



National Science Foundation

4201 Wilson Boulevard
Arlington, Virginia 22230

Office of Inspector General

MEMORANDUM

DATE: 12/19/2006

TO: David Elizalde, Director
Division of Acquisition and Cooperative Support (DACS)

FROM: Deborah H. Cureton
Associate Inspector General for Audit

SUBJECT: NSF OIG Audit Report No. 07-1-004, Review of Raytheon Polar Services Company's Cost Accounting Standards Board Disclosure Statement

In response to your request for audit support of the Raytheon Polar Services Company (RPSC) Fiscal Year (FY) 2000 to 2004 incurred cost proposal submission of costs claimed under NSF Contract No. DACS-OPP-0000373, we have coordinated a series of audits to be performed by the Defense Contract Audit Agency (DCAA), Herndon Branch Office. Attached is the final audit report "revised"¹ dated October 20, 2006, on the adequacy of RPSC's Cost Accounting Standards Board (CASB) Disclosure Statement submitted on April 17, 2006, with a proposed effective date of January 1, 2005. The objectives of the audit were to:

- Examine the RPSC Disclosure Statement to determine whether it adequately describes RPSC's cost accounting practices² and is consistent with RPSC's actual practices;
- Examine the disclosed practices to determine whether the practices comply with applicable Cost Accounting Standards (CAS) and Federal Acquisition Regulations (FAR), Part 31; and
- Evaluate the cost impact of the changes in accounting practice in order to describe, categorize, and negotiate with RPSC the cost impact of the changes.³

RPSC has to date not submitted the associated cost impact proposal required by federal regulations for any change in cost accounting practice. When accounting changes meet both

¹ DCAA revised its report to update the Organization and Systems Section of the initial audit report related to the status of outstanding CAS noncompliances.

² A Disclosure Statement is adequate if it is current, accurate, and complete in accordance with FAR 30.202-7(a).

³ This Disclosure Statement describes changes in disclosed and established cost accounting practices which RPSC proposes to use in the performance of the USAP contract.

tests of adequacy and compliance, as prescribed in FAR 30.602, DCMA is required to request that RPSC submit a cost impact proposal that identifies the cost impact of the changes on the NSF contract.

Due to the significant inadequacies found in RPSC's descriptions of its accounting practices, DCAA was unable to perform the compliance portion of the audit or to identify the resulting cost impact. Except for this qualification, the DCAA audit was performed in accordance with generally accepted government auditing standards.

Background Information

Previously we reported to your office⁴ that RPSC did not comply with CAS 418, which requires that RPSC consistently classify costs on the (USAP) contract as stated in its CASB Disclosure Statement. RPSC was included in the Disclosure Statement of its parent company, Raytheon Technical Services Company (RTSC). Since the inception of the USAP contract through December 31, 2004 (five years), RPSC did not comply with RTSC's disclosed accounting practices for distinguishing direct costs from indirect costs. This resulted in RPSC improperly claiming indirect costs as direct costs totaling [REDACTED] ([REDACTED] for Fiscal Years (FYs) 2000 through 2002, and [REDACTED] for FYs 2003 and 2004) in its incurred cost submissions for these five years. On August 22, 2006, the Defense Contract Management Agency (DCMA) issued a final determination of RPSC's noncompliance with CAS 418 and its disclosed accounting practices to RTSC for the three-year period ending December 31, 2002.

Effective January 1, 2005, Raytheon removed RPSC from RTSC's CASB Disclosure Statement. This left RPSC performing the USAP contract without any CASB Disclosure Statement to describe its cost accounting practices, contrary to FAR and the USAP contract. DCAA issued an audit report citing this additional noncompliance on November 18, 2005.⁵ Also, on April 5, 2006, DCMA cited RTSC with an initial finding of noncompliance with CASB 9903.202-1, Disclosure Statement General Requirements for failing to disclose the cost accounting practices of RPSC in a CASB Disclosure Statement.

In response, Raytheon submitted on April 17, 2006, an "initial" CASB Disclosure Statement for RPSC, retroactively effective to January 1, 2005. While this Disclosure Statement is new for RPSC as a separate organizational unit of RTSC, it functions as a revised (not an initial) Disclosure Statement for the USAP contract. This is because under FAR, a contract, as opposed to an organizational unit of an entity, is subject to Federal Cost Accounting Standards. Therefore, since the USAP contract is a fully CAS-covered contract, the April 17, 2006 Disclosure Statement, if accepted, will result in increased costs to NSF by changing the terms and conditions under which RPSC will bill costs under the contract. The proposed change we

⁴ Reference NSF OIG Audit Report No. 06-1-001, dated March 21, 2006, "Audit of Raytheon Polar Services Company's Noncompliance with Cost Accounting Standard 418, Allocation of Direct and Indirect Costs for Fiscal Years 2000 to 2002."

⁵ Reference NSF OIG Audit Report No. 06-1-011, "RPSC's Failure to File Required Cost Accounting Disclosure Statement," dated July 6, 2006.

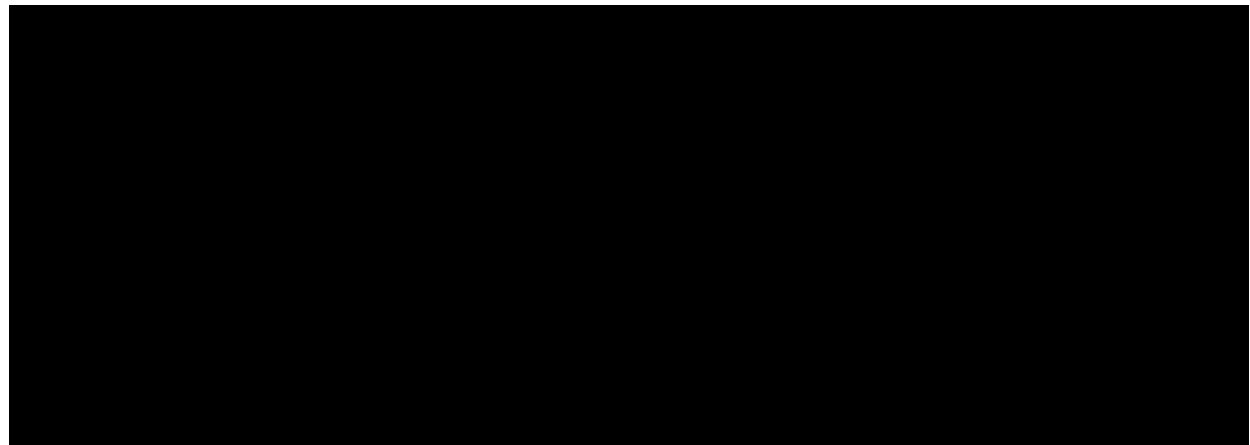
are most concerned about is that certain [REDACTED] previously disclosed as indirect costs⁶ are now disclosed as direct costs.

While this change will allow RTSC to correct its noncompliance with CAS 418 and its prior disclosed accounting practices, it will also allow RPSC to charge certain locally incurred indirect costs that were previously subject to ceiling caps and not allowable. These [REDACTED] approximate [REDACTED] of the [REDACTED], or [REDACTED], of the improperly claimed indirect costs discussed in prior audit reports. Under the new Disclosure Statement, these [REDACTED] will now be allowable as direct costs for the remaining five years of the USAP contract.

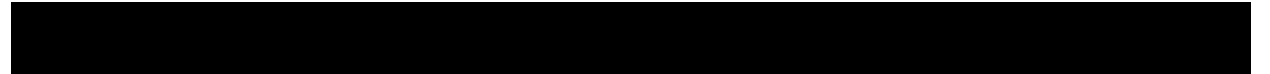
Because RPSC has not provided any cost impact proposal for its change in disclosed accounting practice, and to ensure NSF and the National Science Board are aware of, and have a clear understanding of, the amount of increased costs that will result from this change to the USAP contract, we have requested DCAA to provide an estimate of the amount of resulting increased costs from January 1, 2005 until the anticipated completion of the USAP contract. We will transmit DCAA's estimate of increased costs to NSF upon our receipt and review.

Results of Audit

In the attached report, DCAA found that the RPSC Disclosure Statement does not adequately describe the contractor's cost accounting practices. DCAA identified numerous inadequacies and made recommendations to RPSC to correct each deficiency and submit a revised Disclosure Statement. Specifically, DCAA found that RPSC's Disclosure Statement did not adequately describe how RPSC:



⁶ Prior to contract award, RTSC certified on the cover sheet of its proposal that it had submitted a CASB Disclosure Statement, and that no aspect of its proposal was inconsistent with its disclosed practices, as set forth in its Disclosure Statement that was on file with the Government at that time. This Disclosure Statement cited these [REDACTED]



DCAA also noted that a matrix identifying the various methods that costs are allocated to service center and expense pool allocation bases was omitted from the Disclosure Statement. The contractor concurred with the changes DCAA recommended that RPSC make to its Disclosure Statement and agreed to submit a revised Disclosure Statement by November 1, 2006, to address the noted deficiencies. As of December 13, 2006, however, RPSC still had not provided DCAA with its revised Disclosure Statement.

Upon receipt of the revised Disclosure Statement, DCAA will complete its audit of the adequacy of the Disclosure Statement. When the Disclosure Statement is deemed adequate, DCAA will conduct its audit of compliance. When the Disclosure Statement is both adequate and compliant, DCAA will evaluate the cost impact of the changes in accounting practice upon receipt of RPSC's cost impact proposal.

We recommend that NSF continue to coordinate with and allow DCMA to take the lead in 1) obtaining the revised RPSC Disclosure Statement and determining if the revised Disclosure Statement adequately describes RPSC's cost accounting practices and complies with CAS and FAR, and 2) requesting submission of a cost impact proposal and evaluating the cost impact of the changes in accounting practice from the time of the changes (January 1, 2005) until the anticipated completion of the USAP contract. After receipt of this information, it will then be necessary for NSF to assess the desirability of the change in disclosed accounting practice in light of the resulting increased costs, and, if determined desirable, negotiate a modification of the USAP contract with RPSC.

We consider the issues in the DCAA audit report to be significant. Accordingly, to help ensure that the findings are resolved within six months of issuance of the audit report, please coordinate with our office during the resolution period to develop a mutually agreeable audit resolution memorandum.

We also want to bring to your attention that DCAA has briefly discussed the results of several other audits performed at RTSC or Raytheon Corporate Headquarters beginning on page 9 of the attached DCAA report. Many of the reports have information that may be useful to NSF in administering its USAP contract with RPSC. If NSF desires a copy of any of the referenced DCAA reports, please contact Kenneth Stagner at (303) 312-7655 or David Willems at (703) 292-4979.

We are providing a copy of this memorandum to the Director of the Office of Polar Programs. However, since the responsibility for audit resolution rests with DACS, we ask that no action be taken concerning the report's findings without first consulting DACS at (703) 292-8242. In addition, DCAA did not include DCMA in its distribution list for the attached audit report. Therefore, we provided a copy of the DCAA audit report to DCMA.

OIG Oversight of Audit

To fulfill our responsibilities under Generally Accepted Government Auditing Standards, the Office of Inspector General:

- reviewed the audit report prepared by DCAA to ensure compliance with Generally Accepted Government Auditing Standards and Office of Management and Budget Circulars; and
- coordinated issuance of the audit report to NSF.

DCAA is responsible for the attached auditor's report on RPSC and the conclusions expressed in the report. The NSF OIG does not express any opinion on the conclusions presented in DCAA's audit report.

We thank your staff for the assistance that was extended to us during the audit. If you have any questions about this report, please contact David Willems or Jannifer Jenkins at (703) 292-4996.

Attachment: DCAA Report No. 6161-2006P19100001 "Revised" dated October 20, 2006, "Report on Adequacy and Compliance of RPSC Initial Disclosure Statement Dated January 1, 2005."

cc: Thomas Cooley, Director, BFA
Mary Santonastasso, Director, DIAS
Karl Erb, Director, OPP



DEFENSE CONTRACT AUDIT AGENCY
AUDIT REPORT NO. 6161-2006P19100001
“Revised”



October 20, 2006

PREPARED FOR: National Science Foundation
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 Associate Inspector General for Audit
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 Arlington, VA 22230

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 E-mail Address dcaa-fao6161@dcaa.mil

SUBJECT: Report on Adequacy and Compliance of RPSC Initial Disclosure
 Statement Dated January 1, 2005

CONTRACTOR: Raytheon Polar Services Company (Cage Code No. 3NYQ8)
 Raytheon Technical Services Company
 12160 Sunrise Valley Drive
 Reston, VA 20191

REPORT RELEASE RESTRICTIONS: See Page 28

	<u>Page</u>
CONTENTS: Subject of Audit	1
Scope of Audit	1
Results of Audit	2
Contractor Organization and Systems	9
DCAA Personnel and Report Authorization	28
Audit Report Distribution and Restrictions	29
Appendices	30



Audit Report No. 6161-2006P19100001 “Revised”

SUBJECT OF AUDIT

This purpose of this revised report is to correct wording in the initial audit report and to update the Organization and Systems section of the initial audit report related to the status of outstanding CAS noncompliances.

In response to your August 2, 2006 request, we examined Polar Services’ initial disclosure statement, dated January 1, 2005 to determine if the disclosed practices are adequate and are in compliance with CAS. By submitting its CAS disclosure statement, RPSC asserts that the disclosure statement adequately describes its cost accounting practices, and the disclosed practices comply with Cost Accounting Standards Board rules, regulations, and standards contained in 48 C.F.R. Chapter 99. The purpose of our examination was to evaluate whether the subject disclosure statement adequately describes the cost accounting practices which the contractor proposes to use in the performance of contracts covered by 48 C.F.R. Chapter 99 and to determine whether the disclosed practices described in the RPSC disclosure statement dated January 1, 2005 comply with applicable Cost Accounting Standards and FAR Part 31.

The contractor is responsible for the adequacy of the disclosure statement and compliance of the disclosed accounting practices with applicable cost accounting practices and FAR Part 31. Our responsibility is to express an opinion on the adequacy of the disclosure statement and whether the disclosed accounting practices comply with those requirements based on our examination.

SCOPE OF AUDIT

Except for the qualifications discussed below, we conducted our examination in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the examination to obtain reasonable assurance about whether the contractor’s disclosure statement adequately describes its cost accounting practices. An examination includes:

- evaluating the contractor's internal controls, assessing control risk, and determining the extent of audit testing needed based on the control risk assessment;
- examining, on a test basis, evidence supporting the adequacy of the disclosure statement; and;
- evaluating the overall disclosure statement presentation.



Audit Report No. 6161-2006P19100001 “Revised”

We evaluated the subject disclosure statement using applicable requirements contained in the:

- Federal Acquisition Regulation (FAR); and
- CAS Board rules, regulations and standards.

We evaluated the Indirect and Other Direct Cost System of internal controls at Raytheon Polar Services in Audit Report No. 6161-2004T14980202 Dated December 15, 2005 and determined that RPSC lacked certain control procedures to ensure that indirect and other direct costs, which are proposed, claimed and billed to the U.S. Government, are compliant with applicable laws and regulations and are properly assigned to cost objectives. We determined that the RTSC Indirect and Other Direct Cost System is inadequate in-part.

The scope of our examination reflects our assessment of control risk and includes audit tests designed to provide a reasonable basis for our opinion. Our examination does not provide a legal determination on RPSC compliance with the specified requirements.

QUALIFICATIONS:

As a result of the significant inadequacies, we were unable to appropriately perform the compliance portion of this review or provide the resulting cost impact as requested. We recommend that the contractor submit a revised disclosure statement to address the inadequacies so that a review for compliance can be performed in the near future.

RESULTS OF AUDIT

This revised report corrects wording in our initial audit report and updates the Organization and Systems section of the initial audit report related to the status of outstanding CAS noncompliances.

Our initial audit report has been reissued in its entirety.

In our opinion, the subject disclosure statement does not adequately describe the contractor’s cost accounting practices. Accordingly, we recommend the contractor submit a revised disclosure statement.

This examination was limited to evaluating the adequacy of accounting practice descriptions in the subject disclosure statement. Accordingly, we express no opinion on whether the disclosed practices are proper, approved, or agreed to for pricing proposals, accumulating costs, or reporting contract performance data.

Audit Report No. 6161-2006P19100001 "Revised"

We provided a memorandum to the contractor's representative on September 18, 2006 describing the disclosure statement inadequacies. The contractor's representative, [REDACTED] stated that a formal exit conference was not necessary and that the memorandum describing the inadequacies would be sufficient. The contractor agreed to provide an adequate disclosure statement no later than November 1, 2006. The complete text of the contractor's response appears in the appendix to this report.

We identified the following inadequacies in the contractor's disclosure statement:

[REDACTED]

Condition:

RPSC provides as a contract requirement, wine and liquor as well as various other typically unallowable items to the Antarctic as part of the re-supply of retail and drinking establishments. Since these MWR type items are part of the normal support operations, the contractor feels that the expressly unallowable items are allowable since they are required by the contract. The contractor's opinion on this matter was expressed in a written response to the FY 2003 Incurred Cost Audit Assignment No. 6161-2003P10100201. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Pages 4-7 have been redacted in their entirety.

Audit Report No. 6161-2006P19100001 “Revised”

This recommendation does not assume compliance with CAS 405 or FAR Part 31.205. An assessment of compliance will be performed after the disclosure statement has been deemed adequate.

CONTRACTOR ORGANIZATION AND SYSTEMS

I. Organization

RTSC Headquarters is located in Reston, VA. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

RTSC has a multi-disciplined workforce of approximately 10,000 employees. RTSC provides technical, scientific, and professional services to defense, federal, and commercial customers on all seven continents, including support for operations in space, at sea, and on land. RTSC had annual sales of approximately [REDACTED] in FY 2005, of which approximately [REDACTED] are primarily government prime contracts and subcontracts. Of the government contracts and subcontracts, approximately [REDACTED] are flexibly priced (i.e. cost type and time and materials (T&M) type).

[REDACTED]

Pages 10-27 have been redacted in their entirety.

Audit Report No. 6161-2006P19100001 "Revised"

DCAA PERSONNEL

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General information on audit matters is available at <http://www.dcaa.mil/>.

RELEVANT DATES

Request for Audit: NSF OIG – dated August 02, 2006; received August 04, 2006

AUDIT REPORT AUTHORIZED BY:

/Signed/

LARRY TATEM
Branch Manager
DCAA Herndon Branch Office

Audit Report No. 6161-2006P19100001 “Revised”

AUDIT REPORT DISTRIBUTION AND RESTRICTIONS

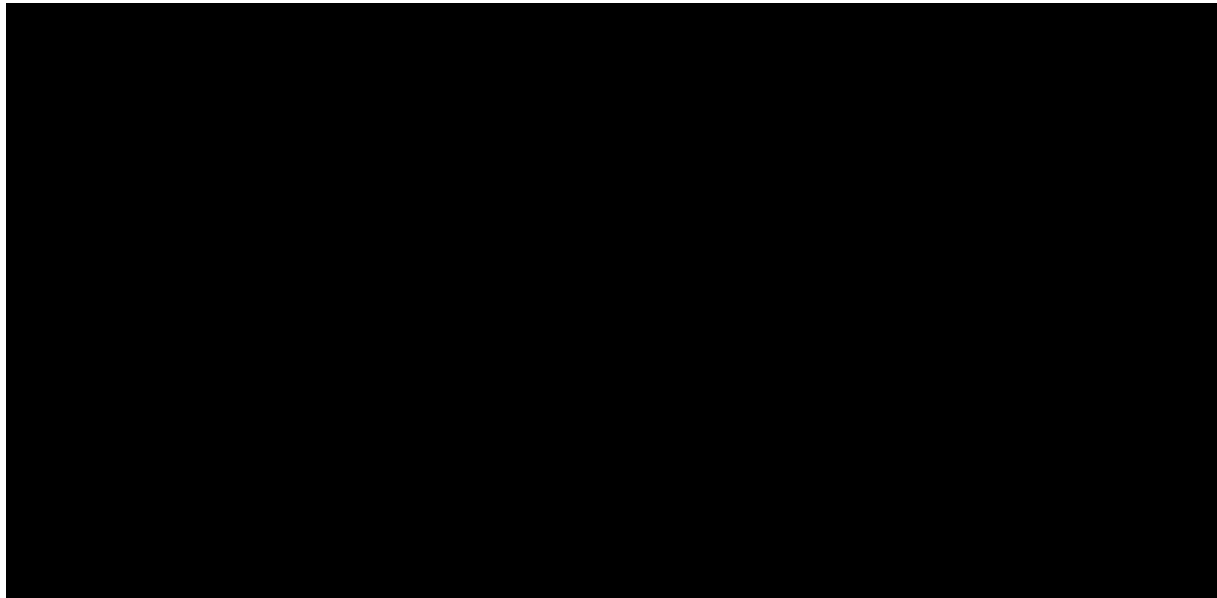
DISTRIBUTION

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Reston, VA 20191
(Copy furnished thru NSF ACO)

RESTRICTIONS



APPENDIX

Contractor's Response dated October 4, 2006.

Memorandum

Date	4 October 2006	Memo number	[REDACTED]
To	Larry Tatem	From	[REDACTED]
Organization	DCAA	Organization	RTSC Finance
Subject	Polar Services Disclosure Statement - Adequacy review	Classification	
Distribution	See Below	Job number	
		File number	

Reference: DCAA draft audit report 06-02L-008, 6161-2006P19100001 dated September 18, 2006

The referenced audit report identified several inadequacies in the Polar Services Disclosure Statement and provided recommendations on enhancements to the document to provide further clarity and detail of RTSC Polar disclosed practices. RTSC has reviewed DCAA's recommendations and concurs that the recommended changes are accurate and will improve the quality of the document. RTSC will submit a revised Disclosure Statement no later than 1 November 2006 to address the items noted in the DCAA audit report.

Please contact me at your convenience if you have any further questions regarding this correspondence.

[REDACTED]
RTSC Business Governance

CC: Andrea Leimer (DCAA)
[REDACTED] (RTSC)
[REDACTED] (RTSC)
[REDACTED] (RTSC)