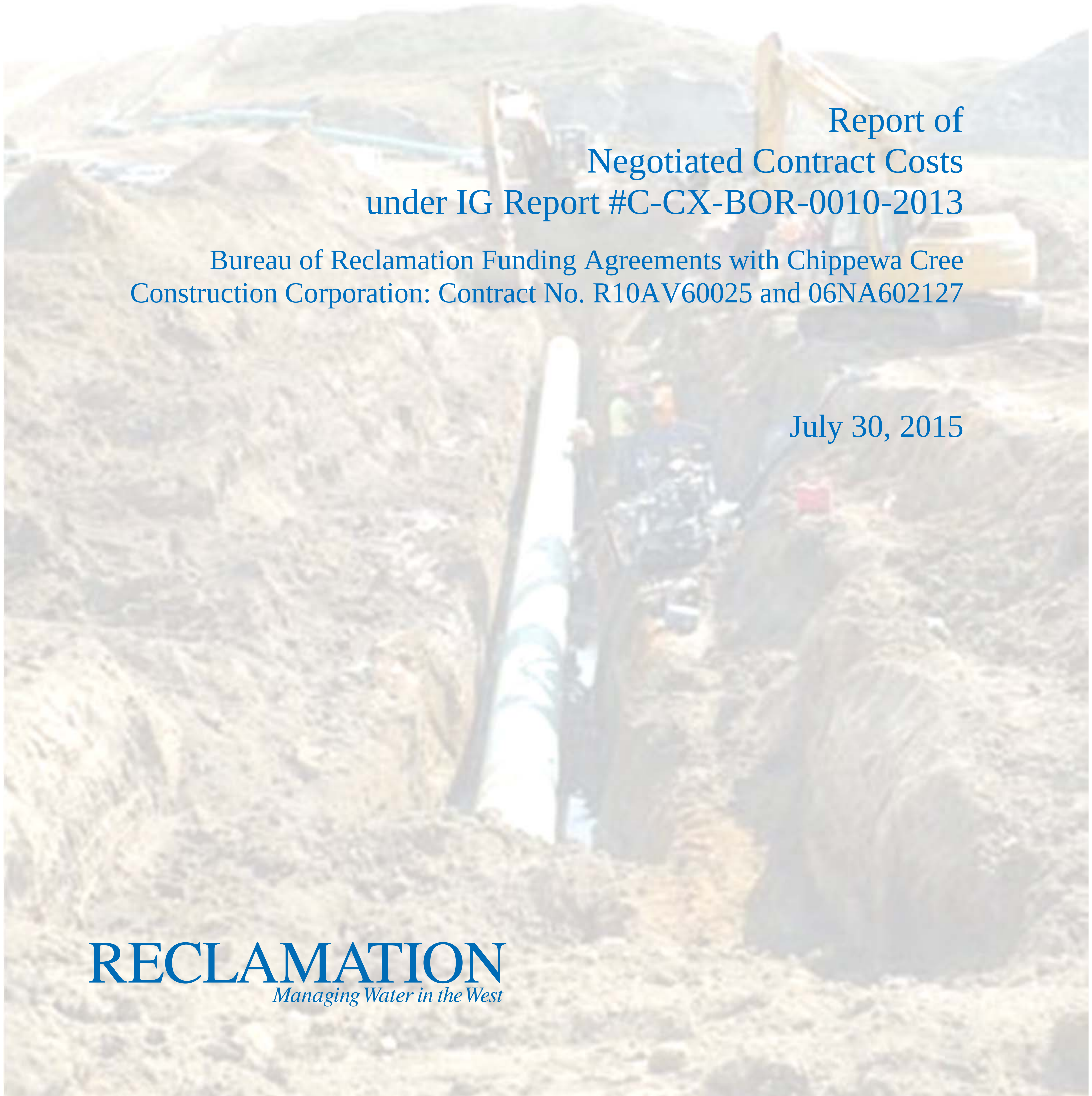
Report of
Negotiated Contract Costs
under IG Report #C-CX-BOR-0010-2013

Bureau of Reclamation Funding Agreements with Chippewa Cree Construction Corporation: Contract No. R10AV60025 and 06NA602127

July 30, 2015



RECLAMATION
Managing Water in the West

Executive Summary

Recommended resolution of Office of the Inspector General (OIG) Audit dated December 16, 2013, of Chippewa Cree Construction Corporation (Corporation) for the period FY 2006 through FY 2012.

The United States Congress authorized and funded in 2002 the construction of the Rocky Boy's/North Central Montana Regional Water System (Project). The United States Bureau of Reclamation collaborates with the Chippewa Cree Tribe (Tribe) through the Corporation to construct the Project. Mr. Michael J. Ryan, Regional Director of Great Plains Region, is the Awarding Official for the Annual Funding Agreement (AFA) R10AV60025 that provides funding for the Project. In April 2013 Reclamation, in coordination with the Corporation, requested an audit of Project costs. On December 16, 2013, the OIG issued their audit report (number C-CX-BOR-0010-2013) to Mr. Ryan (appendix 1 attached).

In March 2014, Reclamation assembled a negotiation team (Federal Team) to review audit results, collaborate with the Tribal negotiation team to gather additional information, and prepare recommendations for Mr. Ryan's decision regarding fiscal years 2006 through 2012, as identified in the OIG's Audit. Throughout the course of the review, the Reclamation Federal Team kept in mind the spirit and intent of P.L. 93-638 as a guiding principle.

The OIG report divided audited costs into three categories: Direct Costs, Profit, and Tribal Employment Rights Ordinance (TERO). Many of the OIG's questioned costs were transactions that benefitted other construction projects going on at the same time as the Project and should have been allocated to all beneficiaries, not just to the Project. The Corporation proposed a methodology for allocating costs in this category by using a ratio of revenue recognized by the Project to total revenue earned by the Corporation. This calculation is 62% cost allowed and 38% disallowed. Reclamation agreed to this methodology and made the following recommendations using the proposed methodology:

	OIG	Reclamation Recommendations		
	Questioned/Ineligible Costs	Allocated Costs*	Allow Costs	Disallow Costs
Direct Costs	$ 8,074,010	$3,142,157	$6,144,974 6,618,073	$1,929,036 1,455,937
Profit Indirect/Admin	2,580,414	$ 0	$ 0 1,085,000	$2,580,414 1,495,414
TERO	2,260,121	$ 0	$2,055,436 2,126,012	$ 204,685 134,109
Total	$12,914,545		$9,829,085	$3,085,460

*Provided for information purposes only; Add the "Allow Costs" and "Disallow Costs" columns which equal the "OIG" Column

NOTE: Numbers in Blue are from the 8/14/2014 Draft Recommendation Report
Numbers in Yellow are the FINAL Amounts

The OIG divided Direct Costs into five categories: Direct Labor, Direct Materials, Equipment Rental, Equipment Purchased, and Other Direct Costs. Reclamation merged the two equipment categories during their analysis, due to similar treatment methods under the applicable guidance.

	OIG	Reclamation Recommendations		
	Questioned/Ineligible Costs	Allocated Costs*	Allow Costs	Disallow Costs
Direct Labor	$3,178,185	$1,345,495	$2,467,805 2,940,904	$ 710,380 237,281
Direct Materials	1,946,297	0	1,651,466 1,651,466	294,831 294,831
Equipment	2,408,420	1,795,486	1,960,042 1,960,042	448,378 448,378
Other Direct Costs	541,108	1,176	65,661 65,661	475,447 475,447
Total	$8,074,010		$6,618,073	$1,455,937

*Provided for information purposes only; Add the "Allow Costs" and "Disallow Costs" columns which equal the "OIG" Column

NOTE: Numbers in Blue are from the 8/14/2014 Draft Recommendation Report
Numbers in Yellow are the FINAL Amount

Direct Labor disallowance recommendations consisted primarily of the portion of salaries allocable to other than Reclamation projects. The Tribe's methodology for estimating the allocation among various projects of the Tribe was based on revenue recognition for the period 2006-2012. Reclamation concurred with the methodology for calculating the estimate. The remaining disallowed costs under Direct Labor were attributed to non-Reclamation projects, benefits not associated with any Corporation employee, and equipment operation costs captured in a use rate, explained in the Equipment section, below.

Direct Materials disallowances were all from equipment and vehicle operation and maintenance costs covered by the equipment use rate and are explained in the Equipment section, below.

Equipment based on daily reports, photographs and other documents provided by the Tribe, the Reclamation team identified equipment used on the project. In April 2014, the Army Corps of Engineers (USACE) published "Construction Equipment Ownership and Operating Expense Schedule" Vol. 4 which established equipment ownership and operating expense rates for construction equipment by region of the country; Montana is in region IV. The hourly rate is the sum of ownership (i.e. depreciation) and operation costs (i.e. fuel, filters, oil/grease, repairs, tires). By applying these USACE's equipment use rates, Reclamation calculated $1.795 million as allowable equipment costs to the Project. An additional $164,600 in equipment purchases was allowed as unique to the type of construction associated with this project.

Other Direct Cost disallowance recommendation consisted of costs related to donations/payments to the local college and training not associated with work performed on the Project by employees.

<u>Profit</u> absent language in the AFA identifying it as a fixed price contract, Reclamation does not have authority to pay profit on the Project. During the course of the review, the Tribal team stated that this category of costs was actually indirect costs. The Tribal Team proposed that we base allowable indirect cost on current tracking since the accounting is more accurate for 2015. The estimated indirect/administrative costs total $250,000 annually and applying 62% for Reclamation's portion yields $155,000. Extended over a seven (7) year period, this results in $1,085,000. The Federal Team agreed with this approach.

<u>TERO</u>, the Tribe's original ordinance was updated during the review to authorize the application of TERO on the Corporation's costs whether on or off the reservation. The TERO rate was 3% from 11/2005 through 5/2010 and 5% from 6/2010 to present. The disallowed costs from the other categories were separated into the two timeframes and the applicable rate was applied to determine the amount of TERO to disallow.

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Direct Labor

Ineligible and Unsupported Costs
Contract Audit Numbers R10AV60025 and 06NA602127
Direct Labor Category

Summary Recommendation:

		Allocation	Allowed	Disallowed
Allocate	$1,345,495			
	Allocate/Allow	$1,142,305	$1,142,305	
	Allocate/Disallow	$203,190		$203,190
Allow	$1,798,599		$1,798,599	
Disallow	$34,091			$34,091
Audit Total	$3,178,185			
Total Costs			$2,940,904	$237,281
Total Costs per the 8/14/14 Report			2,467,805	710,380

Discussion:

1. Disallowed costs were composed of: diesel fuel and truck repairs covered under equipment use rate computations ($20,000) and unassigned 401K contributions ($14,000).

2. Allocated costs primarily resulted from the salary and benefits for the Corporation's Chief Executive Officer (CEO) and Chief Financial Officer (CFO). Costs falling into this category amounted to $1,315,800 per the records provided to the OIG and used in this analysis.

   The remainder of allocated costs was composed of: travel and reimbursable expenses of CEO as contractor ($7,800) and accrued leave and fringe benefits journal entries ($21,900).

   These costs should be allocated between the Project, and other construction projects that the Corporation had on-going at the time. Per Tribal computations, this split should be 62% (rural water) and 38% (other).

3. The Tribe proposed that the gross salary for the CEO (Tony Belcourt) and the CFO (Violet Eagleman) be used in determining what to allocate to the Project. Records provided to the OIG only reflected the salary that Belcourt and Eagleman charged to the rural water project. The Tribe also proposed that Belcourt's allocation be 77% because he spent more time on the rural water project than the 62% already approved for the allocation. The Tribe contends that Belcourt hired project managers for the other projects the Tribe was constructing so that Belcourt could focus on the Project. The Federal Team agreed to this proposal. The Tribe provided a spreadsheet reflecting Belcourt and

Eagleman's gross salary as follows:

Belcourt: $948,854 and 77% equals	$730,617
Eagleman: $634,321 and 62% equals	393,279
Other costs allocated: $29,691 and 62% equals	18,408
Total Allocated Costs Allowed	$1,142,305

Direct Materials

Ineligible and Unsupported Costs
Contract Audit Numbers R10AV60025 and 06NA602127
Direct Material Costs Category

Summary Recommendation:

		Allowed	Disallowed
Allow	$1,651,466	$1,651,466	
Disallow	$294,831		$294,831
Audit Total	$1,946,297		
Total Costs		$1,651,466	$294,831

Discussion:

1. After an evaluation of the equipment used on the Project, the Corporation is being allowed a use rate developed by the USACE for equipment used on the project. The use rate includes operation and maintenance, which includes: fuel, tires and repairs. The following costs are disallowed under Direct Materials:

Diesel fuel and gasoline:	
Best Oil Distribution	$216,493.67
Ezzie's Wholesale Inc.	57,801.27
Replace Engine in 2010 GMS 1 Ton:	
Tillman's	10,304.16
Tires	
Tire Factory	10,232.00
Total Disallowed	$294,831.10

2. The OIG also classified all transactions totaling $875,000 with MT Waterworks for pipe purchases as ineligible costs since the transactions were deemed to not be at arms-length. At the time of these transactions the CEO of the Corporation was the majority owner of MT Waterworks.

   The Federal Team considered additional documentation that compared prices from competitors and prices charged to other customers of MT Waterworks to determine that the charges MT Waterworks applied to purchases to the Corporation were reasonable. The Federal Team also considered the fact that the pipe, valves, etc. were installed on the Project and will benefit the Project. Thus, those costs are allowed.

Equipment – Purchased and Rental

Ineligible and Unsupported Costs
Contract Audit Numbers R10AV60025 and 06NA602127
Equipment Rental and Equipment Purchase Categories

<u>Summary Recommendation:</u>

Allow	$164,556
Disallow	$448,378
Use Rate Allocation	$1,795,486
Total Costs	$2,408,420

Total Costs Allowed: $1,960,042

<u>Discussion:</u>

Due to the commonality of the required treatment of equipment per OMB Circular A-87, these two categories of questioned costs have been combined.

The majority of questioned costs under the equipment rental category are actually capitalized leases. From review of the documentation and the accounting treatment of these rentals by the Corporation, it appears that the Corporation would enter into long-term rentals of heavy equipment, monthly leases that resulted in year-round leases of equipment. From the documentation provided, the Corporation charged the full amount of the rental cost for each capitalized lease which resulted in costs substantially higher than what is allowed by the OMB Cost Principles [see 2 CFR 225, Cost Principles for State, Local, and Indian Tribal Governments (OMB Circular A-87). Appendix B, Section 37, Rental Costs of Buildings and Equipment]. Further, the Corporation indicated during discussions that during the time period in question, the Corporation did not ensure Use Logs were maintained for each piece of equipment to track actual hours used and for what project. In the negotiated AFA budgets, the Corporation indicated that they were to spend approximately $30,000 per year on leases and fuel purchases in support of the Project, which is substantially lower than the approximately $3,200,000 in equipment rental, purchase, repairs, and fuel that they actually charged to the Project.

For the equipment purchased category, much of the purchased equipment was either not directly (or in some cases indirectly) allocable to the Project. Further, there were many fleet vehicle purchases that were charged to the Project.

The Federal Team estimated the costs for capitalized equipment used in construction of the Project based upon the annual construction schedules (based in large part on progress reports submitted by the Corporation to Reclamation), documentation of what equipment was used on the project, the USACE's use rates for each piece of equipment, and a maximum use of the equipment of 40 hours per week for hourly rates (which is in accordance with the capitalized leases the Corporation entered into with vendor) and 140 miles round trip (Box Elder, MT, to Tiber, MT, and back) for the fleet mileage rates. This calculation was done for all pieces of equipment charged to the Project and questioned by the OIG or identified with the Project by the Corporation during discussions

In addition to the costs questioned by the OIG and the documentation provided by the Corporation for those questioned costs, the Corporation also provided a list of equipment that was associated with the Project, including items from the depreciation schedule that apparently were not charged to the Project. When developing the use rates, these additional pieces of equipment and fixed assets were included to ensure that the recommendation was thorough and took into consideration all of the documentation the Corporation was able to provide.

In summary, of the questioned costs under both Equipment Rental and Equipment Purchase $2,408,420, applying a liberal use rate methodology for all pieces of equipment that were found allocable to the Project plus, and in a few cases, recommending purchase of fixed assets (including some that were not charged to the Rural Water Project), the Federal Team is recommending the Awarding Official allow $1,960,042. A summary of these calculations is included below. As the use rates already include allocations for fuel usage and repairs, these costs are to be disallowed from questioned costs in the Direct Labor and Direct Materials Categories.

Summary of Discussions and Position of the Tribe:

A draft of this recommendation and supporting work papers was provided to the Tribe on August 14, 2014, for review and comment. Over the course of approximately six (6) months, the Tribe provided two (2) separate analyses and recommendations for the equipment rental and purchase costs.

Tribe’s November 2014 Analysis and Proposal.

The Tribe conducted an alternate analysis and provided it to the Federal Team on November 24, 2014. The Tribe’s proposal used equipment hours developed from payroll charged to the Project and hourly equipment rates provided from a local construction company. The amount of equipment rental and purchase proposed by the Tribe based upon this analysis was $3,957,495. This amount was $1,548,804 higher than the total equipment rental and purchase costs originally charged by the Tribe to the Project.

The Federal Team reviewed the analysis and held a conference call with the Tribe. The accuracy of the payroll records, both in accurately allocating personnel time to the Project versus other construction projects and capturing personnel time operating equipment versus other tasks, was questioned by the Federal Team. In comparison to the progress reports and daily inspection reports, there were times that personnel and equipment were identified as working on other construction projects, but the Tribe’s analysis attributed the payroll and equipment to the Project. Further, the reasonableness of the equipment rates provided by the local construction company were questioned because the rates included operator costs as well as profit and other increments of cost above what is allowable for inclusion in a use rate in accordance with OMB Circular A-87, Appendix B, Section 11. Where the Tribe did not use the USACE rates, the equipment rates identified in the Tribe’s analysis were 25% to 350% higher than the USACE equipment use rates. Based upon the inaccuracy of the source data for the hours and the unreasonable hourly use rates proposed by the Tribe, the Federal Team disagreed with the Tribe's November 2014 analysis and proposal.

Tribe's March 2015 Analysis and Proposal.

The Tribe contracted with their Architecture/Engineering Firm (Advanced Engineering and Environmental Services, Inc. (AE2S)) to develop a second alternative analysis. While the AE2S Technical Memorandum states that the analysis was a "third party evaluation," AE2S has been under contract with the Tribe for design and construction management for the Project during the entire period in which the OIG questioned costs associated with the Project. This analysis leveraged the daily and weekly reports prepared by the AE2S Resident Project Representative (RPR) and equipment rates published by www.EquipmentWatch.com in their "Blue Book." The amount of equipment rental and purchase costs proposed by the Tribe, based upon AE2S's analysis, was $5,157,074. This amount was $2,748,654 higher than the total equipment rental and purchase costs originally charged by the Tribe to the Project.

The Federal Team reviewed the analysis and held a conference call with the Tribe. The Federal Team disagreed with the Tribes analysis in the estimated number of standby hours and proposed "Blue Book" equipment rates. It should be noted that the Federal and Tribal Teams agreed that no significant difference in the number of project days per fiscal year were found in either analysis.

For the calculation of estimated hours per piece of equipment, the Tribal Team's analysis included the overall assumption that if the RPR identified the piece of equipment in his/her logs, then that piece of equipment was determined as running 100 percent of the time at 8 hours / day and 40 hours / week. The Federal Team's estimate, while based upon an 8 hour work-day and 40 hour work-week, did not assume 100 percent usage for all pieces of equipment. One hundred percent usage was reserved for only those pieces of equipment that, based upon the nature of the work, could be expected to run 100 percent of the time (or through a combination of multiple pieces of equipment - collectively could be expected to run 100 percent of the time). For example, as the Core Pipeline required at least two (2) excavators running nearly 100 percent of the time (one for excavating the trench and laying the pipe, the other for filling the trench and compaction), the Federal Team's estimate included the 100 percent assumption for two (2) excavators. However, for the front-end loaders, of the five (5) identified in the equipment records, the Federal Team's estimate provided for 100 percent usage of the two (2) largest capacity loaders (which were selected out of the five (5) to confer the highest hourly rate to the Tribe's benefit). As noted below, when compared to the FY2014 actual usage (appropriately tracked via equipment use logs) both of these assumptions were higher than actual usage for similar work. To assume 100 percent usage for all pieces of equipment is simply unreasonable and that approach taken by AE2S analysis contributed, in part, to the increase in estimated equipment cost over the Federal Team's initial recommendation.

In addition to accounting for actual running hours, the Tribe's analysis included "standby" hours. If a piece of equipment was identified as being onsite by the RPR, any hours of operating time not accounted for in the operators timesheets was billed at a reduced standby rate. This led to several pieces of equipment being billed to the Project for many weeks, even months, at the standby rate while the piece of equipment was actually only used on the Project for a minimal amount of time. The time that equipment is not being used is more appropriately classified as "idle," not "standby." Standby time is applicable when, due to circumstances outside the control of the contractor, work stoppage has occurred and the equipment is not able to be run. In these cases, a contractor cannot simply move the equipment to another job as the work could restart at any time. For the purposes of the Project, idle equipment due to the Tribe's decisions regarding project management such as the time equipment sits idle for an extended period because it is not needed should not be billed to the Project.

The equipment rates used in the Tribes analysis are from the Blue Book. The Equipment Watch publishes various equipment information guides, including equipment ownership rates. The ownership rates in the Blue Book contain various cost factors that are very similar to the USACE rates including hourly costs associated with depreciation, cost of facilities capital, overhaul, and fuel. They also include various components that are already reimbursed to the Tribe separately and not included in the USACE rates; including indirect costs, overhaul repair labor, and field labor. If the overhead and labor costs are removed from the Blue Book rates, the Blue Book rates are generally in the same range as to the USACE rates used in the Federal Team's analysis. However, the equipment rates proposed by the Tribe in their analysis are from the Equipment Watch <u>Rental</u> Rate Blue Book *(emphasis added)*. These rates are much higher than the ownership rates. For example, the rate proposed for the Caterpillar D8T by the Tribe was $286.03, but the Blue Book ownership rate is $162.88 (including overhead and other separately reimbursed costs) and the USACE ownership rate is $151.34. The Federal Team disagreed with the approach of applying rental rates, as they include overhead, profit, and other increments above cost that are not allowable in use rates (OMB Circular A-87, Appendix A. Section 11.)

Comparison of Federal Team's Estimate versus Actual, Documented Equipment Usage.

As a result of changes to the AFA terms and conditions as well as better management by the Tribe, the Tribe did employ Use Logs to document equipment usage during construction on the Core Pipeline in fiscal year 2014. Since this data was available in late calendar year 2014, the Federal Team compared the estimated equipment usage to actual equipment usage in FY 2014. The FY 2014 Core Pipeline construction activity was nearly analogous to construction activity during FY2010 - FY2012, with the exception that the Tribe did not employ construction contractors (and their equipment) during the FY 2014 construction season. Instead, it employed direct labor and its own equipment (which should have resulted, if anything, in higher equipment usage by the Tribe as there were no contractor supplied equipment available). The comparison found that for every major category and piece of equipment, the Federal Team's estimated hours were significantly higher than the actual hours logged in FY 2014 (~70 percent higher estimated versus actual usage). From this analysis, even taking into consideration minor differences between the construction work performed in FY2010 - FY2012 versus the work performed in FY 2014, it is apparent that the methodology used by the Federal Team to estimate equipment use hours was substantively liberal and generous, to the benefit of the Tribe, and to result in a substantial portion of the equipment costs questioned by the OIG ultimately supported. This analysis was shared with the Tribe during the discussions on December 10, 2014:

Type of Equipment	Federal Team Estimation Methodology	FY2014 Actual Usage
Dozers	150% (50% D8, 100% D6)	92% (39% D8, 53% D6)
Excavators	200% (100% 330, 100% 320)	117% (67% 330, 50% 320)
Loaders	200% (100% 966, 100% 962)	150% (23% 966, 50% 962, 51% 966, 26% 950)
Motor Graders	150% (50% 160, 100% 140)	35% (0% 160, 35% 140)
Telehandler	25%	11%
Water Trucks	200%	87%

This comparison validates that the Federal Team took a liberal approach to generating the initial equipment usage recommendation. As such, in determining the final recommendation to the Awarding Official, no substantive revisions were found necessary to the Federal Team's draft recommendations for resolution of the questioned costs under the equipment rental and purchase categories from the OIG's contract audit.

Other Direct Costs

Ineligible and Unsupported Costs
Contract Audit Numbers R10AV60025 and 06NA602127
Other Direct Costs Category

Summary Recommendation:

		Allocation	Allowed	Disallowed
Allocate	$1,176			
	Allocate/Allow	$729	$729	
	Allocate/Disallow	$447		$447
Allow	$64,932		$64,932	
Disallow	$475,000			$475,000
Audit Total	$541,108.00			
Total Costs			$65,661	$475,447

Discussion:

1. Disallowed costs all result from scholarship, training and education costs. Training and education costs are only allowed to be paid using the Tribe's water distribution project funds when paid for employees of the Corporation who are working on the water distribution project. Donations to other governmental entities (i.e., for general scholarships) is not allowed per 2 CFR 225, Appendix B, Item 12 (Donations and contributions) which states: "Contributions or donations, including cash, property, and services made by the governmental unit, regardless of the recipient, are unallowable."

   One charge (for $125,000) was annotated "2010 AFA Training". Supporting documentation was requested and not provided. It was determined by the Corporation that the check, with no supporting back-up, was deposited into the Tribal savings account.

   The Tribe was asked on several occasions for lists of course attendees and syllabi for all training courses, Tribal Youth Employment programs, and college scholarships. None were provided. The Tribe's own policies require that the Corporation supervisors track all training and education expenditures for their staff and report it to the Corporation's CEO. This documentation was requested, but not provided.

2. Allocated costs of $1,176 are for a summer intern stipend paid to Megan Eagleman. Sixty-two percent (or $729) is allowed as a cost to the Project. Shared costs are allocated between the water distribution project, and other construction projects that the Corporation had on-going at the time. Per Tribal computations, this split should be 62% (water distribution) and 38% (other).

Profit

Ineligible and Unsupported Costs
Contract Audit Numbers R10AV60025 and 06NA602127
Profit Category

Summary Recommendation:

Profit

Allow	$0
Disallow	$2,580,414
Allocate	$0
Total	$2,580,414

Indirect/Administrative Costs

Allow	$1,085,000
Disallow	$1,495,414
Allocate	$0
Total	$2,580,414

Total Costs Allowed per the 8/14/14 report: $122,994

I. Introduction.

On page 7 of its audit, the OIG found:

> [The Corporation] claimed $2,703,408 for profit and utility bills that were classified as an administrative fee. It stated that the administrative fee is profit and this 10 percent profit rate was applied to its costs. The Corporation could not provide the supporting documentation for the costs and the calculation. The contract does not provide for profit and as a result, we questioned $2,580,414 as unsupported costs.

P.L. 93-638, as amended, along with applicable regulations in 25 CFR part 900, limit profit to tribes or tribal organizations that enter into fixed-price contracts with the United States. The Tribe agreed in the AFAs that the provisions of P.L. 93-638, as amended, and 25 CFR Part 900 apply despite the Tribe's self-governance status. In this cost-reimbursable arrangement, the Corporation is not entitled to profit.

II. Background.

The Corporation is a "tribally chartered tribal business corporation," chartered in calendar year 2005 "under the authority of the Constitution and Bylaws of the Chippewa Cree Tribe as a Tribally Chartered Corporation" (Tribal Charter of Incorporation). The Corporation "has the same powers, privileges, and immunities" as the Tribe. The Corporation is wholly owned by the Tribe, and "is and shall be considered an instrumentality of" the Tribe. By Tribal Resolution and as set forth in the AFAs, the Tribe "delegated to [the Corporation] all responsibilities in implementing the terms and conditions of" the AFAs.

The AFAs do not provide for profit. Further, the AFAs do not explicitly specify whether the contract is a fixed-price contract or a cost-reimbursement contract. However, by its terms the

AFAs are clearly not fixed-price. The Corporation has not provided an overall cost for completing the Project, or any part of the Project. Instead, the Corporation requests advances under the AFAs, then later supplies documentation showing that the advances were properly spent under the AFAs. This procedure is in the nature of a cost-reimbursement contract, not a fixed-price contract.

III. Analysis.

The Corporation is chartered and wholly owned by the Tribe, made an instrumentality of the Tribe, and given delegated authority by the Tribe to carry out the AFAs, so the Corporation is a "tribal organization." The applicable statute and regulations provide that profit for tribes and tribal organizations is only permissible in fixed-cost contracts, and the AFAs between Reclamation and the Tribe are cost-reimbursable contracts, not a fixed-cost contracts. Also, while the statute and regulations would not necessarily apply to the Tribe—a self-governance tribe under Title IV of P.L. 93-648, as amended by P.L. 103-413—the AFAs state that P.L. 93-638, as amended, and 25 CFR Part 900 are applicable.

A. Self-Governance.

The Tribe is a compacted tribe under Title IV of P.L. 93-648, as amended by P.L. 103-413, the Tribal Self-Governance Act of 1994. The Tribe entered into a Compact of Self-Governance with the United States on June 26, 1995 (Compact). Accordingly, Title I of P.L. 93-638, along with the regulations at 25 CFR Part 900, do not automatically apply to the Tribe in its contract relationships with the United States. However, section 403(*l*) (25 U.S.C. § 458cc(*l*)) allows the Tribe to choose to include provisions of Title I. Also, the Compact states:

> Subject to the provisions of the regulations to be promulgated pursuant to Section 407 of Title II of P. L. 103-413, the administration of programs, services, functions or activities under Section 403 (b) (2), (b) (3), and (c) of Title II of Pub. L. 103-413, shall be controlled by the terms of the applicable annual funding agreements.

The AFAs between Reclamation and the Tribe state that P.L. 93-638, as amended, and 25 CFR Part 900, apply to the AFAs. That requirement is set forth in an attachment to the AFAs entitled "List of Applicable Federal Laws, Program Statutes, and Regulations."

B. Status of the Corporation.

The applicable statutes and regulations addressing profit apply to tribes and "tribal organizations." The Corporation is the entity to which profit would be paid. Thus, the subject statutes and regulations only apply to the Corporation if the Corporation is a "tribal organization."

> "[T]ribal organization" means the recognized governing body of any Indian tribe; any legally established organization of Indians which is controlled, sanctioned, or chartered by such governing body or which is democratically elected by the adult members of the Indian community to be served by such organization and which includes the maximum participation of Indians in all phases of its activities:

> Provided, That in any case where a contract is let or grant made to an organization to perform services benefiting more than one Indian tribe, the approval of each such Indian tribe shall be a prerequisite to the letting or making of such contract or grant.

25 U.S.C. § 450b(*l*). As explained above, the Corporation is controlled, sanctioned, and chartered by the Tribe's governing body, and is an "instrumentality" of that body. The Corporation is a "tribal organization."

C. <u>Applicable Statutes and Regulations</u>.

P.L. 93-638, as amended, and 25 CFR Part 900 contain specific rules regarding a contractor's profit in a self-determination contract.

P.L. 93-638, Title I, provides:

> (4) (A) Subject to subparagraph (B), in funding a <u>fixed-price construction contract</u> pursuant to section 106(a) [25 USCS § 450j-1(a)], the Secretary shall provide for the following:
>
> (i) The reasonable costs to the tribe or tribal organization for general administration incurred in connection with the project that is the subject of the contract.
>
> (ii) <u>The ability of the contractor that carries out the construction contract to make a reasonable profit</u>, taking into consideration the risks associated with carrying out the contract and other relevant considerations.
>
> (B) In establishing a contract budget for a construction project, the Secretary shall not be required to separately identify the components described in clauses (i) and (ii) of subparagraph (A).
>
> (C) The total amount awarded under a construction contract shall reflect an overall fair and reasonable price to the parties, including the following costs:
>
> (i) The reasonable costs to the tribal organization of performing the contract, taking into consideration the terms of the contract and the requirements of this Act and any other applicable law.
>
> (ii) The costs of preparing the contract proposal and supporting cost data.
>
> (iii) The costs associated with auditing the general and administrative costs of the tribal organization associated with the management of the construction contract.
>
> (iv) <u>In the case of a fixed-price contract, a fair profit determined by taking into consideration the relevant risks and local market conditions</u>….

25 USCS § 450j(m) (emphasis added).

The applicable regulations, found at 25 CFR Part 900, further provide:

> § 900.116 Are negotiated fixed-price contracts treated the same as cost-reimbursable contracts?
>
> > Yes, except that in negotiated fixed-price construction contracts, appropriate clauses shall be negotiated to allocate properly the contract risks between the government and the contractor.

In other words, unlike in a cost-reimbursable contract, contractors in fixed-price contracts are entitled to profit to compensate for the risk that they will not complete the contract within the bid price.

Note that when the regulations were implemented, "[n]ine comments suggested that cost reimbursement contracts should also allocate the risk. The Committee took no action. One comment suggested replacing 'fixed-price' with 'negotiated.' The Committee adopted 'negotiated' and inserted it before 'fixed-price' in both the question and response." 61 FR 32492. Thus, the rulemakers appear to have considered whether risk allocation—presumably profit—should also have been permitted in cost reimbursement contracts. The rulemakers declined to do so, possibly because they had no authority to do so in light of the statute.

The regulations further provide:

> § 900.127 What can be included in the Indian tribe or tribal organization's contract budget?
>
> > (c)(4) In cases where the Indian tribe or tribal organization is submitting a fixed-price construction contract:
> >
> > * * *
> >
> > > (ii) The ability of the contractor that carries out the construction contract to make a reasonable profit, taking into consideration the risks associated with carrying out the contract, local market conditions, and other relevant considerations.
>
> § 900.128 What funding shall the Secretary provide in a construction contract?
>
> > The Secretary shall provide an amount under a construction contract that reflects an overall fair and reasonable price to the parties. These costs include:
> >
> > > * * *
> > >
> > > (d) If the Indian tribe or tribal organization is submitting a fixed-price construction contract:

*   *   *

> (2) The ability of the contractor that carries out the construction contract to make a reasonable profit, taking into consideration the risks associated with carrying out the contract, local market conditions, and other relevant considerations including but not limited to contingency.

In the statute and in each of these regulations, profit is only permitted in the case of fixed-price contracts. And as explained above, the AFA is not a fixed-price contract.

D. <u>Statutory Interpretation</u>.

Two different principles of statutory interpretation lead us to conclude that the relevant statute and regulations allow profit for fixed-price contracts and prohibit profit in cost-reimbursable contracts.

First, "[s]tatutes must be interpreted, if possible, to give each word some operative effect." *Walters v. Metro. Educ. Enters.*, 519 U.S. 202, 209 (U.S. 1997); *see also Am. Vantage Cos. v. Table Mountain Rancheria*, 292 F.3d 1091, 1098 (9th Cir. 2002) ("It is a well-established principle of statutory construction that legislative enactments should not be construed to render their provisions mere surplusage." (*internal quotation marks omitted*)). Here, an interpretation allowing for profit in both cost-reimbursable and fixed price contracts would render as inoperative surplusage several clauses like:

- "In the case of a fixed-price contract" (25 USCS § 450j(m));
- "except that in negotiated fixed-price construction contracts" (25 CFR § 900.116);
- "In cases where the Indian tribe or tribal organization is submitting a fixed-price construction contract" (25 CFR § 900.127(c)(4)); and
- "If the Indian tribe or tribal organization is submitting a fixed-price construction contract" (25 CFR § 900.128).

If Congress and the rulemakers intended to allow for profit in contracts other than fixed-price contracts, each of those clauses would be completely unnecessary. The statute and regulations cannot be interpreted that way.

Another applicable canon of statutory interpretation is known by the Latin phrase *expressio unius est exclusio alterius*, which translates to "the expression of one is the exclusion of the other." As explained in Singer, STATUTES AND STATUTORY CONSTRUCTION, § 47:23 (2000), the doctrine of "*expressio unius est exclusio alterius*" means that "[a] statute which provides that a thing shall be done in a certain way carries with it an implied prohibition against doing that thing in any other way." Or, as the Supreme Court has explained, "[t]he canon depends on identifying a series of two or more terms or things that should be understood to go hand in hand, which [is] abridged in circumstances supporting a sensible inference that the term left out must have been meant to be excluded." *Barnhart v. Peabody Coal Co.*, 537 U.S. 149, 168 (2003) (quoting *Chevron U.S.A. Inc. v. Echazabal*, 536 U.S. 73, 81 (2002). Here, by explicitly stating profit is allowed in fixed-price contracts, Congress and the Department have deliberately excluded the possibility of profit for the Contractor in cost-reimbursable contracts.

However, "statutes are to be construed liberally in favor of the Indians, with ambiguous provisions interpreted to their benefit." *Mont. v. Blackfeet Tribe of Indians*, 471 U.S. 759, 766 (U.S. 1985). And further, 25 CFR § 900.3(b)(11) provides:

> The Secretary's commitment to Indian self-determination requires that these regulations be liberally construed for the benefit of Indian tribes and tribal organizations to effectuate the strong Federal policy of self-determination and, further, that any ambiguities herein be construed in favor of the Indian tribe or tribal organization so as to facilitate and enable the transfer of services, programs, functions, and activities, or portions thereof, authorized by the Act.

But there is nothing ambiguous about the applicable language here. Applying the principles of statutory interpretation set forth here, Congress' and the rulemakers' intent is clear.

IV. Conclusion.

Under statutes and regulations which the Tribe agreed would apply to the AFA, profit is not allowed in this cost-reimbursable arrangement.

Subsequent Proposal by the Tribal Team:

At the January 20-21, 2015, meeting between the Tribal and Federal Negotiation Teams, the Tribal Team stated that included in this category are costs that would be considered "Indirect Costs." Indirect Costs are defined as costs incurred for a common or joint purpose benefiting more than one cost objective.

The Tribal Team requested, and the Federal Team agreed to allow, additional time to prepare an analysis of the Indirect Costs to determine what would qualify for consideration. On March 13, 2015, the Tribal Team provided a list to the Federal Team of indirect costs for consideration. After review of the items, the Federal Team determined that the list provided was not sufficient to support allowance of all costs on the list. However, some of the costs do appear to qualify as indirect costs. To resolve the issue, the Tribal and Federal Team used cost information from FY 2015 as a baseline for determining an allowable amount. This is justified because, in FY 2015, accounting for indirect/administrative costs was being tracked appropriately. Indirect/administrative costs for FY 2015 were estimated to be $250,000 through September 2015. By applying the previously agreed split of 62%/38%, Reclamation's portion is estimated to be $155,000 per year. For the seven year period under audit, this equates to $1,085,000 of allowable indirect/administrative costs.

Tribal Employment Rights Ordinance

Ineligible and Unsupported Costs
Contract Audit Numbers R10AV60025 and 06NA602127
TERO(Tribal Employment Rights Ordinance) Category

Summary Recommendation:

Allow	$2,126,012
Disallow	$134,109
Allocate	$0
Total	$2,260,121

Total Costs Allowed per the 8/14/14 report: $2,055,435.85

I. Introduction.

On page 7 of the OIG report, the OIG found:

> [The Corporation] claimed $2,260,121 for the TERO fees and could not or did not provide supporting documentation that TERO fees should be claimed for work outside of the reservation per the Tribe's TERO regulation. We therefore questioned $2,260,121 as unsupported costs. *(Emphasis added.)*

The OIG is correct: the Tribe's current TERO does not appear to apply to much if any of the Corporation work here. But the TERO may be amended and applied retroactively to cover certain work done outside the Reservation. If a sufficient amended TERO is enacted, then most of the questioned TERO fees may be allowed. However, approximately $134,109 in TERO fees assessed against other disallowed costs should be disallowed.

II. Analysis.

The 2012 AFA provides that the "Tribal Employment Rights Ordinance will apply to all activities conducted by the Tribe or its subcontractors under this AFA." FY 2012 AFA, Art. II, § 3.C. However, by its own terms, the Tribe's TERO does not appear to apply to the Corporation's RB/NCMRWS work.

The Tribe's Employment Rights Ordinance, No. 2-86, was passed in 1986. The TERO applies to "Covered Employers," meaning employers "employing two or more employees who during any 30 day period, spend, cumulatively, 40 or more hours performing work within the exterior boundaries of the Rocky Boy Reservation." Ordinance No. 2-86, § 2.C., *emphasis added*. The applicable TERO fee portion of the ordinance then provides:

> Every covered employer with a construction contract in the sum of ____ or more shall pay a one-time fee of 1% of the total amount of the contract. Such fee shall

> be paid by the employer prior to commencing work on the Rocky Boy Reservation. However, where good cause is shown, the Director may authorize a construction contractor to pay said fee in installments over the course of the contract. [1]

Though the initial TERO fee was 1%, the fee was increased in 1993 to 2%. Ordinance No. 2-93. At some point before work began on the Project, the TERO fee was increased again, to 3%. Finally, several years into the Project work at issue here, the TERO fee was increased to 5% in 2010. Resolution No. 86-10.

The Reservation is defined in the Act as "includ[ing] all land and interests in land that are held in trust by the United States for the Tribe at the time of the enactment of this title." Much of the core system will be located outside the exterior boundary of the Reservation. The water treatment plant and the core pipeline will be on lands in which the United States has acquired an interest (fee or right-of-way) in trust for the Tribe since the enactment of the Act.

So far, a majority of the work done on the Project has been off the Reservation, but within rights-of-way held in trust for the Tribe. However, significant work has also taken place on the Reservation, including approximately eighteen miles of twelve-inch PVC pipeline for segments known as Laredo Phase 1, Box Elder/Middle Dry Fork, and Divide. These segments have largely been short-term projects, as opposed to years of ongoing work on approximately eighteen miles of thirty-six-inch steel and concrete pipe being laid for the core pipeline. While the lengths of thirty-six-inch versus twelve-inch pipeline are comparable, work on the thirty-six inch segment is much more difficult and time-consuming due to the size, weight, and complexity of the larger pipe.

Thus, the Corporation does not appear to be a "covered employer" if its employees were spending less than 40 hours per month working on the Reservation. But the TERO definition is ambiguous. Is an employer a Covered Employer only during those 30 day periods in which two or more employees cumulatively spend 40 hours or more working on the Reservation? Given the ambiguity and the fact that most of the Corporation's work, most of the time, was off the Reservation, the Corporation is probably not a "Covered Employer," at least during most of the subject time period.

Even if the TERO did not apply to much (or any) of the Corporation's work on the Project, the Tribe can resolve the problem by amending the TERO and explicitly applying it retroactively.

Generally speaking, retroactivity is unusual and disfavored. "[R]etroactivity is not favored in the law, and . . . congressional enactments and administrative rules will not be construed to have retroactive effect unless their language requires this result." *Landgraf v. Usi Film Prods.*, 511 U.S. 244, 264 (1994) (*internal punctuation omitted*).

But here, assuming the only affected entity is the Corporation, and assuming the Corporation does not object, the Tribe can amend its TERO with retroactive effect and resolve the IG's

[1] Ordinance No. 2-86, § 11.A. The meaning of the blank in the first sentence is not clear, but we assume THE CORPORATION's contracts are for amounts well in excess of whatever amount may have been intended.

concerns.[2] The Federal Team recommended this to the Tribe at our May 2014 meetings. We will not presume to propose exact language for such an amendment, but the TERO could be amended to cover work performed on or associated with Reservation lands or other interests in land held in trust by the United States for the Tribe. Also, 25 U.S.C. § 450e(c) applies TEROs "with respect to any self-determination contract, or portion of a self-determination contract, that is intended to benefit one tribe." The Tribe here might also amend its TERO to explicitly apply "to any self-determination contract, or portion of a self-determination contract, that is intended to benefit" the Tribe, regardless of where the work is performed. According to the Tribe's attorney, Dan Belcourt, the Tribal Council has already passed, or will soon pass, an amended TERO. Reclamation should review the TERO before making a final decision on the TERO costs.

III. **Conclusion**.

The Tribe's current TERO probably does not cover the Corporation's work on the Project. However, the Tribe may amend its TERO to clearly cover all of the Corporation's work on the Project, and explicitly apply the TERO retroactively.

The total allowed TERO fee must be reduced by the portion of the fee that was charged on other disallowed or reallocated costs. Approximately 40.43% of TERO fees were assessed at a 3% rate, while approximately 59.56% were assessed at a 5% rate. The report concludes that $4,884,038 should be disallowed or reallocated. The 3% and 5% TERO rates were applied to the disallowed costs in the same ratios they were applied to total costs. Thus, we calculate that $134,109 in TERO must be disallowed because it was assessed against costs that should be disallowed or reallocated.

[2] If a contractor (the Corporation or otherwise) objected to the TERO's application outside the Reservation, a court may hold that the Tribe had no jurisdiction to enforce the TERO. The Tribe's TERO can likely only apply off the reservation with the consent of the contractor. *Montana Dep't. of Trans. v. King*, 191 F.3d 1108; 1999 U.S. App. LEXIS 21566 (9th Cir. 1999) (Tribes lacked jurisdiction to enforce tribal employment ordinance against plaintiff state for work performed within boundaries of the reservation on the right of way owned by the state, and as such, exhaustion of tribal remedies by the state was not required). In *Moss* v. *Bossman*, 2009 U.S. Dist. LEXIS 26367 (D. S.D. 2009) (in dicta) (Tribe did not have jurisdiction to apply its TERO ordinance to a non-Indian business located outside the disputed but court-determined boundary of the reservation).

Subsequent Information Provided by the Tribal Team:

On April 29, 2015, the Tribal Team submitted an updated TERO resolution that covers the Corporation's work on the Project. Therefore, the only adjustment to the TERO costs is a result of disallowed costs in other categories. The TERO rate was 3% from 11/2005 through 5/2010 and 5% from 6/2010 on. The disallowed costs were separated into these two timeframes to determine what the TERO amount should be. The calculation is as follows:

	11/2005 - 05/2010 3%	06/2010 - present 5%	TERO
Direct Labor			
Disallowed	43,616.38	193,665.62	10,991.77
Direct Materials			
Disallowed	62,499.43	232,331.67	13,491.57
Other Direct			
Disallowed	300,446.88	175,000.00	17,763.41
Equipment			
Disallowed		448,378.00	22,418.90
Profit/Admin			
Disallowed	266,373.56	1,229,040.90	69,443.25
Total Disallowed TERO			$134,108.90

Appendix 1

OFFICE OF
INSPECTOR GENERAL
U.S.DEPARTMENT OF THE INTERIOR

Contract Audit

Bureau of Reclamation Funding Agreements with Chippewa Cree Construction Corporation: Contract No. R10AV60025 and 06NA602127

This report is exempt from disclosure to the public pursuant to exemption 4 of the Freedom of Information Act, 5 U.S.C. § 552(b)(4). For this reason, recipients of this report may not show or release its contents for purposes other than official review and comment under any circumstances.

OFFICE OF
INSPECTOR GENERAL
U.S.DEPARTMENT OF THE INTERIOR

December 16, 2013

AUDIT REPORT

Memorandum

To: Michael J. Ryan
Regional Director, Great Plains Region
U.S. Bureau of Reclamation

From: Charles Haman
Regional Manager for Audits, Inspections, and Evaluations

Subject: Audit Report – Bureau of Reclamation Funding Agreements with Chippewa Cree Construction Corporation: R10AV60025 and 06 NA602127
Report No. C-CX-BOR-0010-2013

This report presents the results of our audit of costs claimed by the Chippewa Cree Construction Corporation (Corporation) for Annual Funding Agreement (AFA) R10AV60025 and Contract Number 06 NA602127. The U.S Bureau of Reclamation (USBR) requested that we audit incurred costs—totaling $52,729,482. We identified questioned costs of $12,914,545. The "Results of Audit" section of this report provides details on these costs.

Background

In 2006, Congress passed the Rural Water Supply Act of 2006 (Public Law (Pub. L.) 109-451), that provides the basis for a rural water program in USBR. Prior to the Rural Water Supply Act, rural water projects were authorized and funded by specific legislation for each project. On March 3, 2006, USBR awarded a Pub. L. 93-638 agreement, Title IV, for $129,280,000. The purpose of this agreement was to transfer funds to the Chippewa Cree Tribe (Tribe) of the Rocky Boys Reservation for planning, designing, and constructing the Tribe's portion of the Rocky Boy's/North Central Montana Regional Water Systems (project), as authorized by Pub. L. 107-331. The Tribe formed the Corporation to oversee construction of tribal infrastructures, including the project. The Board of Directors manages the Corporation's business affairs. The Board of Directors has five members appointed by the Tribe's Business Committee. The Corporation's Board of Directors appoints three more members to the board.

For fiscal years (FY) 2006 through 2012, the Corporation was awarded $52,729,482 for the project through AFAs. This includes $27,526,000 in American Reinvestment and Recovery Act (ARRA) funds awarded in 2009 and 2010 for project management, design, and construction of the intake superstructure and core pipeline segments. An AFA is a legally binding, written, annual agreement negotiated and entered into between a self-governing tribe and an entity such as USBR.

Figure 1 below shows the funding for FYs 2006 through 2012.

Fiscal Year	AFA	ARRA	Additional AFA	Additional Funds	Total
2006	$1,614,747		$3,758,501		$5,373,248
2007	$420,000				$420,000
2008	$3,554,680				$3,554,680
2009	$4,412,554	$19,860,000			$24,272,554
2010	$5,660,000	$7,666,000	$864,000		$14,190,000
2011	$540,000			$32,000	$572,000
2012	$4,287,000			$60,000	$4,347,000
TOTALS	$20,488,981	$27,526,000	$4,622,501	$92,000	$52,729,482

Figure 1. Funding for FY 2006 through FY 2012

The Corporation provided a general ledger that included $59,092,819 in costs associated with the project. In regards to the $59,092,819, USBR awarded the Corporation $52,729,482. We found the difference of $6,363,337 as funds the Corporation commingled with State of Montana funds received through the North Central Montana Regional Water Authority. USBR also gave additional funds to the Corporation that could have been used by USBR for administrative costs associated with the ARRA funds. The additional funds were awarded as modifications to the contract to the Corporation.

Objectives

The objectives of our audit were to determine whether the claimed costs were—

- allowable under applicable Federal laws and regulations;
- allocable to the contract and incurred in accordance with its terms and conditions; and
- reasonable and supported.

To meet these objectives, we—

- interviewed USBR staff, the Corporation's personnel, and other appropriate individuals;
- reviewed the agreements and Federal Acquisition Regulation (FAR) and Code of Federal Regulations provisions pertaining to claimed costs;
- reviewed the Office of Management and Budget (OMB) Circular A-87 "Cost Principles for State, Local and Indian Tribal Governments," for regulations pertaining to claimed costs;

- reviewed and analyzed the Corporation's general ledger (computer-generated data) pertaining to claimed costs for reasonableness;
- reviewed the Corporation's explanation of its information controls over computer-generated data relevant to the audit;
- reviewed the Corporation's policies and procedures;
- reviewed the Corporation's and its subcontractors' invoices to become familiar with how amounts were being billed on the contract; and
- reviewed the support for the Corporation's claimed costs.

Scope

Our audit work included reviewing the Corporation's $52,729,482 claimed costs. This amount included indirect costs of $4,963,529 and direct costs of $47,765,953. We performed our audit at the Corporation's office in Box Elder, MT; the subcontractor's office in Great Falls, MT; and our offices in Lakewood, CO.

Methodology

We conducted this audit in accordance with Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. We obtained computer information including general ledger, payroll, and depreciation schedules from the Corporation.

We used computer-generated data for all costs during our contract review. We did not perform reliability assessments of the quality of the data because it was outside of our review. Based on our test results, we either accepted the data or performed additional testing. We relied on computer-generated data for all direct and indirect costs associated with the contract. We took samples of costs and verified them against documents such as invoices, receiving reports, sub-contracts, and payment documentation.

Results of Audit

We based our determination of questioned costs on our review and evaluation of the Corporation's and subcontractors' costs. We identified numerous areas with significant deficiencies. We identified costs as unsupported when we were given insufficient documentation related to the costs. We identified costs as ineligible when we determined that they were either unreasonable or not allowable under the terms of the contract or applicable provisions of the FAR and OMB circular A-87.

The Corporation does not have a cost accounting system, and as a result, cannot allocate costs to more than one project. Those receiving Federal financial assistance must comply with applicable regulations governing the program as clearly identified in the AFA they sign. This includes adherence to OMB Circular A-87 as codified in 43 C.F.R. § 12, which establishes that a recipient must abide by administrative requirements of financial assistance programs. These requirements include maintaining an accounting system that provides effective control and accountability for all funds, property, and other assets.

Of the $52,729,482 in claimed costs, we identified $11,739,744 in unsupported costs and $1,174,801 in ineligible costs, totaling $12,914,545 in questioned costs, as shown below in Figure 2. Of the $12,914,545 in questioned costs, we identified $4,379,460 related to ARRA funds.

Category Description	Claimed Costs	Ineligible Costs	Unsupported	Revised Claimed Costs
Direct Costs	$47,765,953	$1,174,801	$6,899,209	$39,691,943
Subtotal of Direct Costs Prior to Profit	$47,765,953	$1,174,801	$6,899,209	$39,691,943
Profit (Administration Fee of 10 percent)	$2,703,408		$2,580,414	$122,994
TERO Costs	$2,260,121		$2,260,121	$0
Total of Corporation's Indirect Costs	$4,963,529		$4,840,535	$122,994
Total Costs	$52,729,482	$1,174,801	$11,739,744	$39,814,937

Figure 2. Ineligible and unsupported costs under the agreements.

Notes

1. Direct Costs—Claimed Costs of $47,765,953; Ineligible Costs of 1,174,801 and Unsupported Costs of $6,899,209

The Corporation claimed $47,765,953 for the direct costs as summarized in Figure 3.

This report is exempt from disclosure to the public pursuant to exemption 4 of the Freedom of Information Act, 5 U.S.C. § 552(b)(4). For this reason, recipients of this report may not show or release its contents for purposes other than official review and comment under any circumstances.

Description	Claimed	Ineligible Costs	Unsupported	Notes
Direct Costs				
Direct Labor	$26,704,632	$0	$3,178,185	A
Direct Materials	$16,126,728	$874,801	$1,071,496	B
Equipment Rental	$2,796,127	$0	$1,581,481	C
Equipment Purchased	$972,564	$0	$826,939	D
Other Direct Costs	$1,165,902	$300,000	$241,108	E
Total Corporation's Direct Costs	$47,765,953	$1,174,801	$6,899,209	

Figure 3. Direct cost summary.

A. Direct Labor—Claimed Costs of $26,704,632; Unsupported Costs of $3,178,185

The Corporation claimed $26,704,632 for the subcontractors' work for design, planning, and construction of the Rocky Boy pipeline. The Corporation's general ledger showed that the claims started on May 4, 2006, and ended on March 31, 2013. We reviewed the subcontractors' contracts and other supporting documentation identifying that the Corporation is performing work on other projects and billing these costs incorrectly to this project. The Corporation does not have an accounting system that allows for cost allocation required by 43 C.F.R. § 12. Consequently, the salaries and benefits for the Chief Executive Officer (CEO) and the Chief Financial Officer were allocated entirely to the project and not allocated to other projects. In addition, the Corporation did not allocate subcontractors' direct labor and construction expenses to other projects that the Corporation was working on during the same time, or provide supporting documentation for these costs. We therefore have unsupported costs of $3,178,185 of the claimed direct labor costs.

B. Direct Materials—Claimed Costs of $16,126,728; Ineligible Costs of $874,801; and Unsupported Costs of $1,071,496

The Corporation claimed $16,126,728 for subcontractors' direct materials that consisted of pipeline supplies, sand, steel, concrete, fuel, valves, and other related direct materials. As noted above, the Corporation does not have an accounting system to allow for cost allocation. The Corporation did not allocate expenses such as fuel, supplies, and repair equipment to other projects that the Corporation was working on during this period. At the time of the incurred costs, the CEO was an owner of a subcontractor's supply business that charged $874,801. OMB Circular A-87 is clear regarding arms-length transactions. As a result of the CEO being a related party and not bargaining at arms-length, we consider these costs ineligible. In addition, there was no supporting documentation for other direct materials' costs of $1,071,496 as required by 43 C.F.R § 12. We therefore classified $874,801 as ineligible costs and $1,071,496 as unsupported costs of the claimed amount.

C. Equipment Rental—Claimed Costs of $2,796,127; Unsupported Costs of $1,581,481

The Corporation claimed $2,796,127 for equipment rental costs related to excavating and constructing the water pipeline. The Corporation rented heavy equipment with USBR funds. The Corporation used the heavy equipment for projects, including those that were not USBR funded. 43 C.F.R § 12 requires that recipients shall adequately safeguard all such assets and assure they are used solely for authorized purposes. Additionally, as noted above, the Corporation did not have a cost accounting system to allocate rental expenses to the other projects, and as a result, was unable to provide documentation to support that the rental costs were appropriately allocated to the USBR project. We therefore classified $1,581,481 as unsupported costs.

D. Equipment Purchased—Claimed Costs of $972,564; Unsupported Costs of $826,939

The Corporation claimed $972,564 for equipment purchase costs related to excavating and constructing the water pipeline. The Corporation bought heavy equipment with USBR funds. The Corporation used the heavy equipment for projects, including those that were not USBR funded. As previously noted, 43 C.F.R § 12 requires that assets are used solely for authorized purposes. Additionally, as noted above, the Corporation did not have a cost accounting system and was unable to provide support that $826,939 of these claimed costs were appropriately allocated. We therefore classified $826,939 as unsupported costs.

E. Other Direct Costs—Claimed Costs of $1,165,902; Ineligible Costs of $300,000; and Unsupported Costs of $241,108.

The Corporation claimed $1,165,902 for other direct costs relating to the construction of the water pipeline. Other direct costs include a sales catalog, rights-of-way, crop damage, easements, and training. Of this amount, the Corporation contributed and claimed $425,000 for scholarships and higher education. Of this amount, $300,000 is an ineligible contribution per the FAR 31.205-44 "Training and Education Costs" and $125,000 was not supported. In addition, the Corporation could not provide supporting documentation for $116,108 for crop damages, rights-of-way, and a sales catalog. We therefore classified $300,000 as ineligible costs and $241,108 as unsupported costs.

2. **Profit (Administration Fee of 10 percent)—Claimed Costs of $2,703,408; Unsupported Costs of $2,580,414**

The Corporation claimed $2,703,408 for profit and utility bills that were classified as an administration fee. It stated that the administrative fee is profit and this 10 percent profit rate was applied to its costs. The Corporation could not provide the supporting documentation for the costs and the calculation. The contract does not provide for profit, and as a result, we questioned $2,580,414 as unsupported costs.

3. **Tribal Employment Rights Ordinance (TERO)—Claimed Costs of $2,260,121; Unsupported Costs of $2,260,121**

The Corporation claimed $2,260,121 for the TERO fees and could not or did not provide supporting documentation that TERO fees should be claimed for work outside of the reservation per the Tribe's TERO regulation. We therefore questioned the $2,260,121 as unsupported costs.

Recommendations

We recommend that USBR:

1. Resolve the unsupported costs of $11,739,744; and
2. Resolve the ineligible costs of $1,174,801.

Response to Report

In accordance with the Departmental Manual (361 DM 1), please provide us with your written response by March 17, 2014, regarding disposition of the ineligible and unsupported costs identified in this report. Copies of documentation related to the final disposition of the questioned and unsupported costs should be provided with your response. If final disposition of the questioned and unsupported costs is not obtained by the requested date, please provide information on actions taken or planned, including target dates and titles of officials responsible for implementation.

Please address your response to me at:

U.S. Department of the Interior
Office of Inspector General
12345 West Alameda Parkway, Suite 300
Lakewood, CO 80228

The legislation creating the Office of Inspector General requires that we report to Congress semiannually on all audit, inspection, and evaluation reports issued; actions taken to implement our recommendations; and recommendations that have not been implemented.

If you have any questions regarding this report, please contact Ms. Patty Van Duzer, Audit Supervisor, or me at 303-236-9161.

Report Fraud, Waste, and Mismanagement

Fraud, waste, and mismanagement in Government concern everyone: Office of Inspector General staff, departmental employees, and the general public. We actively solicit allegations of any inefficient and wasteful practices, fraud, and mismanagement related to departmental or Insular Area programs and operations. You can report allegations to us in several ways.

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