U.S. Department of the Interior
Office of Inspector General

SURVEY REPORT

RECOVERY OF OVERHEAD COSTS BY THE BUREAU OF LAND MANAGEMENT

REPORT NO. 99-I-393
MARCH 1999

United States Department of the Interior

OFFICE OF INSPECTOR GENERAL,
Washington, D.C. 20240

MAR 3 1 1999

SURVEY REPORT

Memorandum

To: Director, Bureau of Land Management

From: Robert J. Williams Robert J Williams
Assistant Inspector General for Audits

Subject: Survey Report on Recovery of Overhead Costs by the Bureau of Land Management (No. 99-I-393)

INTRODUCTION

This report presents the results of our review of the Bureau of Land Management's recovery of overhead costs through its indirect cost rate. The objective of our audit was to determine whether the Bureau accurately computed and properly applied the indirect cost ram.

BACKGROUND

The Bureau of Land Management, as custodian of 264 million acres of public land and an additional 300 million acres of subsurface mineral resources, conducts programs and activities that provide benefits to organizations and individuals beyond the benefits received by the general public. For example, when the Bureau processes a mineral patent application, the applicant receives a benefit not received by the general public. Federal law and policy require the Bureau to recover the full costs, including overhead costs, for conducting these programs and activities. In fiscal year 1997, the Bureau recovered overhead costs of $2.5 million for services provided to organizations and individuals. The amount collected generally represented 18 percent of the costs incurred for those activities for which the Bureau determined that it would impose charges.

In fiscal year 1997, the Bureau reviewed its procedures for assessing and collecting costs to determine whether the procedures adequately provided for full cost recovery. Specifically, the Bureau formed a Revenue Enhancement Team, which studied cost recovery. The results of the study were presented in Bureau Instruction Memorandum No. 98-97, dated April 17, 1998, which required each State Director to develop cost recovery plans for their respective programs and projects.[1] Also during our survey, the Bureau was reviewing the indirect cost rate charged to outside organizations and individuals. In conjunction with the Bureau's review, the Office of the Solicitor issued an opinion dated December 5, 1996, on the Bureau's efforts to recover the costs from outside individuals and organizations for processing minerals documents, which stated that the Bureau has the authority to recover costs for those specific activities for which costs had not been collected. According to the opinion, these activities included conducting inspection and enforcement work, reviewing bonds for sufficiency, and reviewing lessee qualifications for mineral leasing.

SCOPE OF SURVEY

We performed our survey from February through May 1998 at the Bureau's National Business Center in Denver, Colorado. To accomplish our objective, we reviewed the methodology for determining the Bureau's indirect cost rate, the support for the rate calculation based on Bureau cost data for fiscal year 1997, and laws and regulations concerning cost recovery. We also tested selected transactions to review the Bureau's application of the indirect cost rate. We conducted the survey in accordance with the "Government Auditing Standards," issued by the Comptroller General of the United States. Accordingly, we included such tests of records and other auditing procedures that were considered necessary under the circumstances to accomplish the objective. We also reviewed the Departmental Report on Accountability for fiscal year 1997, which includes information required by the Federal Managers' Financial Integrity Act of 1982, and the Bureau's annual assurance statement on management controls for fiscal year 1997 to determine whether any reported weaknesses were within the objective and scope of our review. Neither the Accountability Report nor the Bureau's assurance statement reported control weaknesses in the Bureau's recovery of overhead costs.

PRIOR AUDIT COVERAGE

Neither the Office of Inspector General nor the General Accounting Office has issued any reports on the Bureau's recovery of overhead costs through an indirect cost rate during the past 5 years.

RESULTS OF SURVEY

The Bureau of Land Management did not accurately compute and properly apply the indirect cost rate to recover the total reimbursable overhead costs of providing services to organizations and individuals during fiscal year 1997. Office of Management and Budget Circular A-25 ("User Charges"), the Departmental Manual (346 DM), and the Federal Land Policy Management Act of 1976 require the Bureau to recover the overhead costs incurred when performing work for others. However, the Bureau (1) based the indirect cost rate on estimated costs and limited the rate to 18 percent and (2) used an unsupported rate (less than

[1]The memorandum did not address the issues discussed in the Results of Survey section of this report.

18 percent) to assess overhead costs to two other bureaus and the road maintenance program. As a result, the Bureau did not recover fiscal year 1997 costs of more than $386,000.

Circular A-25 states, "When a service .. provides special benefits to an identifiable recipient beyond those that accrue to the general public, a charge will be imposed (to recover the full cost to the Federal Government for providing the special benefit, or the market price)." In addition, the Departmental Manual states, "Recovered costs will include both direct and indirect costs of the performing bureau .. in furnishing the services." Finally, the Federal Land Policy and Management Act authorizes the Bureau to establish fees and charges based on actual costs, excluding "management overhead."[2]

The Bureau computed its indirect cost rate for fiscal year 1997 as follows:

$$\frac{\text{Total Overhead Costs Less Management Overhead Costs}}{\text{Total Direct Costs}}$$

$$\frac{\$171{,}548{,}015 \text{ less } \$45{,}584{,}476}{\$678{,}953{,}082} = 18.55 \text{ percent}$$

To determine management overhead costs, the Bureau had to estimate the costs based on historical data. Prior to fiscal year 1995, the Bureau's financial system identified management overhead costs separately. However, since fiscal year 1995, the Bureau has had to estimate the costs.

Although the Bureau calculates a rate each year, the Bureau's budget office, in accordance with established practice, limits the indirect cost rate to 18 percent. Bureau officials told us that the indirect cost rate was limited to 18 percent to avoid complaints from client organizations about increasing the rate and that the rate had been set at 18 percent for at least 15 years. As a result of limiting the fiscal year 1997 indirect cost rate to 18 percent, we estimated that the Bureau did not recover overhead costs of $76,400. This amount was derived by applying the .55 percent difference between the rates to the estimated total direct costs of $13.9 million[3] for reimbursable work. Since the actual amount of management overhead costs was not available, we could not estimate the full cost impact of using estimated management overhead costs.

The Bureau also used an unsupported indirect cost rate of 3.5 percent to charge two bureaus for technical support services provided to those bureaus under a Bureau of Land Management

'Management overhead as interpreted by the Bureau includes overall program management and support that would include providing overall program planning and direction, developing program policies and procedures, and preparing and executing program budgets.

'We estimated the direct costs of 613.9 million by dividing the recovered overhead costs of $2.5 million by 18 percent.

contract and 5 percent for road maintenance services. Specifically, for the contract services, Bureau officials agreed to lower the 18 percent indirect cost rate to 3.5 percent to reflect the minimum amount of administrative effort required by the contract. Although the Bureau indicated that the rate should be lowered from the standard 18 percent, it could not provide us with documentation as to how the 3.5 percent rate was determined, and the contract did not specify a rate. Therefore, overhead costs of $113,755 (based on the difference between the 3.5 percent rate and the standard 18 percent rate applied to direct costs of $784,514[4]) were not recovered by the Bureau for fiscal year 1997.

For the road maintenance services, the Bureau included 5 percent in its calculation of the road maintenance fee. According to Bureau officials, the Bureau used 5 percent as required by then-existing legislation. However, the 5 percent requirement was repealed with enactment of the Federal Land Policy Management Act of 1976. Therefore, overhead costs of $196,297 (based on the difference between the 5 percent rate and the standard 18 percent rate applied to direct costs of $1,509,977) were not recovered by the Bureau for fiscal year 1997.

Recommendations

We recommend that the Director, Bureau of Land Management:

1. Identify management overhead costs and use the resultant cost data in calculating the Bureau's indirect cost rate.

2. Discontinue the practice of limiting the indirect cost rate to ensure that all overhead costs are properly recovered.

Bureau of Land Management Response and Office of Inspector General Reply

In the March 19, 1999, response (Appendix 2) to the draft report from the Acting Director, Bureau of Land Management, the Bureau did not state specific concurrence or nonconcurrence with the recommendations and also did not provide detailed information on the actions taken or planned to implement the recommendations. Accordingly, we request that the Bureau reconsider its responses to both recommendations, which are unresolved (see Appendix 3).

Recommendation 1. Concurrence/nonconcurrence not stated.

Bureau Response. The Bureau said that it had undertaken a "major exercise" during the last half of fiscal year **1998** "to come up with a verifiable, justifiable overhead rate method for each year." The Bureau further stated, "A rate of 18.55 percent, as mentioned in your [Office of Inspector General] report, was established for FY [fiscal year] **1999."** The Bureau further stated that it would review and adjust the rate at the beginning of each fiscal year.

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[4]We estimated direct costs of $784,514 by dividing the recovered overhead costs of $27,458 by 3.5 percent.

Ofiice of Inspector General Reply. The Bureau did not include detailed information on the actions it has taken "to come up with a verifiable, justifiable overhead rate method for each year." Our report stated that the Bureau had computed an indirect cost rate of 18.55 percent for fiscal year 1997 but that it had to estimate its management overhead costs based on historical data. Consequently, we could not determine whether the rate that the Bureau established for 1999 was based on a new computation which included actual management overhead costs as a result of its "major exercise" to develop a "verifiable, justifiable overhead rate method" or on the rate it had calculated in 1997. Accordingly, we request that the Bureau provide additional details on its method of identifying management overhead costs and of including such costs in its annual rate calculation.

Recommendation 2. Concurrence/nonconcurrence not stated.

Bureau Response. The Bureau stated that it will continue "in some circumstances" to apply an indirect rate of less than the current year general indirect rates "where appropriate justification can be demonstrated and documented." The Bureau further stated that it "should have some flexibility to limit or waive the overhead rate when a project has significant benefit" to the Bureau that "outweighs the overhead assessment."

Office of Inspector General Reply. We agree that some flexibility is needed to limit or waive the rate when a lower rate can be justified and documented. However, we could not determine from the response whether the annual indirect cost rate established by the Bureau would be limited to 18 percent or what criteria would be used for limiting or waiving the rate. Therefore, we request clarification regarding the Bureau's policies and procedures for establishing and applying indirect cost rates, including the circumstances under which the use of an indirect rate that is lower than the current year's rate would be appropriate.

In accordance with the Departmental Manual (360 DM 5.3), we are requesting a written response to this report by May 10, 1999. The response should provide the information requested in Appendix 3.

The legislation, as amended, creating the Office of Inspector General requires semiannual reporting to the Congress on all audit reports issued, the monetary impact of audit findings (Appendix 1), actions taken to implement audit recommendations, and identification of each significant recommendation on which corrective action has not been taken.

We appreciate the assistance of Bureau personnel in the conduct of our audit.

CLASSIFICATION OF MONETARY AMOUNTS

Finding	Potential Additional Revenues
Collection of Overhead Costs	$386,452

United States Department of the Interior

BUREAU OF LAND MANAGEMENT
Washington, D.C. 20240
http://www.blm.gov

In Reply Refer To:
1245 (880)

MAR 1 9 1999

MEMORANDUM

To: Assistant Inspector General for Audits

Through: Sylvia V. Baca Sylvia V. Baca MAR 23 1999
Acting Assistant Secretary, Land and Minerals Management

For

From: Acting Director, Bureau of Land Management

Subject: Response to Draft Survey Report entitled "Recovery of Overhead Costs by the Bureau of Land Management," dated January 1999 (W-IN-BLM-002-98-D)

Thank you for the opportunity to respond to the subject draft survey report on the recovery of overhead costs by the Bureau of Land Management (BLM). We submit the following comments regarding the two recommendations contained in your draft survey report:

Recommendation 1:

Identify management overhead costs and use the resultant cost data in calculating the Bureau's indirect cost rate.

Response: **A** major exercise was undertaken by the BLM during the last half of Fiscal Year (FY) 1998 to come up with a verifiable, justifiable overhead rate method for each year. A rate of 18.55 percent, as mentioned in your report, was established for FY 1999. In addition, the rate will be reviewed and adjusted at the beginning of each FY.

Recommendation 2:

Discontinue the practice of limiting the indirect cost rate to ensure that all overhead costs are properly recovered.

Response: In some circumstances, the BLM will continue to apply an indirect rate of less than the current year general indirect rates where appropriate justification can be demonstrated and documented. For example, the BLM should have some flexibility to limit or waive the overhead rate when a project has significant benefit to the BLM that outweighs the overhead assessment.

The BLM official who is responsible for implementing the recommendations is the Acting Assistant Director for Business and Fiscal Resources.

Should you need additional information regarding the BLM's response, please contact Brenda Adams or Bob Blaicher, BLM Budget Group, at (202) 452-7700 or Gwen Midgette, BLM Management Systems Group, at (202) 452-7739.

STATUS OF SURVEY REPORT RECOMMENDATIONS

Finding/Recommendation Reference	Status	Action Required
1 and 2	Unresolved.	Provide a response to the recommendations. If concurrence is indicated, provide information on the actions taken or planned, including target dates and titles of officials responsible for implementation. If nonconcurrence is indicated, provide reasons for the nonconcurrence.

ILLEGAL OR WASTEFUL ACTIVITIES SHOULD BE REPORTED TO THE OFFICE OF INSPECTOR GENERAL

Internet/E-Mail Address

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Within the Continental United States

U.S. Department of the Interior
Office of Inspector General
1849 C Street, N.W.
Mail Stop 5341
Washington, D.C. 20240

Our 24-hour
Telephone HOTLINE
l-800-424-5081 or
(202) 208-5300

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(202) 208-2420 or
l-800-354-0996

Outside the Continental United States

Caribbean Region

U.S. Department of the Interior
Office of Inspector General
Eastern Division - Investigations
4040 Fairfax Drive
Suite 303
Arlington, Virginia 22203

(703) 235-9221

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U.S. Department of the Interior
Office of Inspector General
North Pacific Region
415 Chalan San Antonio
Baltej Pavilion, Suite 306
Tamuning, Guam 96911

(67 1) 647-6060

Toll Free Numbers:
1-800-424-5081
TDD 1-800-354-0996

FIX/Commercial Numbers:
(202) 208-5300
TDD (202) 208-2420

HOTLINE

1849 C Street, N.W.
Mail stop 5341
Washington, D.C. 20240