



## Why We Did The Audit

In fulfilling its responsibilities as receiver for failed FDIC-insured financial institutions, the FDIC retains electronically stored institution information and documentation to meet its fiduciary requirements, resolve legal issues, and provide ongoing customer service. To accommodate the enormous data conversion and storage demands associated with the large number of institution failures in recent years, the FDIC entered into a contract (the Contract) with Lockheed Martin Services, Inc. (Lockheed) for data management services. The Contract requires Lockheed to provide the FDIC with a standard method of maintaining failed institution data, including secure data migration, conversion, cataloging, indexing, storage, security, and retrieval.

In view of the significance of the Contract, the Office of Inspector General (OIG) engaged Reed & Associates, CPAs, Inc. (Reed) to conduct a performance audit of Lockheed's invoices. The performance audit objective was to determine whether charges paid by the FDIC to Lockheed were adequately supported, allowable under the terms and conditions of the contract, and reasonable. The audit covered payments made during the period November 1, 2008 through May 31, 2011. The audit also included an assessment of compliance with a provision in the Contract requiring Lockheed, its employees, and its subcontractor employees to execute confidentiality agreements with the FDIC to mitigate the risk of unauthorized disclosure of sensitive information.

## Background

The FDIC procures services under the Contract through task orders that may be awarded on either a firm fixed price or time and materials basis. Under firm fixed price task orders, the FDIC pays Lockheed an agreed-upon amount or service rate for satisfactory performance that covers the contractor's costs and expenses (direct and indirect) as well as any profit, fees, or markups. The FDIC awards firm fixed price task orders to procure such things as data storage and data center maintenance and system monitoring and reporting. Under time and materials task orders, the FDIC compensates Lockheed for actual productive work at the hourly rates specified in the Contract; reimburses Lockheed for necessary travel and per diem expenses that do not exceed the limitations in the *FDIC Contractor Travel Reimbursement Guidelines*; and pays reasonable amounts for materials that Lockheed has been invoiced. The FDIC awards time and materials task orders to procure such services as the capture and migration of data from failed institutions to Lockheed's data center and the imaging and indexing of hardcopy documents. When appropriate, Lockheed uses credit invoices to reimburse the FDIC for overcharges that are identified during the firm's internal reviews and reconciliations of labor, travel, materials, and other charges.

The Contract, which became effective on November 1, 2008, has an initial 3-year base period of performance and two 2-year option periods, for a total potential period of performance of 7 years. As of May 31, 2011, the FDIC had awarded 78 task orders with a total value of \$327,872,811 under the Contract. As of the same date, the FDIC had paid 8,902 invoices totaling \$158,352,966. The Contract has no ceiling price.

## Audit Results

Except as described below, charges paid to Lockheed that Reed reviewed were adequately supported, allowable under the terms and conditions of the Contract, and reasonable. Specifically, all \$8,310,150 of the firm fixed price costs reviewed were adequately supported, consistent with the rates approved in the Contract, and reasonable. Accordingly, Reed did not question any firm fixed price costs. In addition,

Reed did not question any of the \$121,476 in credits that it reviewed. However, Reed did identify a total of \$740,784 in questioned costs pertaining to other categories of reviewed charges. We will include these questioned costs in our next *Semiannual Report to the Congress*. The amount ultimately disallowed by the FDIC could change based on final management decisions after evaluating the findings and recommendations included in the report. In summary, Reed questioned:

- \$140,079 (or about 2 percent) of the \$7,020,304 in time and materials costs reviewed. These questioned costs consisted of \$29,731 in labor, \$102,496 in travel, and \$7,852 in materials. Of the total amount questioned, \$137,958 was unsupported.
- \$123,014 in costs resulting from the misclassification of a subcontractor employee's labor category. Lockheed identified this misclassification in November 2010, but as of the end of our fieldwork, the FDIC had not been reimbursed for the overcharge.
- \$477,691 in unallowable indirect costs that Lockheed applied to travel expenses. Although Lockheed agreed in February 2011 to process a credit for this amount against future invoices submitted under the Contract, the credit had not been processed as of the end of our fieldwork.

Using statistical sampling techniques, Reed estimated that there is a 90-percent probability that the amount of questioned costs billed to the FDIC under the Contract's time and materials task orders through May 31, 2011 is not less than \$583,390. This estimated amount does not include questioned costs for the labor category misclassification or the indirect costs on travel because the underlying causes were isolated matters. The report does not recommend that the FDIC disallow this amount, and we do not plan to recognize the amount as a questioned cost in our *Semiannual Report to the Congress*. Instead, the estimated amount is an indication of the potential payment risk under the Contract that the FDIC should consider as part of its ongoing contract administration and oversight management activities.

Further, confidentiality agreements were not consistently executed and maintained for contractor and subcontractor employees assigned to the Contract. Finally, the report includes an observation pertaining to the FDIC's oversight management of the Contract.

## **Recommendations and Corporation Comments**

The report contains a total of six recommendations. Three of the recommendations are aimed at recovering unallowable and unsupported questioned costs that were charged by Lockheed and paid under the Contract. The remaining three recommendations are intended to enhance the FDIC's contract administration and oversight management controls and practices.

FDIC management provided a written response, dated September 25, 2012, to a draft of the report. In the response, management concurred with all six of the report's recommendations, described completed and planned corrective actions to address each recommendation, and noted that action had been taken to address the report's observation on the FDIC's oversight management of the Contract. Further, relevant portions of the draft report were provided to Lockheed for its review and informal comment. The OIG and Reed considered Lockheed's informal comments before the report was finalized.

Because this report contains sensitive information, we do not intend to make the report available to the public in its entirety. We will, however, post this Executive Summary on our public Web site.