 for computer terminal usage at monthly rates of \$100, \$150, and \$200 for each work station.
- \$29,700 for telephone instrument usage at monthly rates of \$45 and \$60 per workstation.
- \$107,785 for voice mail usage at \$0.40 per call.
- \$96,347 for reproduction at \$0.06 per copy.
- \$9,000 for use of the company van at \$225 a month.

3. Biospherics billed \$7,915 [\$6,377 paid plus \$1,020 of general and administrative (G&A) expense and \$518 profit] for direct mail services subcontracted to ABR Services, Inc. The subcontract and associated costs were not identified in the contract or any of the contract modifications. Biospherics sent a letter to the contracting officer dated February 20, 1998, requesting written approval to proceed with the proposed subcontract. According to Biospherics' contract administrator, contracting officer approval was never received, but they did receive approval from an information specialist at AmeriCorps. Contract Section H.2, states that prior written contracting officer approval is required before utilizing the services of any consultant. Because Biospherics did not have written contracting officer approval to incur these costs, we questioned the \$7,915 claimed.

**INDEPENDENT AUDITORS' REPORTS ON COMPLIANCE  
AND INTERNAL CONTROL STRUCTURE**

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March 1, 1999

Inspector General  
Corporation for National and Community Service

## INDEPENDENT AUDITORS' REPORT ON COMPLIANCE

We audited costs claimed by Biospherics, Inc., to the Corporation for National and Community Service under Contract No. 95-743-1009 for the period from June 22, 1995, through October 31, 1998, the contract period, and have issued our report thereon dated March 1, 1999.

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 schedule is free of material misstatement.

Compliance with applicable laws and regulations related to the contract is the responsibility of Biospherics management. As part of obtaining reasonable assurance that costs claimed 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 tests of compliance regarding claimed costs disclosed the following material instances of noncompliance that are required to be reported herein under *Government Auditing Standards*:

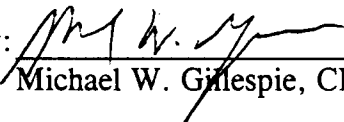
Biospherics claimed labor, other direct costs, and subcontract costs that were unallowable and unallocable in accordance with contract terms and conditions and the *Federal Acquisition Regulation*. Refer to the Schedule of Contract Costs on page 6.

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

We considered the above material instance of noncompliance in forming our opinion on whether Biospherics' costs claimed under the contract for the period from June 22, 1995, through October 31, 1998, are presented fairly, in all material respects, pursuant to contract terms and conditions and the *Federal Acquisition Regulation*. Because of the material instance of noncompliance and matters described in the Schedule of Contract Costs, our opinion on the schedule is qualified.

This report is intended for the use of the Inspector General and Corporation management. This report is a matter of public record, and its distribution is not limited.

COTTON & COMPANY, LLP

By:   
Michael W. Gillespie, CPA



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March 1, 1999

Inspector General  
Corporation for National and Community Service

## INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL STRUCTURE

We audited costs claimed by Biospherics, Inc., to the Corporation for National and Community Service under Contract No. 95-743-1009 for the period from June 22, 1995, through October 31, 1998, the contract period, and have issued our report thereon dated March 1, 1999.

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 schedule is free of material misstatement.

Biospherics 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 Biospherics' internal control structure. We obtained an understanding of the design of relevant policies and procedures and whether they have 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.

We noted two matters involving the internal control structure and its operations that we consider reportable conditions under the standards established by the American Institute of Certified Public Accountants. 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.

1. Biospherics billed the Corporation for some types of costs as "standard costs." It did not document in writing the calculation of the standard costs or support the reasonableness of the rates used by periodic comparisons to actual costs. The contract requires other direct costs to be billed as actual costs.

**Recommendation:** We recommend that the Corporation direct Biospherics to revise its policies and procedures for determining standard costs to be in compliance with CAS 407.

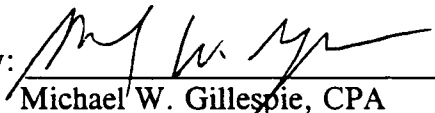
2. Biospherics does not have adequate timekeeping procedures. Sound internal controls dictate that, at a minimum, employees and supervisors mark through and initial timesheet changes. Biospherics employees used correction fluid to alter timesheets, and employees and supervisors did not initial all changes.

**Recommendation.** We recommend that the Corporation direct Biospherics to require employees and supervisors to initial all timesheet corrections and prohibit the use of correction fluid.

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 may occur 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 the American Institute of Certified Public Accountants. We believe, however, the first matter described above is a material weakness.

This report is intended for the use of the Inspector General and Corporation management. This report is a matter of public record, and its distribution is not limited.

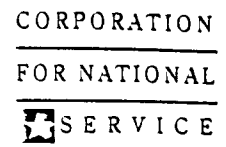
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By:   
Michael W. Gillespie, CPA

**APPENDIX**

**THE CORPORATION'S RESPONSE**

MEMORANDUM



DATE: April 21, 1999

TO: Luise Jordan, OIG  
*Simon G. Woodard*

FROM: Simon G. Woodard, Director, Procurement Services

CC: Wendy Zenker, COO  
Wilsie Minor, Assistant General Counsel

SUBJECT: OIG Report 99-09, Draft Audit of Contract No. 95-743-1009 with Biospherics, Inc.

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The subject draft report cites conditions and deficiencies pertaining to the performance of Biospherics, Inc under Contract No. 95-743-1009. We have reviewed the draft report and do not have specific comments at this time. We will address the findings and recommendations in the final management decision.

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Getting Things Done.  
AmeriCorps, National Service  
Learn and Serve America  
National Senior Service Corps