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OFFICE OF INSPECTOR GENERAL

OPERATIONS INTERNAL AUDIT TEAM

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Lawrence Warder, Chief Financial Officer
Office of the Chief Financial Officer
U.S. Department of Education
400 Maryland Avenue, SW
Washington, DC 20202

Grover J. Whitehurst, Director
Institute of Education Sciences
U.S. Department of Education
400 Maryland Avenue, SW
Washington, DC 20202

Dear Messrs. Warder and Whitehurst:

This **Final Audit Report**, entitled *Controls Over Contract Monitoring for Institute of Education Sciences Contracts*, presents the results of our audit. The purpose was to determine whether the Department's contract monitoring process ensures (1) contractors adhere to the requirements of the contract, and (2) the Department receives the products and services intended. Our review included evaluation of the 10 Institute of Education Sciences (IES) contracts for which the highest amount of payments were made during Fiscal Year (FY) 2005.

BACKGROUND

The Department of Education (Department) contract management staff includes the Contracting Officer (CO), Contract Specialist (CS), and the Contracting Officer's Representative (COR). CO and CS staff are located in Contracts and Acquisition Management (CAM) under the Department's Office of the Chief Financial Officer (OCFO). The COR is a member of the Principal Office (PO) staff, in this case, IES.

The CO has overall responsibility for contract management. However, the contract monitoring process is a team effort between the CO, CS, and COR. Contract monitoring is based on the

terms and conditions in each contract, the requirements set forth in the *Federal Acquisition Regulation* (FAR), and Department policies and procedures.

For FY 2005, payments under Department contracts totaled \$1,474,385,045. Payments to IES contracts totaled \$351,921,139 (24 percent). During the year, IES was responsible for 142 of the total 519 active contracts (27 percent). IES was the PO with the second highest amount of contract payments for FY 2005, and was responsible for the most active contracts during the year.

On September 20, 2002, the Office of Inspector General (OIG) issued an audit entitled, *Audit of the Department's Process for Identifying and Monitoring High-Risk Contracts that Support Office of Educational Research and Improvement (OERI) Programs*.¹ In the prior audit, we found Department staff did not always ensure compliance with contract terms and conditions, or follow established regulations, policies, and procedures in monitoring OERI contracts. We made recommendations to IES and OCFO to improve contract monitoring for IES contracts related to the following major areas: (1) staff familiarity with regulations, policies, procedures, and contract terms; (2) deliverable tracking, receipt and acceptance; (3) written evaluations of contractor reports; (4) invoice review process; and (5) requirements for issuing COR delegation letters.

This report evaluates the current contract monitoring process for IES contracts and assesses the effectiveness of corrective actions implemented as a result of the prior audit.

AUDIT RESULTS

We found the Department's contract monitoring process for IES contracts did not always ensure contractors adhered to the contract requirements and the Department received the products and services intended. Department staff did not adequately document receipt and acceptance of deliverables, prepare written evaluations of contractor-submitted reports, appropriately review invoices prior to approving payment, and issue or sign COR appointment letters timely. This occurred because Department staff were not always familiar with regulations, policies and procedures, or with the terms of the contract they were assigned responsibility to monitor.

All of the issues noted were also reported in the prior audit of IES contract monitoring. The corrective actions taken by the Department for these items in the prior audit were not always effective, and further corrective actions are needed to improve monitoring in these areas.

In a combined response to the draft report, OCFO and IES concurred with the finding and recommendations, and presented proposed corrective actions for implementing the recommendations. The combined response is summarized after the finding, and is included in full as Attachment 3 to this report.

¹ The IES was formerly part of the OERI. In 2002, IES became a separate PO.

FINDING – Improvements Were Needed in Contract Monitoring for IES Contracts

We noted at least one area where improvements were needed in contract monitoring for each of the 10 contracts reviewed. Specifically, we noted CAM staff and IES CORs did not always:

1. Adequately document receipt and acceptance of deliverables (10 contracts),
2. Prepare written evaluations of contractor-submitted reports (10 contracts),
3. Detect inappropriate charges on invoices prior to approving payments (3 contracts), and
4. Issue and/or sign COR appointment letters timely (3 contracts).

Federal Acquisition Regulation (FAR) Section 1.602-2, states,

Contracting officers are responsible for ensuring performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the United States in its contractual relationships.

Department Directive (Directive) OCFO:2-108, *Contract Monitoring for Program Officials*, dated September 16, 2004, Section II, states,

The policy of the Department is: (a) to monitor every contract to the extent appropriate to provide assurance that the contractor performs the work called for in the contract; and (b) to develop a clear record of accountability for performance.

Details on the issues noted in each area follow. Attachment 2 includes details of issues noted for each contract.

Issue 1 – Department Staff Did Not Adequately Document Receipt and Acceptance of Deliverables

In all 10 contracts, we noted CAM staff and/or CORs did not adequately document receipt of deliverables. Specifically, we noted improvements were needed to ensure all deliverables were received, were received timely, met contract requirements, and acceptance of deliverables was formally documented. (*ED01CO0010, ED01CO0011, ED01CO0012, ED01CO0039/0007, ED01CO0093/0004, ED01CO0120, ED02CO0023, ED02CO0034, ED02CO0035, RN95127001*)²

Directive Section VII.D.2, “Elements of a contractor’s performance of importance to the Government,” states,

- a. Contractor Performance Outcomes and Specifications – Deliverables provided by the contractor must meet the specifications called for in the contract.

² Contract numbers are provided parenthetically for each issue area. See Attachment 1 for a list of the contracts reviewed, and Attachment 2 for details of the issues noted by contract.

- b. Timeliness – Deliverables must be provided on or before the exact due dates cited in the contract.
- c. Quality – Deliverables must conform to the quality called for in the contract.
- d. Cost Control – The contractor in cost-reimbursement contracts is to stay within the limit of funds specified in the contract and must expend funds in an efficient and well-managed manner....

Directive Section VI.E.4 states the COR

Maintains regular written communication with the CO concerning all aspects of contractor performance, including, but not limited to, providing monitoring information, advice, and requests for formal administrative action to the CO in a timely manner. Such communication may be informal, such as by electronic mail, but must be in writing so that a written record is available.

Directive Section VII.N.2 states,

Only a CO can formally accept or reject deliverables. However, with respect to deliverables which the contractor must send directly to the COR, the COR will recommend acceptance or rejection to be furnished in writing to the CO.

Directive Section VII.O.1.a-d states,

Deficient contractor performance is any inexcusable failure by the contractor to perform as called for in the contract. Examples include:

- a. Failure to make such satisfactory progress as to endanger contract performance;
- b. Failure to submit required reports on time;
- c. Failure to submit deliverables on time; and,
- d. Failure to submit reports or deliverables as specified (quantity, quality, etc.)

In 6 of the 10 contracts reviewed, Department staff stated that acceptance of deliverables was indicated in the Contracts and Purchasing Support System (CPSS) when invoices are paid. Prior to payment of invoices, a receipt for the invoice is created in CPSS. Department staff stated that recommendation of acceptance of deliverables is noted on the receipts in CPSS. However, we found this process did not adequately document the COR's recommendation for acceptance or rejection of specific deliverables. The CPSS information did not always indicate whether deliverables were received timely, and whether the deliverables were determined by Department staff to meet all requirements. Specifically, we found that complete information on deliverables' dates of receipt/timeliness was not annotated in CPSS, and the acceptability of deliverables was not indicated for four contracts. The other two contracts included blanket statements that all deliverables were on time and acceptable, but they did not list the deliverables. These determinations should be fully documented to protect the Department's interests. Seven calendar days after receipt, deliverables are considered to be constructively accepted by the Department if no indication is made that the deliverables do not meet requirements. Since deliverable due dates are not necessarily aligned with invoice billing dates, acceptance may have occurred due to the

passage of time if the invoice receipt process is used to document deliverable receipt and acceptance. A separate process is needed to document the Department's evaluation of deliverables for timeliness and to ensure the deliverables meet requirements. (**ED01CO0010, ED01CO0011, ED01CO0012, ED02CO0023, ED02CO0035, RN95127001**)

In another contract, the COR stated she never communicated with the CO/CS regarding acceptance of deliverables, although she was required to since the deliverables were received by the COR, not the CO. (**ED02CO0034**) In three other contracts, the CORs stated they sent comments back and forth with the contractor until there were no more issues with the reports received. (**ED01CO0039/0007, ED01CO0093/0004, ED01CO0120**) However, this represents an inappropriate practice; as stated in the Directive cited above, only a CO has the authority to accept or reject deliverables. By sending deliverables back to the contractor for correction, the CORs were, in effect, rejecting the deliverables. We found these CORs were not aware of this restriction.

In one of the contracts above, we also found the contractor did not meet all requirements of a deliverable (**RN95127001**). Specifically, the contractor did not provide statistical detail as required by the contract as part of the monthly report submissions. Section B.1.2 of the Statement of Work in the contract terms states,

At a minimum, the contractor shall include the following items in the Monthly Activity Report:

1. Period covered;
2. Statistics on the number of [Education Statistical Services Institute] ESSI personnel by labor category and assignment including management and clerical support . . .

The CS stated the absence of the statistical data was not a problem because the monthly reports come in at the same time as the invoices, and the invoices show charges for personnel. However, the COR stated the monthly reports do not come in at the same time as the invoices. No change had been made to the contract to eliminate the requirement for the statistics on the monthly report. Department staff should have noted the report did not comply with requirements, and the CO should have rejected the deliverable until all requirements of the report were met.

Without close review of deliverables to ensure all requirements were met, and adequate documentation on deliverable receipt and acceptance, the Department cannot ensure it has received the products and services intended. By accepting deliverables that do not meet requirements, the Department may be setting a precedent that may affect its ability to enforce other requirements. By not fully documenting the receipt and acceptance or rejection of deliverables, the Department may have difficulty pursuing action against a contractor for nonperformance. Acceptance or rejection of deliverables by unauthorized personnel may also compromise efforts to enforce contract requirements.

Issue 2 – CORs Did Not Prepare Written Evaluations of Contractor-Submitted Reports

In all 10 contracts reviewed, we noted that CORs did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO. (*ED01CO0010, ED01CO0011, ED01CO0012, ED01CO0039/0007, ED01CO0093/0004, ED01CO0120, ED02CO0023, ED02CO0034, ED02CO0035, RN95127001*)

Directive Section VII.G.2.a.ii states,

The COR must make a written evaluation of each report. Depending on the type of contract and relative importance of the report, the evaluation might be either rigorous or reasonably informal. For example, the evaluation of a progress report should compare required versus actual performance, whereas the evaluation of an occasional report detailing technical rather than performance issues might simply note that it was read and found to disclose no problems.

In addition, Directive Section VII.G.3 states, “All evaluations of reports made by the COR must be sent to the CO”

We found the CORs were not familiar with these requirements. Five CORs stated that any issues noted with respect to the reports submitted by the contractor were discussed with the contractors, but that written evaluations were not provided to the COs.. (*ED01CO0010, ED01CO0011, ED01CO0120, ED02CO0023, ED02CO0035*) One COR stated written evaluation of progress reports were documented in CPSS, which the CO could access. We found that although CPSS information for this contract included some brief comments on what deliverables had been received, the comments do not meet the requirements for a written evaluation of reports received. (*ED02CO0034*)

The information contained in the contractor-submitted reports is generally technical in nature and outside the scope of the CO’s expertise. Without feedback from the COR on the technical aspects of the progress reports, the CO may not be aware of information that may indicate problems with contract progress and the need for future actions. The Department’s interests could be harmed in the event of a dispute if the CO is not kept fully informed of contract performance issues.

Issue 3 -- Department Staff Did Not Detect Inappropriate Charges on Invoices Prior to Approving Payments

In 3 of the 10 contracts reviewed, we noted CAM staff and CORs did not note problems with invoices. Specifically, we found the Department paid invoices that included:

- Expenses not pre-approved when required (*ED01CO0012, RN95127001*),
- Application of incorrect direct labor or indirect cost rates (*ED02CO0023, RN95127001*), and
- Insufficient information and/or supporting documentation (*ED01CO0012, ED02CO0023*).

Directive Section VII.A.6 states,

The process of approving a contractor's invoices for payment must be carried out carefully and quickly to protect the Government's interests and ensure that the contractor is dealt with fairly.

Directive Section VII.G.2.d states,

There are many varieties of payment provisions that might be incorporated into contracts depending on the nature of the work and other factors. It is the responsibility of the COR to become familiar with the payment provisions applicable to each contract he or she must monitor.... The COR must review invoices individually and collectively as part of the responsibility to monitor the contractor's progress in performing under the contract.

Directive Section VII.N.4 states,

The CO is responsible for approving a contractor's invoices for payment, but usually after review and advice from the COR in conjunction with the CO's own analysis concerning the contents of the invoice/voucher and the contractor's performance relative to what is being billed.

OCFO Procedure CO-45, *Processing Invoices/ Vouchers for Payment*, dated September 15, 2000, Sections 1.d.2-3 and 5, states,

2. Costs incurred – If the contract is cost-reimbursement, check the costs and labor hours on the invoice/voucher to ascertain whether they reasonably appear to reflect costs and hours incurred in performing the work. Review the costs for reasonableness, allocability and allowability in accordance with [Federal Acquisition Regulation] FAR Part 31 and verify that the labor rates used are those specified in the contract for the period covered by the invoice/voucher. If a disagreement or question exists over indirect cost rates, hours, costs incurred, or contractor compliance with contract requirements, notify the contractor that payment is being withheld pending resolution of the disagreement.
3. Time-and-materials or labor-hours – If the invoice/voucher is labor-hour or time-and-materials, check the materials costs and labor hours on the invoice/voucher to ascertain whether they reasonably appear to reflect those incurred in performing the work. Review the materials costs for reasonableness, allocability and allowability in accordance with FAR Part 31 and verify that the labor rates used are those specified in the contract for the period covered by the invoice/voucher. Ensure that materials charges do not contain labor costs (e.g., under a subcontract) for any of the labor categories specified in the contract. Verify that the contractor did not increase labor rates for overtime, unless the contract included overtime rates and the overtime was authorized by the contracting officer. Check that the contractor substantiated the invoice/voucher (as required by FAR clause 52.2327) by evidence of actual payment, individual daily job timecards, or other substantiation approved by the contracting officer. If a disagreement or question exists, promptly notify the contractor.
5. Arithmetical errors – If errors exist, promptly notify the contractor.

Costs Not Preapproved When Required

In 2 of the 10 contracts reviewed, invoices and supporting documentation detailed costs that were not pre-approved when required. These costs included purchases of government property and charges for consultants.

In one contract, government property totaling \$5,249 was included on invoices paid in FY 2005, but contract file documentation did not include preapproval of these purchases as required. **(RN95127001)** Section G.3 of the contract, “Additional Requirements for Control of Government Property,” states,

The contractor shall request written authorization from the contracting officer before acquiring any contractually necessary property to which the Government will have title. In addition the request shall include complete descriptions of all individual items which exceed \$1,000 in cost . . .

Each of the items purchased exceeded \$1,000 in cost and should have been preapproved by the CO according to the terms above. CAM staff stated they were not aware the contractor had purchased any property. However, the supporting documentation submitted with the invoices clearly indicated the purchase of these items. The COR was aware these purchases were being made, but the COR did not enforce the preapproval requirement. The COR was not familiar with the government property clause in the contract which required preapproval.

Another contract included charges for consultants that were not preapproved as required. **(ED01CO0012)** Specifically, 12 of 21 invoices for the year included a total of \$184,376 in charges for 64 different consultants that were not preapproved as required. Clause H.7 of the contract, “Consultant Services and Consent,” states,

The Contractor shall obtain the consent of the Contracting Officer prior to using any consultant on this contract. The Contractor shall determine whether any consultant that is used has in effect an agreement with another Federal agency for similar or like services and, if so, shall notify the Contracting Officer.

The contract file did not include any documentation to support approval of these consultants. As a result of our inquiries, CAM staff obtained a spreadsheet from the contractor that included 34 consultant names and amounts charged to the contract. However, this spreadsheet did not document the consent of the CO. The CS was subsequently able to locate supporting documentation for 9 of 73 consultants listed on the invoices but not for the remaining 64 consultants.

Application of Incorrect Direct Labor or Indirect Cost Rates

We found Department staff did not note 2 of the 10 contractors did not apply correct labor and/or indirect rates on invoices during the year. In one contract, the contractor did not apply the correct labor rates on 6 of the 12 invoices for the year. **(RN95127001)** In four invoices, the contractor applied a rate of \$235.00 per hour for one category, rather than the specified rate of \$273.21 per hour, for 183 hours. The contractor was underpaid \$6,992 in direct labor for this

error. On two additional invoices, the contractor charged 312 hours at \$51.81 per hour, or a total of \$16,165, for a labor category that was not listed at all in the contract.

In another contract, we found the overhead rate on 3 of the 14 invoices did not match the provisional overhead rate of 19.86% that was specified in the contract. **(ED02CO0023)** During the first three months of FY 2005, the contractor applied a rate of 16.26% to direct labor on three invoices. Thereafter, nine invoices during the year included the provisional overhead rate of 19.86%. We could not verify the overhead rate for two invoices that did not include supporting documentation. The contract did not include documentation to support the lower overhead rate of 16.26% on the three invoices. Therefore, we could not verify costs applied to determine any under/overpayment to the contractor.

The CS stated when the contract was first awarded it did not have a provisional rate agreement and the Department partnered with the Defense Contract Audit Agency in order to establish an agreement. The CS did not know whether the provisional rate of 19.86% was ever officially approved. The CS stated there should be documentation in the official files verifying the specific approved overhead rate that should have been used. However, the only documentation in the files was for the provisional rate agreement specifying a rate of 19.86%.

Insufficient Information and/or Supporting Documentation

Information on and/or submitted with invoices for 2 of 10 contracts reviewed was not sufficient to allow CAM staff or the COR to adequately review the appropriateness of charges. Contract terms for both contracts included the following in an attachment referenced in Section G.1, "Invoice and Contract Financing Request Submission," Section C (emphasis in original):

The Government has the responsibility to pay the invoice, *after* determining which of the *costs* are reasonable, allocable, and allowable. To make this determination we must receive a detailed invoice with the *costs* broken out.

For one contract, line items included on 9 of the 14 invoices paid during FY 2005 were not sufficiently detailed to allow CAM staff and the COR to verify whether the overhead applied was correct. **(ED02CO0023)** The contractor presented all other direct costs (ODC) as one lump sum, but overhead was not applicable to all ODC. As a result, Department staff could not verify whether the correct overhead rate was used, and whether overhead was only applied to applicable costs. Based upon our inquiries, CAM staff stated future invoices would include detail on overhead-bearing ODC, and non overhead-bearing ODC. CAM staff and the COR were not familiar with this issue, and therefore had not attempted to verify these costs on prior invoices.

The indirect cost agreement for another contract included a provisional rate of 12.8% dated November 2004, effective through November 2005. **(ED01CO0012)** According to the agreement, the rate was to be applied to,

Total direct costs less items of equipment, alterations and renovations, stipends and the portion of each competitive bid sub-award in excess of \$25,000 regardless of the period covered by that subaward.

The invoices submitted by the contractor did not detail the calculation of the indirect rate, nor disclose what rate was being applied. The invoices and supporting documentation also did not provide sufficient detail to determine whether any costs were excluded from the rate calculation (e.g. equipment, stipends, etc.).

We requested assistance from the CS to determine how the rates were applied, and found she was not familiar with how the rate was to be charged or how the calculations on the actual invoices were made, indicating that she had not verified the amounts charged on the invoices. We also discussed this issue with the COR who stated that he did not verify the indirect rates on the invoices. (See Attachment 2 for this contract for further information on the various rates charged on the invoices reviewed.)

CAM staff and the CORs did not fulfill their responsibilities to ensure payments to contractors were appropriate. The process followed for reviewing invoices did not detect the issues noted in our review. As a result, inaccurate and unsupported payments were made to the contractors. In some cases, the contractors underbilled and were underpaid because Department staff did not note errors with the invoices. In other cases, the contractors overbilled and were overpaid for items that had not been preapproved, for items that were not supported, or for inaccurate rate applications. Without a vigorous invoice review process to ensure the contractors are complying with contract terms and requirements, the Department lacks assurance that payments are proper, its interests are protected, and contractors are dealt with fairly.

Issue 4 – Department Staff Did Not Issue and/or Sign COR Appointment Letters Timely

For three contracts, COR appointment letters were not issued by the CO or signed and/or returned by the COR timely. Directive Section VI.C.2-3 states the CO,

2. Ensures that a COR is designated for each contract.
3. Issues to the COR for each contract a memorandum outlining the COR's basic contract monitoring responsibilities and limitations, and explains this information to the extent judged appropriate. COR appointment letters are issued not later than seven (7) days from the date of contract award.

Directive Section VI.E.1 states the COR

Ensures receipt of appointment memorandum from CO by no later than seven (7) days from the date of award. Reads, signs and returns one copy of the original memorandum to the CO for inclusion in the official contract file within ten (10) days of receipt of the memorandum.

Specifically, we noted the following:

- An appointment letter dated August 1, 2003, was not signed by the COR until November 17, 2003. (**ED01CO0010**)

- Another contract was awarded on December 13, 2000, and the appointment letter for the original COR was dated May 2001. An appointment letter was not in the contract file for the current COR. **(ED01CO0011)**
- One COR stated she was assigned to the contract in January of 2004. However, the COR Appointment Letter was dated March 30, 2005, more than a year later. **(ED02CO0034)**

The COR appointment memorandum reminds the COR of his/her responsibilities and limitations in the monitoring process. The memorandum includes such things as training and certification requirements, monitoring and communication responsibilities, and actions the COR does not have the authority to perform. Without issuing and signing these documents timely, the CO does not have assurance that the COR understands the extent and limitations of his/her responsibilities and authority.

Summary

Improvements were needed in monitoring by CAM and/or IES staff for each of the 10 contracts reviewed. Department staff were not always familiar with regulations, policies and procedures, and/or were not always familiar with contract terms and conditions. The Department's process for documenting receipt and acceptance of deliverables needs improvement to fully document contractor performance. CORs were not always aware of the requirement to provide written evaluations of contractor-submitted reports and did not provide such evaluations in any of the contracts reviewed. Department staff did not adequately review invoices to ensure amounts charged were appropriate. Finally, COs did not ensure COR appointment letters were issued and/or signed timely.

As a result, the Department lacks assurance contractors are adhering to contract requirements and the Department is receiving the services for which it contracted. The Department is not able to document whether all deliverables, including contractor reports, were received, were on time, met contract requirements, and were formally accepted. Without COR evaluations of contractor-provided reports, the CO is not kept informed of contract activity and may not be aware of developing issues. Inadequate invoice review resulted in inappropriate or unsupported payments. By not enforcing contracts requirements, the Department's interests may not be protected and contract terms may not be enforceable. Untimely issuance and/or signoff of COR appointment memoranda could result in confusion over the responsibilities and limitations of the COR's duties.

In May 2005, OCFO implemented a policy to require that contract monitoring plans be developed for contracts.³ In December of 2005, the contracting staff was notified that contract monitoring plans for existing contracts must be established by January 31, 2006. At the time of our fieldwork, these plans were still being developed. However, as of September 2006, contract monitoring plans had been implemented for the six contracts reviewed that were still active.

³ OCFO Procedure, CO-111: *Writing and Implementing a Contract Monitoring Plan*, May 31, 2005.

Recommendations:

We recommend that the Chief Financial Officer and Director, Institute for Education Services, take actions to:

- 1.1 Develop and implement contract monitoring plans for all existing IES contracts. Ensure the plans specifically include areas to address the deficiencies noted in this report related to tracking deliverable receipt and acceptance, written evaluations of contractor-submitted reports, invoice review, and responsibilities and limitations of the CORs' duties.
- 1.2 Direct CAM and IES staff to work together to develop and/or review the plans to ensure clear communication between the CO, CS, and COR on the requirements of each contract, the means by which the requirements will be monitored, and who is responsible for that monitoring.
- 1.3 Develop and implement a process to fully document receipt and acceptance of deliverables. Ensure CORs provide written recommendations of deliverable acceptance/rejection to the CO in order to prevent constructive acceptance and to protect the Department's interests.
- 1.4 Provide training to CAM and IES staff responsible for monitoring IES contracts to ensure staff are aware of and adhere to regulations, policies and procedures that apply to their responsibilities as contract managers. Specifically include in the training the areas noted in this report.
- 1.5 Ensure COR appointment letters are issued timely by the CO, and signed and returned timely by the COR. Review all IES contracts to ensure that all current CORs have received an appointment letter and that a signed copy is included in the contract file.
- 1.6 Resolve, as appropriate, the specific invoice/payment issues noted in this review for contracts ED01CO0012, ED02CO0023, and RN95127001. As needed, modify the contracts or billing terms to ensure that adequate supporting documentation is provided to allow review and validation of invoice amounts, processes are implemented to review and approve equipment purchases or consultants, and labor and indirect rates are formally established and accepted. As needed, require contractors to resubmit billings or adjust invoices to correct prior under- or overpayments.

OCFO/IES Response:

In a combined response to the draft report, the OCFO and IES concurred with the finding and recommendations, and presented proposed corrective actions for implementing the recommendations. The OCFO stated that contract monitoring plans had been developed for all IES contracts, and the plans addressed the deficiencies noted. The response stated that OCFO/CAM and IES staff collaborated to develop the contract monitoring plans, and all CORs will be requested to sign the contract monitoring plan as affirmation that they understand its content.

OCFO stated it is exploring available tools to implement Department-wide for receipt and acceptance of deliverables. OCFO stated it will evaluate current technology available in EDCAPS, as well as other forms of electronic documentation and tracking and proposes to have a solution for use by March 31, 2007.

OCFO stated it will schedule a training session at the IES sites to ensure staff are aware of and adhere to regulations, policies and procedures that apply to their responsibilities. OCFO/CAM staff will conduct the training jointly with senior IES officials for all CORs. The training will be scheduled in February 2007, will be mandatory, and will cover the findings outlined in the audit.

OCFO stated that all files have appropriate COR appointment letters, and it commits to resolving the specific invoice/payment issues noted for the three contracts by January 31, 2007.

See Attachment 3 to this report for the full text of the combined response.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of our audit were to determine whether the Department's contract monitoring process ensures (1) contractors adhere to the requirements of the contract, and (2) the Department receives the products and services intended. To accomplish our objective we performed a review of internal control applicable to the process for monitoring contracts within the Department. We interviewed OCFO and IES staff to obtain an understanding of the process. We evaluated prior audits and reviews relating to the contract monitoring process to determine possible vulnerabilities and any areas that required audit follow-up. We reviewed requirements in the FAR and Department policy and procedures related to the contract monitoring process. We reviewed contract files in CAM and those maintained by the COR, and other related materials that supported the contract monitoring process for a sample of contracts as further described below.

We focused our review on contracts that were active during the period October 1, 2004, through September 30, 2005. We obtained a listing of contract payments for FY 2005 for all principal offices from OCFO staff. The listing was extracted from the Financial Management Support System (FMSS), a component of the Education Centralized Automated Processing System (EDCAPS). In order to focus our review on contracts with significant activity that were most likely to require active contract monitoring, we refined this list to eliminate payments that represented interagency, purchase orders, and other types of payments, and those that totaled less than \$100,000 for a particular contract the year. In total, we identified 9,080 payments to 519 different contracts that totaled \$1,474,385,044 for the year.

We determined that IES had the highest number of payments of any PO (1,705 or 19 percent), the highest number of active contracts (142 or 27 percent), and the second highest amount of payments during the year (\$351,921,139 or 24 percent). We selected IES for review because it represented a significant number of the active contracts and amount of payments during the scope period, and to follow up on the prior audit recommendations and corrective actions.

We selected for further review the 10 IES contracts with the highest amount of contract payments for the year. These contracts totaled \$193,833,367 or 55 percent of the total \$351,921,139 total payments to IES contracts. These contracts were judgmentally selected for review to provide coverage of the highest amount of contract payments. See Attachment 2 for a list of the contracts selected for review, and the number and dollar value of FY 2005 payments to those contracts.

During our review, we relied on computer-processed data obtained from EDCAPS/FMSS representing contract payments for FY 2005. To assure ourselves of the completeness of this data, we compared the contracts listed with payments to lists of active contract awards from CAM's website as of November 2004 and November 2005 -- a total of 996 unduplicated items. We found that 629 of the active awards as of those two dates were included in the list of contracts with payments during FY 2005. For the 367 contracts in the two lists from CAM's website that were not included in the listing of contract payments, we found that 251 were multiple award task orders or blanket purchasing agreements under which separate orders would be placed. These awards would not have payments. Of the remaining 116 awards, 3 were small purchases and not considered contracts for the purposes of our review. Payments under these purchases in FY 2005 were not material. All other contracts were either awarded after or ended before FY 2005, or no payments were made under these contracts during FY 2005. Based on this analysis, we determined the listing of contract payments was complete for the purposes of our audit.

To evaluate the accuracy of the information contained in the contract payments listing received from OCFO for the 10 contracts reviewed, we confirmed the payment amounts with the hard copy invoices in the contract files, and with payment information included in the Contract Purchasing and Payment System (CPSS), another component of EDCAPS. We did not note any exceptions. Based on these analyses, we determined the computer-processed data used was sufficiently accurate and reliable for the purposes of our review.

We conducted fieldwork at Department offices in Washington, DC, during the period December 13, 2005, through June 28, 2006. We held an exit conference with OCFO and IES staff on August 30, 2006. Our audit was performed in accordance with generally accepted government auditing standards appropriate to the scope of the review described above.

ADMINISTRATIVE MATTERS

Corrective actions proposed (resolution phase) and implemented (closure phase) by your office will be monitored and tracked through the Department's Audit Accountability and Resolution Tracking System. Department policy requires that you develop a final corrective action plan (CAP) for our review in the automated system within 30 days of the issuance of this report. The CAP should set forth the specific action items, and targeted completion dates, necessary to implement final corrective actions on the findings and recommendations contained in this final audit report.

In accordance with the Inspector General Act of 1978, as amended, the Office of Inspector General is required to report to Congress twice a year on the audits that remain unresolved after six months from the date of issuance.

Statements that managerial practices need improvements, as well as other conclusions and recommendations in this report, represent the opinions of the Office of Inspector General. Determinations of corrective action to be taken will be made by the appropriate Department of Education officials.

In accordance with the Freedom of Information Act (5 U.S.C. § 522), reports issued by the Office of Inspector General are available to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act.

We appreciate the cooperation provided to us during this review. Should you have any questions concerning this report, please call Michele Weaver-Dugan at (202) 245-6941. Please refer to the control number in all correspondence related to the report.

Sincerely,

Helen Lew /s/
Assistant Inspector General for Audit Services

Attachments

Attachment 1: Contracts Included in the Audit

Contract Number	Vendor Name	Number of FY 2005 Payments	Total Amount of Payments
ED01CO0010	Brown University	14	\$ 9,506,651
ED01CO0011	North Central Regional Education Laboratory	15	\$ 10,874,114
ED01CO0012	Western Regional Educational Laboratory	17	\$ 8,440,929
ED01CO0039/0007	Mathematica Policy Research	18	\$ 8,040,604
ED01CO0093/0004	ABT Associates	14	\$ 9,284,632
ED01CO0120	Westat	12	\$ 11,087,880
ED02CO0023	Educational Testing Service	21	\$ 19,834,363
ED02CO0034	Westat	15	\$ 53,639,562
ED02CO0035	NCS Pearson	38	\$ 41,914,965
RN95127001	American Institutes for Research	41	\$ 21,209,667
Total number/amount of FY 2005 payments		205	\$ 193,833,367

Attachment 2: Issues Noted by Contract

ED01CO0010 – Brown University, \$9,506,651⁴

1. ***Department staff did not adequately document receipt of deliverables.*** The COR stated acceptance of deliverables is implied through payment of invoices in CPSS. Upon review, we found the COR did insert comments on the receipt summaries stating whether the deliverables were acceptable or not. However, this method does not adequately document what deliverables were received, when the deliverables were received, whether deliverables were timely, and whether deliverables met all contract requirements.
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The COR stated she makes comments directly on the reports and sends comments to the contractor, but she did not write any formal evaluations.
3. ***Department staff did not issue and/or sign COR appointment letters timely.*** During our review of the contract files, we found that the COR appointment letter dated August 1, 2003, was not signed by the COR until November 17, 2003.

ED01CO0011 – North Central Regional Education Laboratory, \$10,874,114

1. ***Department staff did not adequately document receipt of deliverables.*** The CS stated acceptance of deliverables is implied through payment of invoices in CPSS. Upon review, we found the COR did insert comments on the receipt summaries stating all deliverables were on time and acceptable. However, this method does not adequately document what deliverables were received, when the deliverables were received, and whether deliverables met all contract requirements.
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The CS stated formal evaluations of the quarterly reports were not completed, although informal comments may be made. The COR provides comments to the contractor, not the CO.
3. ***Department staff did not issue and/or sign COR appointment letters timely.*** The only COR appointment letter found in the contract files was for a former COR, appointed until May 8, 2001, when the contract was awarded in December of 2000. The contract files did not include a copy of the appointment letter for the current COR, although he was appointed in approximately December 2004. Nor could the COR produce a copy of his appointment letter.

⁴ Amounts listed represent the FY 2005 payments made under each contract.

ED01CO0012 – Western Regional Educational Laboratory, \$8,440,929

1. ***Department staff did not adequately document receipt of deliverables.*** There was no formal acceptance of deliverables noted in the contract files. The COR stated acceptance of deliverables is implied through the payment of invoices in CPSS. However, we found recommendation of acceptance of deliverables in CPSS was not indicated on 4 out of 21 receipt summaries for this contract (invoices #72, #73, #74, and #87).
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The COR stated he did not prepare individual written evaluations of reports received, but at the end of the year there was a past performance evaluation was completed.
3. ***Department staff did not detect inappropriate charges on invoices prior to approving payments.***

The contract included charges for consultants that were not preapproved as required. Specifically, 12 of 21 invoices for the year included a total of \$184,376 in charges for 64 different consultants that had not been approved. The contract file did not include any documentation to support approval of these consultants. As a result of our inquiries, CAM staff obtained a spreadsheet from the contractor that included 34 consultant names and amounts charged to the contract. However, this spreadsheet did not document the consent of the CO, nor include all consultants noted. The CS was able to locate supporting documentation for 9 of total 73 consultants listed on the invoices, but could not locate approval documents for the remaining 64 consultants. The CS stated it was difficult to locate the supporting documentation based on the fact that the contract has been going on a long time, and CAM had moved to a different building during that time period.

In addition, we found the indirect cost agreement for this contract included a provisional rate of 12.8% dated November 14, 2004, effective through November 2005. According to the agreement, the rate was to be applied to,

Total direct costs less items of equipment, alterations and renovations, stipends and the portion of each competitive bid sub-award in excess of \$25,000 regardless of the period covered by that subaward.

The invoices submitted by the contractor did not detail the calculation of the indirect rate, nor disclose what rate was being applied. The invoices and supporting documentation also did not provide sufficient detail to determine whether any costs were excluded from the rate calculation (e.g. equipment, stipends, etc.). By dividing the indirect costs by the subtotal direct costs on the invoices, we determined the following indirect rates were applied to the invoices paid in FY 2005 after the rate agreement went into effect:

<u>Performance Month</u>	<u>Rate</u>	<u>Performance Month</u>	<u>Rate</u>
December 2004	4.0%	May 2005	12.4%
January 2005	11.6%	June 2005	12.3%
February 2005	12.7%	July 2005	12.5%
March 2005	12.6%	August 2005	10.5%
April 2005	12.3%		

We requested assistance from the CS to determine how the rates were applied, and found she was not familiar with how the rate was to be charged or how the calculations on the actual invoices were made, indicating she had not verified the amounts charged on the invoices. We also discussed this issue with the COR who stated he did not verify the indirect rates on the invoices.

ED01CO0039/0007 – Mathematica Policy Research, \$8,040,604

1. ***Department staff did not adequately document receipt of deliverables.*** The COR stated she would send comments to the contractor to ensure the deliverable is adequate. This represents an inappropriate practice, due to the fact that only a CO has the authority to accept or reject deliverables.
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The COR confirmed she did not send written evaluations of monthly progress reports to the CO for this contract.

ED01CO0093/0004 – ABT Associates, \$9,284,632

1. ***Department staff did not adequately document receipt of deliverables.*** The COR stated she sent comments back and forth to the contractor until there were no more issues regarding the deliverable received. This represents an inappropriate practice, due to the fact that only a CO has the authority to accept or reject deliverables.
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The COR she was not aware of the policy regarding written evaluations of progress reports received.

ED01CO0120 – Westat, \$11,087,880

1. ***Department staff did not adequately document receipt of deliverables.*** The COR stated she provides comments to the contractor regarding changes needed to deliverables until she has no other feedback. This represents an inappropriate practice due to the fact that only a CO has the authority to accept or reject deliverables.
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The COR stated she was not aware of any policy for

preparing written evaluations of deliverables such as the monthly reports. The COR stated she sends comments to the contractor for any issues she may have. This represents an inappropriate practice due to the fact that only a CO has the authority to accept or reject deliverables.

ED02CO0023 – Educational Testing Service, \$19,834,363

1. ***Department staff did not adequately document receipt of deliverables.*** There was no formal acceptance of deliverables noted in the contract files. The CS stated acceptance of deliverables is implied through the payment of invoices in CPSS. However, we found recommendation of acceptance of deliverables in CPSS was not indicated on 5 out of 14 receipt summaries for this contract, (invoices #26, #27, #28, #31, and #34).
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The COR stated he did not prepare written evaluations of the reports. He said he gathers comments from a number of reviewers, which they discuss along with the authors (contractors) in a collaborative process to agree to the changes that should be made for the next draft. The COR stated the comments do not go to the CO, as they are more in the nature of internal working documents.
3. ***Department staff did not detect inappropriate charges on invoices prior to approving payments.*** We found the overhead rate on 3 of the 14 invoices did not match the provisional 19.86% overhead rate specified in the contract. During the first three months of FY 2005, the contractor applied a rate of 16.26% to direct labor on three invoices. Thereafter, nine invoices during the year included the provisional overhead rate of 19.86%. We could not verify the overhead rate used for two additional invoices that did not include supporting documentation. The contract did not include documentation to support the lower overhead rate of 16.26% on the three invoices. Therefore, we could not verify costs applied to labor for these invoices totaling \$569,549. In addition, the contract did not include documentation to support whether or not the provisional rate of 19.86% was ever approved.

CAM staff and the COR did not note this issue in their reviews of the invoices. The CS stated when the contract was first awarded it did not include a provisional rate agreement. The Department partnered with the Defense Contract Audit Agency in order to establish an agreement. The CS did not know whether the provisional rate of 19.86% was ever officially approved. The CS stated there should be documentation in the official files verifying the specific approved overhead rate that should have been used. However, the only documentation in the files was for the provisional rate agreement specifying a rate of 19.86%. In addition, the CS stated this specific issue occurred before she was the CS for the contract, so could not assist us other than by reviewing the documentation in the contract files.

In addition, for this contract, we found line items included on 9 of the 14 invoices paid during FY 2005 were not sufficiently detailed to allow CAM staff and the COR to verify whether the overhead applied was correct. The contractor presented all ODC as one lump sum, but overhead was not applicable to all ODC. As a result, Department staff could not verify whether the correct overhead rate was used, and whether overhead was

only applied to applicable costs. Based upon our inquiries, CAM staff stated future invoices would include detail on overhead-bearing ODC, and non overhead-bearing ODC. CAM staff and the COR were not familiar with this issue, and, therefore, had not attempted to verify these costs on prior invoices.

ED02CO0034 – Westat, \$53,639,562

1. ***Department staff did not adequately document receipt of deliverables.*** The COR stated she never communicated to the CS/CO regarding acceptance of deliverables. We found brief comments in CPSS on what deliverables had been received, but these comments were not adequate to document whether deliverables were received on time, and whether the deliverables met all contract requirements.
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The COR stated she provided written evaluations of progress reports in CPSS. We found the comments in CPSS did not meet requirements for a written evaluation of reports received.
3. ***Department staff did not issue and/or sign COR appointment letters timely.*** The COR stated she was assigned to the contract in January of 2004. However, we found the COR Appointment Letter was dated March 30, 2005, more than a year later.

ED02CO0035 – NCS Pearson, \$41,914,965

1. ***Department staff did not adequately document receipt of deliverables.*** There was no formal acceptance of deliverables noted in the contract files. The COR stated acceptance of deliverables is implied in CPSS when invoices are paid. Upon review, we found the COR did insert a statement on all 13 receipt summaries recommending payment based on the deliverables being on schedule and within budget. However, this methodology does not adequately document whether the deliverables met all contract requirements.
2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The CORs stated he sent comments to the contractor in order to discuss issues regarding the reports. This represents an inappropriate practice due to the fact that only a CO has the authority to accept or reject deliverables.

RN95127001 – American Institutes for Research, \$21,209,667

1. ***Department staff did not adequately document receipt of deliverables.*** There was no formal acceptance of deliverables noted in the contract files. The CS stated acceptance of deliverables is implied through the payment of invoices in CPSS. However, we found recommendation of acceptance of deliverables in CPSS was not indicated on all 12 receipt summaries for this contract. We noted comments on the receipt summaries stating “invoices processed” and the date. These statements do not adequately document

whether deliverables were received, were received on time, and whether the deliverables met all contract requirements.

We noted one deliverable that did not include statistical data as required by the contract. The CS stated not including the statistical data was not a problem because the monthly reports come in at the same time as the invoices, which show charges for personnel. However, the COR stated the monthly reports do not come in at the same time of the invoices. No change had been made to the contract to eliminate the requirement for the statistics on the monthly report. This deliverable did not comply with contract requirements.

2. ***The COR did not prepare written evaluations of contractor-submitted reports and provide the evaluations to the CO.*** The CO stated no written evaluations were prepared for the monthly reports for this contract.
3. ***Department staff did not detect inappropriate charges on invoices prior to approving payments.*** The Department paid for equipment totaling \$5,249 without preapproval. Each of the items purchased exceeded \$1,000 in cost and should have been preapproved by the contracting officer according to the contract terms. CAM staff stated they were not aware that the contractor had purchased any property. However, the supporting documentation submitted with the invoices clearly indicated the purchase of these items. The COR was aware that these purchases were being made, but did not enforce the preapproval requirement. The COR was not familiar with the government property clause in the contract which required preapproval.

In addition, we found Department staff did not note the contractor applied incorrect labor on invoices during the year. The contractor applied incorrect labor rates on 6 of the 12 invoices for the year. On four invoices, the contractor applied a rate of \$235.00 per hour for one category, rather than the specified rate of \$273.21 per hour, for 183 hours. The contractor was underpaid \$6,992 in direct labor for this error. On two additional invoices, the contractor charged 312 hours at \$51.81 per hour, or a total of \$16,165, for a labor category that was not listed at all in the contract.

The contract included a labor rate schedule in Modification 6. The CS stated that this schedule was the only rate schedule that applied to the invoice period under review, and confirmed the rates charged on the invoices were incorrect. However, neither CAM staff nor the COR noted these inaccuracies during review of the invoices.



UNITED STATES DEPARTMENT OF EDUCATION

WASHINGTON, D.C. 20202-_____

NOV 20 2006

MEMORANDUM

TO: Nancy Brown, Acting Director
Operations Internal Audit Team
Office of Inspector General

FROM: Lawrence Warder
Chief Financial Officer

Grover J. Whitehurst, Director
Institute of Education Sciences

SUBJECT: DRAFT AUDIT REPORT: Controls over Contract Monitoring for IES Contracts, Control Number ED-OIG/A19G0004

Thank you for your draft Office of Inspector General (OIG) audit report, *Controls over Contract Monitoring for IES Contracts*, ED-OIG/A19G0004, dated October 11, 2006. The Office of the Chief Financial Officer (OCFO)/Contracts and Acquisitions Management (CAM) recognizes that the Department faces challenges in contracts management, and we are continuing our efforts to identify process improvements and establish controls to provide better monitoring and oversight of the Department's portfolio of contractor resources. We have made strides over the last 2 years to address some of these challenges. In Fiscal years 2005 and 2006, OCFO/CAM developed and sponsored an agency-wide training program that reinforced the Department's contracting processes, laws, and regulations to senior managers, contracting personnel, and relevant program office personnel; developed procedures for writing contract monitoring plans; and updated and distributed other pertinent contract procedural documents to improve controls and efficiencies. However, OCFO/CAM acknowledges that more work is needed.

In the OIG draft report, you concluded from your sample, that OCFO/CAM and the Institute for Education Sciences (IES) staff did not adequately document receipt and acceptance of deliverables; that IES Contracting Officer Representatives (CORs) did not prepare written evaluations of contractor-submitted reports; that OCFO/CAM and IES staff did not detect inappropriate charges on invoices prior to approving payments; and, that OCFO/CAM and IES CORs did not timely issue and sign COR appointment letters. Additionally, the audit noted that contract monitoring plans were missing in several of the contracts. OCFO and IES have no comments on the objective, scope, methodology or findings in this report. We concur with your finding and related issues and



recommendations and present the following proposed corrective actions for implementing the OIG recommendations.

Finding – Improvements Were Needed in Contract Monitoring for IES Contracts

OIG Recommendation 1.1: *Develop and implement contract monitoring plans for all existing IES contracts. Ensure the plans specifically include areas to address the deficiencies noted in this report related to tracking deliverable receipt and acceptance, written evaluations of contractor-submitted reports, invoice review, and responsibilities and limitations of the CORs' duties.*

OCFO/IES Proposed Corrective Action: Contract monitoring plans have been developed and are now in place for all existing IES contracts. The contract monitoring plans address all noted deficiencies.

OIG Recommendation 1.2: *Direct CAM and IES staff to work together to develop and/or review the plans to ensure clear communication between the CO, CS, and COR on the requirements of each contract, the means by which the requirements will be monitored, and who is responsible for that monitoring.*

OCFO/IES Proposed Corrective Action: OCFO/CAM and IES staff collaborated to develop the contract monitoring plans. Each contract monitoring plan was discussed during the collaboration. All CORs however, will be requested to sign the contract monitoring plan as affirmation that they understand its content by no later than December 29, 2006.

OIG Recommendation 1.3: *Develop and implement a process to fully document receipt and acceptance of deliverables. Ensure CORs provide written recommendations of deliverable acceptance/rejection to the CO in order to prevent constructive acceptance and to protect the Department's interest.*

OCFO/IES Proposed Corrective Action: OCFO/CAM is exploring available tools to implement Department-wide for receipt and acceptance of deliverables. We will evaluate current technology available in EDCAPS, as well as other forms of electronic documentation and tracking. We propose to have a solution available for use by March 31, 2007.

OIG Recommendation 1.4: *Provide training to CAM and IES staff responsible for monitoring IES contracts to ensure staff are aware of and adhere to regulations, policies and procedures that apply to their responsibilities as contract managers. Specifically include in the training the areas noted in this report.*

OCFO/IES Proposed Corrective Action: OCFO/CAM will schedule a training session at the IES sites to ensure staff are aware of and adhere to regulations, policies and procedures that apply to their responsibilities. OCFO/CAM staff will conduct the training jointly with senior IES officials for all CORs. The training will be mandatory,

and will cover the findings outlined in the audit. The training session will be scheduled in February 2007.

OIG Recommendation 1.5: *Ensure COR appointment letters are issued timely by the CO, and signed and returned timely by the COR. Review all IES contracts to ensure that all current CORs have received an appointment letter and that a signed copy is included in the contract file.*

OCFO/IES Proposed Corrective Action: All files have appropriate COR appointment letters. OCFO/CAM regrets the finding that three appointment letters contained untimely dates.

OIG Recommendation 1.6: *Resolve, as appropriate, the specific invoice/payment issues noted in this review for contracts ED01CO0012, ED02CO0023, and RN95127001. As needed, modify the contracts or billing terms to ensure that adequate supporting documentation is provided to allow review and validation of invoice amounts, processes are implemented to review and approve equipment purchases or consultants, and labor and indirect rates are formally established and accepted. As needed, require contractors to resubmit billings or adjust invoices to correct prior under- or overpayments.*

OCFO/IES Proposed Corrective Action: OCFO/CAM commits to resolving the specific invoice/payment issues noted for the three contracts. OCFO/CAM proposes to have all payment issues resolved by January 31, 2007.

Thank you again for this opportunity to respond. We trust that you will consider this response in the preparation of your final audit report. Should you have any questions, please contact Cynthia Bond-Butler, OCFO/CAM at 245-6221.