



U.S. ENVIRONMENTAL PROTECTION AGENCY

OFFICE OF INSPECTOR GENERAL

# EPA Could Recover More Indirect Costs Under Reimbursable Interagency Agreements

Report No. 12-P-0835

September 19, 2012



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## Abbreviations

EPA	U.S. Environmental Protection Agency
FY	Fiscal Year
G&A	General and Administrative
GAO	U.S. Government Accountability Office
HQ	Headquarters
IA	Interagency Agreement
OCFO	Office of the Chief Financial Officer
OFM	Office of Financial Management
OGC	Office of General Counsel
OIG	Office of Inspector General
RIA	Reimbursable Interagency Agreement
RMDS	Resources Management Directive System
SA	Statutory Authority
SFFAS	Statement of Federal Financial Accounting Standards

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# At a Glance

## Why We Did This Review

Our objectives were to determine the methodology the U.S. Environmental Protection Agency (EPA) uses to calculate indirect cost rates for reimbursable interagency agreements (RIAs), and whether EPA is applying the correct indirect cost rates for selected RIAs.

An interagency agreement is a written agreement between federal, state, or local agencies through which goods or services are provided on a funds-out or funds-in basis. The term funds-in applies to an interagency agreement in which EPA provides goods or services to another agency or to a state or local government and is reimbursed for its expenses.

## This report addresses the following EPA Goal or Cross-Cutting Strategy

- *Strengthening EPA's workforce and capabilities.*

For further information, contact our Office of Congressional and Public Affairs at (202) 566-2391.

The full report is at:  
[www.epa.gov/oig/reports/2012/20120919-12-P-0835.pdf](http://www.epa.gov/oig/reports/2012/20120919-12-P-0835.pdf)

## ***EPA Could Recover More Indirect Costs Under Reimbursable Interagency Agreements***

### What We Found

EPA did not recover \$11 million in indirect costs on funds-in RIAs. Federal entities are required to recognize the full cost of goods and services provided among federal entities; full cost includes both direct and indirect costs. For 54 of 59 RIAs reviewed, EPA did not bill other federal agencies the full amount of indirect costs. This occurred because:

- EPA exempted itself from recovering indirect costs on RIAs awarded under 19 statutory authorities.
- EPA issued policies where indirect costs do not apply to RIAs awarded before the policies were effective nor to any agreement amendments.
- EPA issued policies stating that indirect rates in effect at the time the RIA is negotiated will apply for the life of the RIA.
- Other miscellaneous calculating and billing errors occurred.

We estimated that EPA could have recovered \$11 million in indirect costs based on rates for fiscal years 2010 and 2011. Based on amounts remaining in open agreements, we calculated an additional \$2.5 million could be billed during the remaining project periods. The additional indirect costs recovered could be used to pay for other environmental activities.

### Recommendations and Agency Corrective Actions

We recommend that the Chief Financial Officer revise Agency policy to include indirect costs in all RIAs; revise the rules and policies for future actions to include the ability to recover indirect costs and educate the EPA on the new policies while implementation is in progress; revise Agency policy to require that amendments to all RIAs include indirect costs based on current rates; correct the indirect cost rate billing errors noted; and develop policy and procedures to verify that correct indirect cost rates are used.

EPA agreed with all our recommendations or agreed to take actions that satisfy the intent of the recommendations. The Agency has updated policy to clarify that indirect costs should be included in all RIAs, is correcting billing errors, and plans to develop policy to ensure that correct indirect cost rates are used. Recommendation 4 is unresolved pending receipt of a date to correct billing errors.

### Noteworthy Achievement

EPA centralized interagency agreement activities within two service centers to increase consistency in operations and improve efficiency and effectiveness.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY  
WASHINGTON, D.C. 20460

THE INSPECTOR GENERAL

September 19, 2012

**MEMORANDUM**

**SUBJECT:** EPA Could Recover More Indirect Costs Under  
Reimbursable Interagency Agreements  
Report No. 12-P-0835

**FROM:** Arthur A. Elkins, Jr.

A handwritten signature in black ink, appearing to read "Arthur A. Elkins, Jr.", is written over the printed name.

**TO:** Barbara J. Bennett  
Chief Financial Officer

This is our report on the subject audit conducted by the Office of Inspector General (OIG) of the U.S. Environmental Protection Agency (EPA). This report contains findings that describe the problems the OIG has identified and corrective actions the OIG recommends. This report represents the opinion of the OIG and does not necessarily represent the final EPA position. Final determinations on matters in this report will be made by EPA managers in accordance with established audit resolution procedures.

**Action Required**

In accordance with EPA Manual 2750, you are required to provide a written response to this report within 90 calendar days. You should include a corrective action plan for agreed-upon actions, including milestone dates. Your response will be posted on the OIG's public website, along with our memorandum commenting on your response. Your response should be provided as an Adobe PDF file that complies with the accessibility requirements of Section 508 of the Rehabilitation Act of 1973, as amended. The final response should not contain data that you do not want to be released to the public; if your response contains such data, you should identify the data for redaction or removal. In addition to providing us with a paper copy of your response, please e-mail a Microsoft Word version to [curtis.paul@epa.gov](mailto:curtis.paul@epa.gov) and [hiatt.margaret@epa.gov](mailto:hiatt.margaret@epa.gov). We have no objections to the further release of this report to the public. We will post this report to our website at <http://www.epa.gov/oig>.

If you or your staff has any questions regarding this report, please contact Paul Curtis at (202) 566-2523 or Meg Hiatt at (513) 487-2366.

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## Purpose

With the Administration's current focus on reducing the federal budget deficit, we performed this audit to determine whether the U.S. Environmental Protection Agency (EPA) was recovering all appropriate indirect costs related to reimbursable interagency agreements (RIAs). Our objectives were to determine:

- The methodology EPA uses to calculate indirect cost rates for RIAs, including the source of data used and composition of rates.
- Whether EPA is applying the correct indirect cost rates for selected RIAs.

## Background

An interagency agreement (IA) is a written agreement between federal, state, or local agencies through which goods or services are provided on a funds-out or funds-in basis. Funds-in refers to an IA through which EPA provides goods or services to another agency or to a state or local government and is reimbursed for its expenses. Under RIAs, EPA uses reimbursable authority provided by the Office of Management and Budget to perform IA activities.

### **Criteria**

The Statement of Federal Financial Accounting Standards (SFFAS) Nos. 4 and 30 establish standards and policies on the recovery of full costs (direct and indirect) for RIAs.

- SFFAS No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, states: "The managerial cost accounting concepts and standards are aimed at providing reliable and timely information on the full cost of federal programs, their activities, and their outputs." SFFAS No. 4 includes standards to determine the full costs of government goods and services and recognize the costs of goods and services provided among federal entities. Full cost is the total amount of resources used to produce outputs (goods or services) and includes direct and indirect costs. SFFAS No. 4 states that a federal entity providing goods or services has the responsibility to provide the receiving entity with information on the full cost of such goods or services either through billing or other advice.
- SFFAS No. 30, *Inter-Entity Cost Implementation*, requires full implementation of the inter-entity cost provision in SFFAS No. 4. By fully implementing the provisions in SFFAS No. 4, this standard requires that: "each entity's full cost should incorporate the full cost of goods and services that it receives from other entities. This standard requires full implementation for reporting periods beginning after September 30, 2008."

## ***Statutory Authorities***

EPA started recovering indirect costs in 2005 for Oil Spill RIAs, in 2008 for Economy Act RIAs, and in 2009 for other cooperation authority RIAs. An Office of General Counsel (OGC) memorandum dated July 26, 2007, indicates that the two types of statutory authorities (SAs) for IAs that EPA uses most often are the Economy Act (31 U.S. Code 1535) and EPA's cooperation authorities, such as Clean Water Act Section 104(b)(2) and Clean Air Act Section 103(b)(2).

The Economy Act is the authority for an IA when one agency acquires goods or services from another federal agency and the performing agency does not have an interest in providing the goods or services, apart from its interest in performing the work for the requesting agency. In contrast, EPA's cooperation authorities generally authorize the Agency to cooperate with other entities, including federal agencies, in a broad range of specified activities.

The cooperation authorities themselves are silent with respect to payments between agencies for these particular types of costs. However, the fact that the cooperation authorities are silent with respect to payments between agencies for these types of costs does not mean that such payments are unauthorized.

The OGC memorandum also refers to other SAs that provide for reimbursement of the Agency's costs. There are statutory authorities that expressly contemplate the use by EPA of another agency's personnel, services, or other resources, referred to as utilization authorities. Certain utilization authorities expressly authorize EPA to pay for the personnel and associated indirect costs, as well as for travel, supplies, and equipment costs directly related to the IA project.

In addition, the memorandum says that "some utilization authorities contemplate the use by EPA of another agency's personnel and associated resources but do not address reimbursement of the other agency." Further, "if EPA did not reimburse the agency providing assistance to EPA, the other agency would be using its appropriation to perform functions under EPA's statutes and would augment the EPA appropriation that supports the activities in question." OGC's opinion is "the silence of the statutes regarding reimbursement does not foreclose reimbursement and, in fact, the better argument is that reimbursement is required."

## ***Responsibilities***

The following offices are responsible for recognizing and recovering indirect costs on RIAs:

- The Office of the Chief Financial Officer's (OCFO's) Office of Financial Management (OFM), Program Costing Staff, computes and disseminates the indirect cost rates.
- Program offices ensure that indirect costs are assessed and negotiated on IAs with other agencies.
- The Interagency Agreement Shared Service Centers review RIAs to ensure the appropriate indirect rates have been negotiated into agreements.
- The Cincinnati Finance Center issues bills to the other agencies for reimbursable direct and indirect costs.

## ***Calculation of Indirect Rates***

EPA calculates separate indirect cost rates for agreements originating in the headquarters (HQ) general and administrative (G&A) offices, headquarters program offices, and each of the 10 regional offices.

Indirect costs are calculated as a percentage of direct costs. For funds-in IA billings, the indirect cost rate is applied to the direct cost portion of the bill. The rates are updated annually and available on the Office of Grants and Debarment website. The Agency has established different cost pools and allocation bases for the different offices to identify the support organizations and their related costs that cannot be associated in a practical manner with a particular IA.

**HQ G&A Rates:** Pool costs include an allocable share of costs for facilities, human resources, and Office of Personnel Management inter-entity costs. Facilities costs are allocated based on the number of full-time equivalents. Human resources and Office of Personnel Management inter-entity costs are allocated based on personnel compensation and benefits costs. The pools also include depreciation costs incurred by these HQ offices, and HQ administrative and management costs charged to each of these offices. The allocation base used to distribute the HQ indirect cost pool to benefitting cost objectives is calculated by subtracting the HQ indirect cost pool from total Agency costs.

**HQ Program Office Rates:** Pool costs include the three components included in the HQ indirect cost pool as described above, and a separate program office component added for each office. This component is comprised of the administrative costs for each of the program offices for which rates are computed. For example, the Office of Solid Waste and Emergency Response cost pool is comprised of the HQ indirect cost pool, plus the administrative costs of the Office of Solid Waste and Emergency

Response. The allocation base used to distribute the HQ program offices' indirect cost pool to benefitting cost objectives is calculated by subtracting the HQ indirect cost pool, excluding the administrative costs of the respective program office, from total Agency costs.

**Regional Program Office Rates:** Pool costs consist of regional administrative management and support expenses incurred by each region, and an allocable share (by region) of nationwide costs for facilities and human resources. Nationwide costs are those costs that benefit all organizations, including regional offices. Facilities costs are allocated based on the number of full-time equivalents. Human resource costs are allocated based on personnel compensation and benefits costs, and a share of the HQ non-program office costs (i.e., HQ G&A office costs) are allocated to each region by applying the HQ indirect cost rate to total regional costs. National management and support costs are primarily comprised of those costs incurred by HQ non-program offices. The allocation base used to distribute the entire regional indirect cost pool to benefitting cost objectives is equal to total regional non-G&A costs.

## **Noteworthy Achievement**

EPA centralized IA activities within two service centers to increase consistency in operations and provide a more streamlined, efficient, and effective performance of IA functions.

## **Scope and Methodology**

We conducted our audit from January 11, 2012, through June 11, 2012, 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 conclusions based on our audit objectives.

We reviewed EPA policies and laws and regulations concerning full costing, and the ability to recover expenses under IAs. We performed a Compass Data Warehouse Accounts Receivable Query for fiscal years (FYs) 2010 and 2011 using the following reporting categories:

- 01-Reimbursable IAs (Direct Costs only)
- 17-Reimbursable IAs (Full Cost IAs)
- 56-Oil Spill Indirect Costs
- 57-All Other IA Indirect Costs
- 76-DWH (BP) Oil Spill Indirect Costs

The population consisted of 384 IAs totaling \$244,949,192 in billings for FYs 2010 and 2011. We performed a statistical sample of the population to select 59 RIAs totaling \$220,592,610 in direct and indirect costs billed. We interviewed OGC staff on interpreting SAs, and OCFO staff on indirect cost rate policies and developing indirect cost rates. We reviewed spreadsheets and other documents containing the detailed calculations and methodology supporting the reimbursable indirect cost billing rates for funds-in IAs. We reviewed IA files and conducted interviews at the Cincinnati Finance Center and the East and West Interagency Agreement Shared Service Centers.

Appendix A contains further details on our scope and methodology.

## Results of Review

EPA could have recovered over \$11 million in funds-in RIAs billed to other federal agencies. For 54 of 59 RIAs reviewed, EPA did not bill other federal agencies the full amount of indirect costs. SFFAS No. 4 requires federal entities to recognize the full cost of goods and services provided among federal entities; full cost includes both direct and indirect costs. EPA did not recover all indirect costs on RIAs because:

- EPA policies have been interpreted as excluding indirect costs for 15 RIAs awarded under 19 SAs.
- EPA policies requiring indirect costs do not apply to RIAs awarded before the policies were effective nor to any amendments for 23 agreements.
- EPA policies state that indirect rates in effect at the time the RIA is negotiated will apply for the project period of 13 RIAs.
- Other miscellaneous errors occurred in calculating and billing indirect costs, such as applying an incorrect rate.

Based on the unbilled amounts remaining on open agreements, we calculated that an additional \$2.5 million of indirect costs could be billed during the remaining project periods. The additional indirect costs recovered could be used to pay for other environmental activities. Appendix B provides calculations for costs EPA could have recovered.

### ***EPA Did Not Recover Indirect Costs Based on the Statutory Authority***

EPA exempted itself from recovering indirect costs on RIAs awarded under 19 different SAs—such as the Foreign Assistance Act, Homeland Security Act, and Intergovernmental Personnel Act—for which exemptions do not appear warranted. In addition, EPA is not pursuing recovery of indirect costs under the

Robert T. Stafford Disaster Relief and Emergency Assistance Act (Stafford Act).<sup>1</sup> However, the Stafford Act, under which the Federal Emergency Management Agency and EPA operate disaster relief efforts, does not prevent another federal agency from recovering indirect costs. Stafford guidance states that agencies that qualify and may be seeking reimbursement must submit certified annual overhead rate proposals to the Federal Emergency Management Agency for approval prior to billing. Office of Management and Budget Circular A-87 should be used as a guide for this purpose. Indirect cost pools must be defined to explain how the costs are derived and applied. Indirect rates should be negotiated with the Federal Emergency Management Agency annually.

EPA did not recover indirect costs under certain SAs because EPA policies have been interpreted as excluding indirect costs for RIAs awarded under SAs other than the Economy Act or cooperation authorities. However, OCFO's January 26, 2009, Policy Procedure, Resources Management Directive System (RMDS) 2540-13-P1, *Cost Accounting Methods: Agency Indirect Cost Allocation System for Funds-In Interagency Agreements*, says that "EPA's policy is to recover the full cost of IAs, consistent with the authority for a particular IA, the circumstances involved, and the nature of the costs for which payment is made." EPA's exemption of certain statutory authorities stems from OCFO's January 26, 2009, *Policy Technical Interpretation (RMDS 2540-13-T1) Cost Accounting Methods: Full Cost Funds-In Interagency Agreements*, which clarifies the types of funds-in IAs subject to full cost billing by EPA. The technical interpretation clarifies that indirect costs shall be assessed under the Economy Act, and are authorized under the cooperation authorities it lists and the 1996 National Defense Authorization Act. EPA followed its technical interpretation and did not include indirect costs on RIAs with statutory authorities other than those specified. However, OCFO staff stated that no SA should prevent EPA from recovering its full cost under funds-in IAs unless they expressly prohibit recovery of full costs. OGC staff believed there was little if anything in the statutes governing EPA's work with other federal agencies that prevents EPA from recovering all of its costs.

We estimate that EPA could have recovered \$6.4 million on 15 agreements originally exempted based on SA had EPA billed indirect costs using the prevailing indirect cost rates in effect during FYs 2010 and 2011.

### ***EPA Did Not Recover Indirect Costs on RIAs Awarded Before Polices Were Effective***

According to established Agency guidance, EPA started recovering indirect costs in 2005 for Oil Spill RIAs, 2008 for Economy Act RIAs, and 2009 for other cooperation authority RIAs. Prior to these dates, EPA did not recover indirect

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<sup>1</sup> The Act provides "...an orderly and continuing means of assistance by the Federal Government to State and local governments in carrying out their responsibilities to alleviate the suffering and damage which result from such disasters [as floods, earthquakes, etc.]..."

costs on RIAs citing these SAs. On RIAs awarded before these dates that were subsequently amended, EPA also did not recover indirect costs.

RMDS 2540-13.1, *Agency Indirect Cost Allocation System*, requires IAs authorized by the Economy Act negotiated on or after January 28, 2008, to include indirect costs. RMDS 2540-13-P1 and technical interpretation 2540-13-T1 further required funds-in IAs awarded under cooperation authorities on or after January 26, 2009, to include indirect costs. Neither policy applies to funds-in IAs negotiated or awarded before the date of the policies or to any subsequent amendments to the agreements. OCFO staff agreed that the current policy could be revised so that amendments to all RIAs include indirect costs.

Based on our analysis using the prevailing indirect cost rates in effect during FYs 2010 and 2011, we estimate that EPA could have recovered \$3.5 million in indirect costs on 23 agreements awarded before indirect cost policies were effective.

### ***EPA Did Not Recover Indirect Costs Based on Actual Indirect Rates in Effect for the Entire RIA Project Period***

EPA did not recover indirect costs based on the indirect cost rates in effect over the entire project period for some RIAs. Indirect cost rates for funds-in IAs are computed and disseminated by OFM each year. However, EPA applied the indirect cost rate in effect at the time the RIA was negotiated throughout the entire project period of the original award and any amendments.

EPA Policy 2540-13-P1 states that the indirect rates in effect at the time an IA is negotiated will apply for the project period of the IA. However, staff in OGC and OCFO agreed that RIAs, if amended, could be re-negotiated to include current indirect cost rates.

We estimate that EPA could have recovered an additional \$601,774 in indirect costs based on our calculation of the difference between applying the prevailing FYs 2010 and 2011 indirect cost rates and the fixed indirect cost rates in effect at the time of award to the FYs 2010 and 2011 direct costs billed for 13 agreements.

### ***Other Reasons Why EPA Did Not Recover All Indirect Costs***

We found that EPA did not recover over \$584,264 of indirect costs for three RIAs tested. For example, the Agency indirect cost policy for Economy Act IAs became effective January 28, 2008. However, we identified one RIA awarded on February 20, 2008, with the Economy Act cited as the SA, without including applicable indirect costs of about \$376,727. We identified an RIA where EPA did not recover \$6,564 of indirect costs because the Agency used an FY 2009 indirect cost rate instead of the FY 2010 rate. The FY 2010 rate was applicable when the agreement was awarded in FY 2010. We identified another RIA where EPA did

not recover approximately \$200,973 because the Agency charged the direct costs to one agreement and the indirect costs to another agreement. As a result, EPA billed the direct costs in FY 2011 and has not billed any indirect costs.

## Conclusion

EPA could have recovered an additional \$11 million in indirect costs in FYs 2010 and 2011 from other federal agencies. Appendix B provides details, while table 1 shows the overall results of our analysis of amounts that could have been recovered.

**Table 1: Indirect costs that EPA could have recovered**

Reason for not recovering indirect costs	No. of agreements	Estimated amount of indirect costs that could have been recovered
Excluded under 19 SAs	15	\$6,353,482 <sup>a</sup>
Awarded before policy effective	23	3,467,348 <sup>a</sup>
Negotiated rates used over life of RIA	13	601,774 <sup>b</sup>
<b>Subtotal amounts not billed</b>		<b>\$10,422,604</b>
Errors in costs billed	3	584,264
<b>Total</b>	<b>54</b>	<b>\$11,006,868</b>

Source: Office of Inspector General (OIG) analysis

<sup>a</sup> We multiplied the prevailing indirect cost rates in effect during FYs 2010 and 2011 by the amount of direct costs billed during each year to calculate the amount of indirect costs EPA did not recover.

<sup>b</sup> We estimated the amount based on the difference between applying the FYs 2010 and 2011 indirect cost rates to direct costs billed each year and the amount of indirect costs billed for the selected agreements.

Based on the unbilled amounts remaining on the 22 open agreements, we calculated that an additional \$2.5 million of indirect costs could be billed during the remaining project periods. The additional indirect costs recovered could be used to pay for other environmental activities. Appendix C provides our calculation of these future monetary benefits.

## Recommendations

We recommend that the Chief Financial Officer:

1. Revise Agency policy to clarify that indirect costs should be included in all RIAs unless a determination has been made that an SA used for an RIA specifically exempts charging of indirect costs.
2. Revise the rules and policies for future actions to include the ability to recover indirect costs and educate the EPA on the new policies while implementation is in progress.

3. Revise Agency policy to require that amendments to all RIAs include indirect costs based on current indirect rates.
4. Correct the indirect cost rate billing errors.
5. Develop policy and procedures to ensure that the correct indirect costs rates are used.

## **Agency Response and OIG Evaluation**

The Agency agreed with four of the five recommendations. The Agency has updated policy to clarify that indirect costs should be included in all RIAs and require that amendments to all RIAs include indirect costs based on current indirect rates. The Agency is correcting billing errors and plans on developing policy and procedures to ensure that the correct indirect cost rates are used. We concur with the Agency's actions.

The Agency disagreed with the second recommendation that stated EPA should amend RIAs awarded prior to the policy effective dates to include the ability to recover indirect costs, indicating that to do so would be impractical. While we agree that it is impractical to amend all agreements awarded prior to the policy effective dates, our intent was to recommend considering the recovery of indirect costs on any future amendments to existing agreements. In its response the Agency stated it has agreed to revise the rules and policies for future actions and has begun this process. Therefore, the Agency's actions satisfy the intent of our recommendation. Recommendation 4 is unresolved pending receipt of a date to correct billing errors.

## **Status of Recommendations and Potential Monetary Benefits**

RECOMMENDATIONS						POTENTIAL MONETARY BENEFITS (in \$000s)	
Rec. No.	Page No.	Subject	Status <sup>1</sup>	Action Official	Planned Completion Date	Claimed Amount	Agreed-To Amount
1	8	Revise Agency policy to clarify that indirect costs should be included in all RIAs unless a determination has been made that an SA used for an RIA specifically exempts charging of indirect costs.	C	Chief Financial Officer	07/11/12	\$2,524	
2	8	Revise the rules and policies for future actions to include the ability to recover indirect costs and educate the EPA on the new policies while implementation is in progress.	C	Chief Financial Officer	07/11/12		
3	9	Revise Agency policy to require that amendments to all RIAs include indirect costs based on current indirect rates.	C	Chief Financial Officer	07/11/12		
4	9	Correct the indirect cost rate billing errors.	U	Chief Financial Officer		\$584	
5	9	Develop policies and procedures to ensure that the correct indirect cost rates are used.	O	Chief Financial Officer	12/15/12		

<sup>1</sup> O = recommendation is open with agreed-to corrective actions pending  
 C = recommendation is closed with all agreed-to actions completed  
 U = recommendation is unresolved with resolution efforts in progress

## ***Details on Scope and Methodology***

We reviewed EPA's methodology for calculating the indirect costs on RIAs. OFM provided us with electronic spreadsheets containing the detailed calculations and methodology supporting the reimbursable indirect cost billing rates for funds-in IAs. We verified the mathematical accuracy of the indirect cost rates using the FY 2010 rates for HQ G&A offices, HQ program offices, and regional offices. We reviewed OCFO's method for computing both the indirect cost pools and the allocation base used to distribute the indirect costs.

We reviewed OCFO and Grants and Interagency Agreement Management Division policy and technical documents related to funds-in IAs and indirect costs. We also reviewed OGC's memorandum concerning the Reimbursement under Interagency Agreements of Personnel, Indirect, and Travel Costs, and the Interagency Agreement Policies and Procedures Manual. We reviewed standards promulgated by the Federal Accounting Standards Advisory Board.

We conducted interviews with the OGC's Civil Rights and Finance Law Office and with OFM to understand how EPA determines the SAs it cites when entering into IAs, and how the SAs are to be interpreted for full cost recovery. We reviewed selected SAs for language concerning reimbursements of costs between federal agencies.

We generated a list of RIAs with billings from October 1, 2009, through September 30, 2011, using EPA's Compass Data Warehouse Accounts Receivable Query. We used reporting categories that EPA uses in its billing system to properly categorize accounts receivables as a basis for pulling our data. The population consisted of 384 IAs totaling \$244,949,192 in billings for FYs 2010–2011. We performed a statistical sample of the population to select 59 RIAs totaling \$220,592,610 in direct and indirect costs billed.

We reviewed spreadsheets and other documents containing the detailed calculations and methodology supporting the reimbursable indirect cost billing rates for funds-in IAs. We conducted interviews with the Cincinnati Finance Center to determine how indirect costs are billed. We also examined the IAs and amendments maintained by the Cincinnati Finance Center for our 59 sampled RIAs. We conducted interviews about the IA process with staff in the East and West Interagency Agreement Shared Service Centers. We also examined the IA files maintained by the service centers.

To determine the amount of indirect costs EPA could have recovered, we obtained the billed direct costs for FYs 2010 and 2011 and multiplied them by the appropriate indirect cost rates in effect when the agreement was awarded to arrive at the billed indirect costs. We then multiplied the same billed direct costs for FYs 2010 and 2011 by the prevailing FYs 2010 and 2011 indirect cost rates to arrive at the indirect costs that could have been billed. We calculated the difference between the billed indirect costs and the amount that could have been billed to arrive at the difference, which is the amount that could have been billed if the indirect cost rates were adjusted based on the prevailing FYs 2010 and 2011 rates.

To determine the amount of future monetary benefits, we subtracted the total amount billed through September 30, 2011, from the total amount awarded for the 22 active RIAs. We applied the FY 2012 indirect cost rates to the outstanding balances of each agreement. We calculated \$2.5 million in potential future monetary benefits to be obtained if EPA implemented our recommendations.

## Prior Reviews

We researched prior EPA OIG and U.S. Government Accountability Office (GAO) reports related to full costing and the recovery of indirect costs. We noted one pertinent EPA OIG report and one GAO report:

- EPA OIG Audit Report No. 2000-P-0029, “*Follow-up on Headquarters Interagency Agreements*,” September 29, 2000: The audit found that EPA continued to transfer an unknown amount of its resources to other agencies in violation of the Economy Act. EPA was not being reimbursed for the full cost of its work under Economy Act IAs. EPA was not billing other agencies for indirect costs related to performing work or furnishing materials.
- GAO Report RCED 94-196, “*EPA Has Opportunities to Increase Recoveries of Costs*,” September 28, 1994: The report noted that EPA, by excluding some indirect costs including research, development, and site assessment costs, had lost \$2.9 billion of the \$8.7 billion it spent on cleanup actions. Although EPA was considering broadening its definition of recoverable indirect costs, it had not set a date for adopting a final rule. GAO recommended that to ensure maximum recovery of EPA cleanup costs from the parties responsible for these costs, the EPA Administrator should expedite the issuance of the regulation on indirect costs. EPA implemented the recommendation.

## Internal Control Review

In planning and performing our audit, we reviewed management controls related to our audit objectives. We examined EPA’s FY 2011 Federal Managers’ Financial Integrity Act Annual Assurance Letters issued by the regional administrators and assistant administrators for the various EPA programs to identify any weaknesses pertaining to indirect costs applied to RIAs. There were no material weaknesses identified for Office of Administration and Resources Management or OCFO pertaining to indirect cost rates on RIAs.

We examined EPA’s Office of Management and Budget Circular A-123 Appendix A review of internal controls to identify any weaknesses related to indirect costs applied to funds-in (reimbursable) IAs. We did not note any weaknesses related to indirect costs in EPA’s A-123 review of internal controls.

We obtained an understanding of control activities through reviews of EPA’s policies, guidance, and directives related to full costing and indirect costs. We obtained an understanding of the indirect costing process through review of background information, indirect cost rates, and a preliminary research walk-through. We did not review the internal controls over EPA’s

Integrated Financial Management System from which we obtained information, but relied on reviews of systems conducted during the audit of EPA's FY 2011 financial statements. While the Agency has established policies for calculating indirect cost rates and billing indirect costs on IAs, based on our audit, the policies did not provide adequate assurance of compliance with SFFAS for recognizing and billing the full amount of indirect costs for goods and services provided to other federal agencies.

## **Indirect Costs That EPA Could Have Recovered**

<b>Agreement no.</b>	<b>Other agency</b>	<b>Direct costs billed</b>	<b>Indirect costs billed</b>	<b>Indirect costs per OIG<sup>1</sup></b>	<b>Difference (some differences due to rounding)</b>
MA1909DRTN2	DISASTER FINANCE CENTER	\$791,671	\$0	\$111,798	(\$111,798)
MA1980DRMO1	DISASTER FINANCE CENTER	205,743	-	34,215	(34,215)
MA1980DRMO4	DISASTER FINANCE CENTER	813,161	-	135,229	(135,229)
RW96954025	US COAST GUARD - Army-C.	7	-	1	(1)
RW19923244	DOS/OES-DRL/EX/FMD	500,000	-	30,800	(30,800)
RW57955751	DEPARTMENT OF DEFENSE	584,080	-	81,811	(81,811)
RW70957688	DHS	772,500	-	48,734	(48,734)
RW96944308	USACE-C/O USACE FINANCE	369,009	-	56,207	(56,207)
MA1981DRND2	DISASTER FINANCE CENTER	1,276,029	-	223,305	(223,305)
RW19923251	DOS/OES-DRL/EX/FMD	1,560,000	-	105,045	(105,045)
RW19923377	DOS/OES-DRL/EX/FMD	2,500,000	-	182,500	(182,500)
RW19923463	DOS/OES-DRL/EX/FMD	1,300,000	-	88,140	(88,140)
RW96950522	COE/NEW ORLEANS	17,519,843	-	2,316,721	(2,316,721)
RW96950527	COE/NEW ORLEANS	19,345,178	-	2,545,061	(2,545,061)
RW97922769	DEPT OF DEFENSE	5,963,824	-	393,915	(393,915)
<b>Subtotal: Indirect costs excluded under 19 SAs</b>					<b>(\$6,353,482)</b>
MA1604DRMS5	DISASTER FINANCE CENTER	\$8,072	\$0	\$483	(\$483)
RW12922688	DEPT OF AGRICULTURE	102,797	-	11,670	(11,670)
RW13922088	DOC/NOAA COSTAL SERVICE	136,803	-	10,862	(10,862)
RW14955746	DOI/OIA	75,549	-	10,533	(10,533)
RW19922450	DOS/OES-DRL/EX/FMD	1,160,130	-	82,687	(82,687)
RW19922655	DOS/OES-DRL/EX/FMD	954,783	-	84,180	(84,180)
RW69922499	FED. HIGHWAY ADMIN.	1,044,151	-	116,558	(116,558)
RW70940324	DHS	1,007,484	-	157,858	(157,858)
RW96922535	Corps of Engineers-US Army	22,863	-	1,452	(1,452)
RW75922609	DHHS/CDC/ATSDR/FMO/AP	1,130,775	-	71,925	(71,925)
RW75922615	DHHS/CDC/ATSDR/FMO/AP	638,140	-	73,234	(73,234)
RW75948011	DHHS/CDC/ATSDR/FMO/AP	44,848	-	6,346	(6,346)
RW89922396	DOE, OFFICE OF HDQTRS DIV	169,834	-	11,101	(11,101)
RW89945955	US DEPARTMENT OF ENERGY	1,235,905	-	173,482	(173,482)
RW96950504	COE/NEW ORLEANS	233,834	-	35,505	(35,505)

Agreement no.	Other agency	Direct costs billed	Indirect costs billed	Indirect costs per OIG <sup>1</sup>	Difference (some differences due to rounding)
RW96950520	COE/NEW ORLEANS	1,081,192	-	154,929	(154,929)
RW57921609	DFAS-COLUMBUS	1,102	-	118	(118)
RW58950477	DISASTER FINANCE CENTER	3,504,005	-	472,642	(472,642)
RW70939856	DEPT OF HOMELAND SECURITY	1,366,884	-	121,063	(121,063)
RW72922607	USAID/EL SALVADOR	1,693,217	-	110,811	(110,811)
RW86921823	DEPT OF HUD	1,917,656	-	177,393	(177,393)
RW89939695	DOE, OFFICE OF HDQTRS DIV	1,700,000	-	148,410	(148,410)
RW96950486	COE/NEW ORLEANS	10,907,667	-	1,434,106	(1,434,106)
<b>Subtotal: RIAs awarded before the policy effective date</b>					<b>(\$3,467,348)</b>
RW14957875	DOI-US GEOLOGICAL SURVEY	\$98,651	\$7,350	\$8,810	(\$1,460)
RW17923209	DFAS-CLEVELAND	671,608	86,369	103,095	(16,726)
RW69944293	FED H'WAY ADM-AOM	22,098	2,901	2,955	(53)
RW75922992	DHHS-OFC FIN MGMT, NIH	679,380	62,163	86,213	(24,050)
RW89923247	DOE FIN/ACCTNG SVCE	44,692	5,975	7,164	(1,189)
N10036-HQ	US COAST GUARD	4,131,918	262,377	303,572	(41,195)
N10036-R4	US COAST GUARD	3,125,089	416,887	471,780	(54,893)
N10036-R6	US COAST GUARD	7,135,013	936,114	1,053,769	(117,655)
RW19923042	DOS/OES-DRL/EX/FMD	4,922,905	377,095	520,351	(143,257)
RW70957613	DEPT OF HOMELAND SECURITY	1,277,030	150,690	168,882	(18,193)
RW70957863	DHS-BFC	1,480,592	94,018	111,637	(17,619)
RW72923073	USAID M/FM/CMP	1,388,602	106,367	143,220	(36,853)
RW95922996	R. ACCTBLTY&TRANSP BD	13,050,750	687,775	816,405	(128,631)
<b>Subtotal: Negotiated rates used over life of RIA</b>					<b>(\$601,774)</b>
RW12923178	USDA-RURAL DEVELOPMENT	\$251,401	\$19,257	\$25,821	(\$6,564)
RW12923097	DOA, USDA FOREST SERVICE	1,466,958	-	200,973	(200,973)
RW75922711	DHHS-NIH/OFM/GAO	6,085,561	-	376,727	(376,727)
<b>Subtotal: Indirect costs excluded for other reasons</b>					<b>(\$584,264)</b>
<b>Total</b>			<b>\$13,215,336</b>	<b>\$24,222,205</b>	<b>(\$11,006,868)</b>

Source: OIG analysis

<sup>1</sup> We multiplied the billed direct costs for FYs 2010 and 2011 by the appropriate indirect cost rates in effect during FYs 2010 and 2011 to arrive at the amount of indirect costs that could have been recovered.

## *Potential Future Monetary Benefits*

Agreement no.	Agency	Total award	Amount billed at 9/30/11	Remaining balance	Indirect cost rate (2012)	Monetary benefits
RW14955746	DOI/OIA	\$190,000.00	\$138,975.67	\$51,024.33	10.27%	\$5,240.20
RW19922450	DOS/OES-DRL/EX/FMD	2,995,000.00	2,735,932.18	259,067.82	4.49%	11,632.15
RW57955751	DEPARTMENT OF DEFENSE	1,288,316.00	876,104.42	412,211.58	10.27%	42,334.13
RW69922499	FED. HIGHWAY ADMIN.	3,341,970.00	1,895,440.42	1,446,529.58	7.55%	109,212.98
RW70940324	DEPT OF HOMELAND SECURITY	1,650,999.00	1,197,237.82	453,761.18	11.12%	50,458.24
RW70957688	DISASTER FINANCE CENTER-DHS	1,571,168.54	772,499.81	798,668.73	6.44%	51,434.27
RW75922609	DHHS/CDC/ATSDR/FMO/AP	3,208,797.00	1,923,703.00	1,285,094.00	4.36%	56,030.10
RW75922615	DHHS/CDC/ATSDR/FMO/AP	1,750,000.00	1,020,955.60	729,044.40	7.55%	55,042.85
RW89945955	US DEPARTMENT OF ENERGY	4,051,200.00	3,412,217.74	638,982.26	9.49%	60,639.42
RW96944308	USACE-C/O USACE FINANCE CENTER	624,699.00	369,009.41	255,689.59	10.14%	25,926.92
RW96950504	COE/NEW ORLEANS	785,223.00	237,502.70	547,720.30	9.80%	53,676.59
RW96950520	COE/NEW ORLEANS	1,971,907.00	1,545,227.78	426,679.22	9.80%	41,814.56
RW12923097	DOA, USDA FOREST SERVICE	1,750,000.00	1,466,957.91	283,042.09	9.80%	27,738.12
RW19923377	DOS/OES-DRL/EX/FMD	3,820,000.00	2,500,000.00	1,320,000.00	4.49%	59,268.00
RW58950477	DISASTER FINANCE CENTER	214,762,528.00	210,666,236.86	4,096,291.14	9.80%	401,436.53
RW72922607	USAID/EL SALVADOR	4,494,155.00	3,751,815.41	742,339.59	4.49%	33,331.05
RW86921823	DEPT OF HUD	4,046,000.00	3,291,217.72	754,782.28	6.21%	46,871.98
RW89939695	DOE, OFFICE OF HDQTRS DIV	7,096,000.00	5,060,000.00	2,036,000.00	6.44%	131,118.40
RW96950486	COE/NEW ORLEANS	17,110,594.00	16,018,446.88	1,092,147.12	9.80%	107,030.42
RW96950522	COE/NEW ORLEANS	21,798,518.00	17,576,590.28	4,221,927.72	9.80%	413,748.92
RW96950527	COE/NEW ORLEANS	23,211,108.00	19,623,312.51	3,587,795.49	9.80%	351,603.96
RW97922769	DEPT OF DEFENSE	22,279,628.00	13,839,432.27	8,440,195.73	4.61%	389,093.02
<b>Total</b>						<b>\$2,524,682.81</b>

Source: OIG analysis

## ***Agency Response***

July 12, 2012

### **MEMORANDUM**

**SUBJECT:** Response to the Office of Inspector General's Audit: "EPA Could Recover More Indirect Costs under Reimbursable Interagency Agreements," Project No. OA-FY12-0151, dated June 22, 2012

**FROM:** Barbara J. Bennett /s/ **Original Signed By:**  
Chief Financial Officer

**TO:** Arthur A. Elkins, Jr.  
Inspector General

Thank you for the opportunity to respond to the findings and recommendations in the subject audit report. Attention to these issues should further strengthen the agency's fiscal integrity. Attached is our Corrective Action Plan in response to the specific draft report recommendations. We disagree with the recommendation that the agency amend Reimbursable Interagency Agreements awarded before the policy effective dates to include the ability to recover indirect costs.

If you have any questions concerning the audit response, please contact Jeanne Conklin, Deputy Director, Office of Financial Management at (202) 564-5342 or Ellen Rajewski of the Program Costing Staff at (202) 564-4977.

Attachment

cc: Maryann Froehlich  
Joshua Baylson  
Stefan Silzer  
Jeanne Conklin  
Raffael Stein

Melvin Visnick  
Janice Kern  
Howard Corcoran  
Francis Roth  
Armina Nolan  
Melissa Heist  
Paul Curtis  
Bill Samuel  
Janet Kasper  
Meshell Jones-Peeler  
Dale Miller  
John O'Connor  
Sandy Dickens  
Ellen Rajewski

**Office of the Chief Financial Officer’s Response to the Office of the Inspector  
General Draft Audit**

“EPA Could Recover More Indirect Costs Under Reimbursable Interagency Agreements”  
Project No. OA-FY12-0151, dated June 22, 2012

<b>Rec. No.</b>	<b>OIG Recommendation</b>	<b>Action Official(s)</b>	<b>Proposed Action</b>	<b>Proposed Completion Date</b>
1.	Revise agency policy to clarify that indirect costs should be included in all Reimbursable Interagency Agreements unless a determination has been made that statutory authority used for an RIA specifically exempts charging of indirect costs.	OCFO	The U.S. Environmental Protection Agency concurs with this recommendation. Interim IA and Financial Policy notices were sent to all IA Project Officers and the CFC by OFM and OGD.	Completed 04/02/12
2.	Amend RIAs awarded before the policy effective dates to include the ability to recover indirect costs.	OCFO, OARM	OCFO/OGD respectfully disagrees with this recommendation. Specific reasons are outlined below	N/A
3.	Revise agency policy to require that amendments to all RIAs include indirect costs based on current indirect rates.	OCFO	The OCFO/OGD concurs with this recommendation. The OCFO policy update has been posted in the RMDS.	7/10/12
4.	Correct the indirect cost rate billing errors.	OCFO	OCFO/OGD concurs with this recommendation. The agency is developing a cradle to grave Standard Operating Procedures on financial management of RIAs. All existing RIAs that do not have the appropriate indirect cost rates applied will be renegotiated if a new monetary action is initiated by the program.	On-going
5.	Develop policy and procedures to ensure that the correct indirect costs rates are used.	OCFO	OCFO concurs with this recommendation. The policy will be posted in the RMDS.	12/15/12

## **Response to Recommendation 2**

The EPA disagrees with the OIG recommendation number two, amend RIAs awarded before the policy effective dates to include the ability to recover indirect costs.

Implementing this recommendation is impractical for a number of reasons.

First, opening RIAs for the sole purpose of collecting indirect costs is not cost effective. In addition to the time and effort of the Interagency Shared Service Centers, Project Officers would need to renegotiate existing agreements to seek additional funding from our partner agencies (funding the partners may not have available), and process new RIA amendments. The burden in payroll costs would significantly offset any return. As an example of the scope, in FY 2011 and FY 2012, fewer than 300 total actions (including amendments and no-cost extensions) have been processed for reimbursable IAs.

Second, management and tracking of such an amendment process would be impractical. Given the time and requirements necessary to negotiate and process amendments, these older awards will continue to expire and be closed during the process. Additionally, depending upon the age and funding sources of these awards, we would also need to manage multiple indirect rates across each award.

Third, implementation of a policy retroactively is not recommended for practical reasons. We cannot change the rules for the in-place RIAs that the agency negotiated and legally accepted. We can, however, revise the rules and policies for future actions and educate the EPA on the new policies while implementation is in progress. OCFO and OGD have begun this process.

## ***Distribution***

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Agency Follow-Up Coordinator  
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