

SIGAR

Special Inspector General for
Afghanistan Reconstruction

SIGAR 19-06 Financial Audit

Department of State's Security Support for Justice Sector, Corrections System, and Counter Narcotics Police Programs in Afghanistan: Audit of Costs Incurred by PAE Justice Support

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In accordance with legal requirements, SIGAR has redacted certain information deemed proprietary or otherwise sensitive from this report.



DECEMBER
2018

SIGAR

Special Inspector General for Afghanistan Reconstruction

WHAT THE AUDIT REVIEWED

On December 15, 2014, the Department of State (State) awarded Pacific Architects and Engineers Inc. a \$52,035,382 cost-plus-fixed-fee contract. The contract's objective was to ensure that there was a secure environment for personnel supporting State programs for the justice sector, the corrections system, and the Counter Narcotics Police in Afghanistan. The contract's initial period of performance was to end on December 31, 2015. State modified the contract 15 times, increasing the total value to \$74,784,378 and extending the period of performance to September 18, 2017. Beginning with the first modification to the contract, the name of the entity receiving the contract was changed to PAE Justice Support (PAE).

SIGAR's financial audit, performed by Crowe LLP (Crowe), reviewed \$72,193,961 in expenditures and fixed fees charged to the contract from December 15, 2014, through September 18, 2017. The objectives of the audit were to (1) identify and report on significant deficiencies or material weaknesses in PAE's internal controls related to the contract; (2) identify and report on instances of material noncompliance with the terms of the contract and applicable laws and regulations, including any potential fraud or abuse; (3) determine and report on whether PAE has taken corrective action on prior findings and recommendations; and (4) express an opinion on the fair presentation of PAE's Special Purpose Financial Statement (SPFS). See Crowe's report for the precise audit objectives.

In contracting with an independent audit firm and drawing from the results of the audit, SIGAR is required by auditing standards to review the audit work performed. Accordingly, SIGAR oversaw the audit and reviewed its results. Our review disclosed no instances where Crowe did not comply, in all material respects, with U.S. generally accepted government auditing standards.

December 2018

Department of State's Security Support for Justice Sector, Corrections System, and Counter Narcotics Police Programs in Afghanistan: Audit of Costs Incurred by PAE Justice Support

SIGAR 19-06-FA

WHAT THE AUDIT FOUND

Crowe identified one material weakness, two significant deficiencies, and three deficiencies in PAE's internal controls, and seven instances of noncompliance with the terms and conditions of the contract and applicable regulations. For example, the auditors found one instance of insufficient support to justify the cost for a noncompetitive acquisition. Crowe also found that PAE overcharged the government because it failed to comply with working hours restrictions for an employee and made incorrect foreign currency conversions.

As a result of these internal control deficiencies and instances of noncompliance, Crowe identified \$30,251 in total questioned costs, consisting of \$965 in ineligible costs—costs prohibited by the agreement, applicable laws, or regulations—and \$29,286 in unsupported costs—costs not supported with adequate documentation or that did not have the required prior approval.

Category	Ineligible	Unsupported	Total Questioned Costs
Insufficient support for price reasonableness	\$0	\$28,333	\$28,333
Failure to comply with working hours restrictions	\$965	\$0	\$965
Foreign currency conversions	\$0	\$953	\$953
Totals	\$965	\$29,286	\$30,251

Crowe identified two prior audit reports that had seven recommendations that could be material to the SPFS. Crowe concluded that PAE had taken adequate corrective action on five of the recommendations. For the remaining two, PAE did not resolve late vendor payments and lacked appropriate documentation for property management.

Crowe issued a qualified opinion on the SPFS because the data supporting PAE's level of effort under the contract were not properly maintained. Consequently, Crowe could not conclude that only compensated efforts directly contributing to the contract were included in the statement.

WHAT SIGAR RECOMMENDS

Based on the results of the audit, SIGAR recommends that the responsible contracting officer at State:

- Determine the allowability of and recover, as appropriate, \$30,251 in questioned costs identified in the report.**
- Advise PAE to address the report's six internal control findings.**
- Advise PAE to address the report's seven noncompliance findings.**



SIGAR

Office of the Special Inspector General
for Afghanistan Reconstruction

December 4, 2018

The Honorable Michael R. Pompeo
Secretary of State

The Honorable John R. Bass
U.S. Ambassador to Afghanistan

We contracted with Crowe LLP (Crowe) to audit the costs incurred by PAE Justice Support (PAE) under a Department of State (State) cost-plus-fixed-fee contract.¹ The contract's objective was to ensure that there was a secure environment for personnel supporting State programs for the justice sector, the corrections system, and the Counter Narcotics Police in Afghanistan. Crowe's audit covered \$72,193,961 in expenditures and fixed fees charged to the contract between December 15, 2014, and September 18, 2017. Our contract with Crowe required that the audit be performed in accordance with generally accepted government audit standards issued by the Comptroller General of the United States.

Based on the results of the audit, SIGAR recommends that the responsible contracting officer at State:

- 1. Determine the allowability of and recover, as appropriate, \$30,251 in total questioned costs identified in the report.**
- 2. Advise PAE to address the report's six internal control findings.**
- 3. Advise PAE to address the report's seven noncompliance findings.**

The results of Crowe's audit are discussed in detail in the attached report. We reviewed Crowe's report and related documentation. Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on PAE's Special Purpose Financial Statement. We also express no opinion on the effectiveness of PAE's internal control or compliance with the contract, laws, and regulations. Crowe is responsible for the attached auditor's report and conclusions expressed in it. However, our review disclosed no instances where Crowe did not comply, in all material respects, with generally accepted government auditing standards issued by the comptroller General of the United States.

We will be following up with the department to obtain information on the corrective actions taken in response to our recommendations.

John F. Sopko
Special Inspector General
for Afghanistan Reconstruction

(F-129)

¹ The contract number is SAQMMA15C0003.



PAE Justice Support

Bridge – PAE Security 2015 Contract

Special Purpose Financial Statement

For the Period December 15, 2014, through September 18, 2017

(With Independent Auditor's Report Thereon)

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Transmittal Letter

October 19, 2018

To the Chief Executive Officer of Pacific Architects and Engineers, Inc.
1320 N. Courthouse Road, Suite 800
Arlington, Virginia 22201

Office of the Special Inspector General for Afghanistan Reconstruction
2530 Crystal Drive
Arlington, Virginia 22202

We appreciate the opportunity to provide to you our report regarding the procedures that we have completed during the course of our audit of PAE Justice Support's ("PAE") Bridge – PAE Security 2015 contract funded by the United States Department of State.

Within the pages that follow, we have provided a brief summary of the work performed. Following the summary, we have incorporated our report on the Special Purpose Financial Statement, report on internal control, and report on compliance. We do not express an opinion on the summary or any information preceding our reports.

When preparing our report, we considered comments, feedback, and interpretations of PAE, the Office of the Special Inspector General for Afghanistan Reconstruction, and the Department of State provided both in writing and orally throughout the audit planning and fieldwork phases. Management's final written responses have been incorporated into this report as an appendix.

Thank you for providing us the opportunity to work with you and to conduct the financial audit of PAE's contract.

Sincerely,

A handwritten signature in black ink that reads "John Weber".

John Weber, CPA, Partner
Crowe LLP

Summary

Background

On December 15, 2014, the Office of Acquisition Management of the U.S. Department of State (“DOS”) awarded contract number SAQMMA15C0003 to Pacific Architects and Engineers Incorporated.¹ Beginning with modification number 1 to the contract, the entity receiving the contract was changed to PAE Justice Support (“PAE”). The contract, officially titled “Bridge – PAE Security 2015,” was structured as a cost plus fixed fee arrangement valued at \$52,035,382. Pursuant to the Statement of Work, the objective was to ensure a safe and secure environment for the Bureau of International Narcotics and Law Enforcement Affairs (“INL”) program personnel in support of the National Interdiction Unit (“NIU”), Sensitive Investigative Unit (“SIU”), the Justice Sector Support Program activities, and the Corrections System Support Program in Afghanistan. Further, under the Bridge – PAE Security 2015 contract, PAE was tasked with transitioning the security activities for each of the aforementioned components into one overall contract.² In consideration of these items, the contract was also referred to as the Bridge Afghanistan Security (“BAS”) contract by both PAE and the Government.

The SOW required PAE to execute a series of tasks with respect to accomplishing the objectives, including but not limited to:

1. Providing a plan to recruit, screen, examine, hire, train, assign, supervise, evaluate, process and deploy skilled security, security support, supervisory and command personnel to provide and sustain a 24 hours per day/seven days per week security service for the NIU/SIU;
2. Providing physical security for INL-supported locations that are exempt from the Afghanistan Public Protection Force’s (“APPF”) services;
3. Providing mobile security using APPF services for a) JSSP activities in Kabul; b) CSSP activities in Kabul, Herat, Mazar-e-Sharif, and Nangarhar; and c) PSD support for Camp Gibson-based INL advisors and other INL implementing partners traveling within Kabul to ministries or elsewhere in Afghanistan; and
4. Providing, as a deliverable, a comprehensive security plan for all locations and operations in Afghanistan for which they are responsible at 30 days after contract award.

The contract’s base period of performance spanned from January 1, 2015, through December 31, 2015 and included three option periods, which, if exercised, could extend the period of performance through June 30, 2017. Subsequent to the initial award, the contract was modified fifteen times. The modifications extended the period of performance to September 18, 2017 and increased the total value to \$74,784,378. The table, below, summarizes the contract modifications:

Modification No.	Date	Highlights
1	8/18/2015	Added an incremental funding change of \$12,000,000 and change order under the revised Statement of Work.
2	9/29/2015	Added an incremental funding change of \$2,762,492.
3	1/01/2016	Exercised option period 001 in CLIN 002 and realigned funds in the amount of \$7,325,690 from CLIN 001 to CLIN 002.
4	2/10/2016	Increased funding in the amount of \$4,700,000 to base year CLIN 001 due to an incorrect calculation in modification number 003.

¹ Per the cover page of the contract, the contractor was doing business as “PAE Washington.”

² Reference: “Bridge Afghanistan Security (BAS) SAQMMA15R0012 Technical Proposal dated December 4, 2014

Modification No.	Date	Highlights
5	7/01/2016	Exercised option period 2 and extended the period of performance to reflect July 1, 2016 to December 31, 2016. In addition, the option period was incrementally funded by \$12,480,000.
6	9/22/2016	Added an incremental funding increase of \$9,908,211 under CLIN 003.
7	11/07/2016	Exercised the option period 3 to extend services between January 1, 2017 and June 30, 2017.
8	11/14/2016	Modified the Periods of Performance to their respective CLINs.
9	12/16/2016	Updated the delivery date in CLIN003 to be June 30, 2017, and added a fixed fee funding cap of \$889,293.
10	12/28/2016	Increased funding by \$5,795,870 to cover the extended period of performance.
11	2/15/2017	Updated the position description for the Security Specialist, clearance requirements for the AEGIS guards, and drug testing requirements.
12	2/21/2017	Added requirement that local nationals must be enrolled in the Biometrics Screening System.
13	4/27/2017	Extend the contract through September 18, 2017.
14	5/01/2017	Clarified the Fixed Fee Not To Exceed language under CLIN 003 for the 2.5-month extension period from July 1, 2017 to September 18, 2017.
15	5/15/2017	De-scoped the contract to line up with the revised level of need based on the consolidation of locations within the International Zone.

The audit's scope includes activity within the period December 15, 2014 through September 18, 2017. Within the period under audit, PAE reported \$72,193,961 in total revenue as having been earned, including \$66,957,815 in reimbursable costs.

Work Performed

Crowe LLP ("Crowe") was engaged by the Office of the Special Inspector General for Afghanistan Reconstruction ("SIGAR") to conduct a financial audit of PAE's project.

Objectives Defined by SIGAR

The following audit objectives were defined within the *Performance Work Statement for Financial Audits of Costs Incurred by Organizations Contracted by the U.S. Government for Reconstruction Activities in Afghanistan*:

Audit Objective 1 – Special Purpose Financial Statement

Express an opinion on whether the Special Purpose Financial Statement for the contract presents fairly, in all material respects, revenues earned, costs incurred, items directly procured by the U.S. Government, and balance for the period audited in conformity with the terms of the delivery order and generally accepted accounting principles or other comprehensive basis of accounting.

Audit Objective 2 – Internal Controls

Evaluate and obtain a sufficient understanding of PAE's internal control related to the contract; assess control risk; and identify and report on significant deficiencies including material internal control weaknesses.

Audit Objective 3 – Compliance

Perform tests to determine whether PAE complied, in all material respects, with the contract's requirements and applicable laws and regulations; and identify and report on instances of material noncompliance with terms of the delivery order and applicable laws and regulations, including potential fraud or abuse that may have occurred.

Audit Objective 4 – Corrective Action on Prior Findings and Recommendations

Determine and report on whether PAE has taken adequate corrective action to address findings and recommendations from previous engagements that could have a material effect on the special purpose financial statement or other financial data significant to the audit objectives.

Scope

The scope of the audit covered the period December 15, 2014, through September 18, 2017. The audit was limited to those matters and procedures pertinent to the contract that have a direct and material effect on the Special Purpose Financial Statement ("SPFS"). The audit also included an evaluation of the presentation, content, and underlying records of the SPFS. Further, the audit included reviewing the financial records that support the SPFS to determine if there were material misstatements and if the SPFS was presented in the format required by SIGAR. In addition, the following areas were determined to be direct and material and, as a result, included within the audit program for detailed evaluation:

- Allowable Costs and Activities;
- Cash Management;
- Equipment and Property Management; and
- Procurement.

Methodology

To meet the aforementioned objectives, Crowe completed a series of tests and procedures to audit the SPFS, tested compliance and considered the auditee's internal controls over compliance and financial reporting, and determined if adequate corrective action was taken in response to prior audit, assessment, and findings and review comments, as applicable.

For purposes of meeting Audit Objective 1 pertaining to the SPFS, transactions were selected from the financial records underlying the SPFS, and tested to determine if the transactions were recorded in accordance with accounting principles generally accepted in the United States of America; were incurred within the period covered by the SPFS and in alignment with specified cutoff dates; were appropriately allocated to the award if the cost benefited multiple objectives; and were adequately supported.

With regard to Audit Objective 2 regarding internal control, Crowe requested and the auditee provided copies of policies and procedures to provide Crowe with an understanding of the system of internal control established by PAE during the period of performance. To the extent documented, policies and procedures were unavailable due to either the acquisition, records retention complications, or other matters. Crowe conducted interviews with management to obtain an understanding of the processes that were in place during the period of performance. The system of internal control is intended to provide reasonable assurance of achieving reliable financial reporting and compliance with applicable laws and regulations. Crowe corroborated internal controls identified by the auditee and conducted testing of select key controls to understand if they were implemented as designed.

Audit Objective 3 requires that tests be performed to obtain an understanding of the auditee's compliance with requirements applicable to the contract. Crowe identified – through review and evaluation of the contract executed by and between PAE, the U.S. Department of State (“DOS”), and the Federal Acquisition Regulation (“FAR”) – the criteria against which to test the SPFS and supporting financial records and documentation. Using various sampling techniques, including but not limited to, audit sampling guidance for compliance audits provided by the American Institute of Certified Public Accountants, Crowe selected expenditures, invoices submitted to the Government for payment, procurements, and property and equipment. Supporting documentation was provided by the auditee and subsequently evaluated to assess PAE's compliance. Testing of indirect costs was limited to determining whether indirect costs were calculated and charged to the U.S. Government in accordance with the indirect cost rate memoranda issued by the Defense Contract Audit Agency. We also performed procedures to determine if adjustments to billings that were based on preliminary or provisional rates were made, as required and applicable.

Regarding Audit Objective 4, Crowe inquired of PAE, DOS staff participating in the audit entrance conference, and SIGAR to understand whether or not there were prior audits, reviews, or assessments that were pertinent to the audit scope. Crowe also conducted an independent search of publicly available information to identify audit and review reports. As a result of the aforementioned efforts, we identified two prior reports that contained seven findings and recommendations that could be direct and material to the SPFS. To determine whether adequate corrective action was taken, Crowe requested final Contracting Officer determination letters to understand if corrective action was required and tested applicable transactions, purchases, property, and agreements to determine if the same or similar issues were noted during the course of the audit. To the extent the same or similar issues were not identified during Crowe's testing and/or the findings were not sustained by the Contracting Officer, adequate corrective action is considered to have been taken.

Summary of Results

Upon completion of Crowe's procedures, Crowe identified seven findings because they met one or more of the following criteria: (1) significant deficiencies in internal control, (2) material weaknesses in internal control, (3) noncompliance with rules, laws, regulations, or the terms and conditions of the contract; and/or (4) questioned costs resulted from identified instances of noncompliance.

Crowe issued a qualified opinion on the SPFS due to the data supporting level of effort reports not being maintained in a manner that permitted a determination regarding compliance with each component of Section H-034, *Level-of-Effort*, of the contract. Specifically, the data did not clearly identify the work locations and types of work performed such that the auditor could conclude that only compensated effort in direct contribution to the contract was included in the effort calculations.

Crowe also reported on both PAE's internal controls over financial reporting and compliance with the applicable laws, rules, regulations, and the terms and conditions of the contract. One material weakness in internal control, two significant deficiencies in internal control, and three deficiencies in internal control were reported. All seven findings were classified as instances of noncompliance. Where internal control and compliance findings pertained to the same matter, they were consolidated within a single finding.

In response to identified instances of noncompliance, Crowe reported \$30,251 in questioned costs. SIGAR requires that questioned costs be classified as either “ineligible” or “unsupported.” SIGAR defines unsupported costs as those that are not supported with adequate documentation or did not have required prior approvals or authorizations. Ineligible costs are those that are explicitly questioned because they are unreasonable; prohibited by the audited contract or applicable laws and regulations; or are unrelated to the award. Of the \$30,251 in unique questioned costs, \$965 are deemed ineligible and the remaining \$29,286 unsupported.

Crowe also requested copies of prior audits, reviews, and evaluations pertinent to PAE’s financial performance under the contract. Two reports were identified and assessed for purposes of determining whether there were findings and corrective actions required for follow-up. Seven such findings were noted. **Section 2: Summary Schedule of Prior Audit and Review Findings** provides additional detail regarding the findings. Crowe determined that PAE had taken adequate corrective action on five of the seven findings identified.

The following summary is intended to present an overview of the audit results and is not intended to be a representation of the audit’s results in their entirety. Due to the same costs being questioned in multiple findings, we have included a “Cumulative Unique Questioned Costs” column that is intended to eliminate any duplication of costs within the final questioned cost amount.

Schedule of Findings and Questioned Costs

Finding No.	Finding Name	Classification	Questioned Costs	Cumulative Unique Questioned Costs
2018-01	Employee Worked More than the Authorized Six Consecutive Days	Deficiency and Noncompliance	\$724	\$724
2018-02	Failure to Comply with Working Hours Restrictions	Deficiency and Noncompliance	\$965	\$965
2018-03	Insufficient Support for Cost or Price Reasonableness	Deficiency and Noncompliance	\$28,333	\$29,298
2018-04	Incomplete Level of Effort Reports	Material Weakness and Noncompliance	None	\$29,298
2018-05	Payments to Vendors Not Made Timely	Significant Deficiency and Noncompliance	None	\$29,298
2018-06	Foreign Currency Translations Resulted in Overcharge to the USG	Noncompliance	\$953	\$30,251
2018-07	Indirect Cost Adjustment Calculations Not completed	Significant Deficiency and Noncompliance	None	\$30,251
Total Questioned Costs:				\$30,251

Summary of Management Comments

Management concurred with the facts presented within each finding. However, with the exception of finding 2018-06, management did not expressly concur with the questioned cost amounts.

With respect to findings 2018-01 and 2018-02, management indicated that its understanding of the applicable contract provisions was that the restrictions on work hours and consecutive work days applied to guards only. Therefore, management did not concur with the auditor’s conclusion. Management did, however, commit to providing corrective action with respect to each matter.

Regarding finding 2018-03, management provided additional support for the reasonableness of costs incurred by a sole sourced vendor and considered the support to be appropriate for purposes of documenting the reasonableness of the vendor’s incurred costs.

References to Appendices

The auditor's reports are supplemented by two appendices, **Appendix A**, which contains management's responses to the audit findings, and **Appendix B**, which contains the auditor's rebuttal.

INDEPENDENT AUDITOR'S REPORT ON THE SPECIAL PURPOSE FINANCIAL STATEMENT

To the Chief Executive Officer of Pacific Architects and Engineers, Inc.
1320 N. Courthouse Road, Suite 800
Arlington, Virginia 22201

To the Office of the Special Inspector General for Afghanistan Reconstruction
2530 Crystal Drive
Arlington, Virginia 22202

Report on the Special Purpose Financial Statement

We have audited the Special Purpose Financial Statement ("the Statement") of PAE Justice Support ("PAE"), and related notes to the Statement, with respect to the Bridge – PAE Security 2015 Contract funded by contract number SAQMMA15C0003 for the period December 15, 2014, through September 18, 2017.

Management's Responsibility for the Special Purpose Financial Statement

Management is responsible for the preparation and fair presentation of the Statement in accordance with the requirements specified by the Office of the Special Inspector General for Afghanistan Reconstruction ("SIGAR"). Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of a Statement that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the Special Purpose Financial Statement based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Statement is free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the Statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the Statement in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the Statement.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

(Continued)

Basis for Qualified Opinion

During the course of our audit, we conducted testing of PAE's level of effort reports, which were required by section H-034 of the contract. Pursuant to section H-034 of the contract, certain hours are ineligible for inclusion in the calculation of total direct labor hours contributing to PAE's required [REDACTED] productive hours and [REDACTED] non-productive hours. The documentation supporting PAE's direct labor hours calculation did not indicate whether hours worked reflected uncompensated effort, travel to and from the employee's normal work location, work performed at locations other than the project site, or other such work that is ineligible for inclusion in the direct labor hours calculation. As a result of this matter, we were unable to determine whether the total hours reported meets the required hours contribution. Therefore, the fixed fee amount reported may be materially misstated.

Qualified Opinion

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the Statement referred to above presents fairly, in all material respects, revenue earned, costs incurred, and balance for the indicated period in accordance with the requirements established by the Office of the Special Inspector General for Afghanistan Reconstruction and on the basis of accounting described in Note 1.

Basis of Presentation

We draw attention to Note 1 to the Statement, which describes the basis of presentation. The Statement was prepared by PAE in accordance with the requirements specified by the Office of the Special Inspector General for Afghanistan Reconstruction and presents those expenditures as permitted under the terms of contract number SAQMMA15C0003, which is a basis of accounting other than accounting principles generally accepted in the United States of America, to comply with the financial reporting provisions of the contract task orders referred to above. Our opinion is not modified with respect to this matter.

Restriction on Use

This report is intended for the information of PAE Justice Support, the United States Department of State, and the Office of the Special Inspector General for Afghanistan Reconstruction. Financial information in this report may be privileged. The restrictions of 18 U.S.C. 1905 should be considered before any information is released to the public.

Report on Other Legal and Regulatory Requirements

In accordance with *Government Auditing Standards*, we have also issued reports dated October 18, 2018, on our consideration of PAE's internal controls over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering PAE's internal control over financial reporting and compliance.

Crowe LLP

Crowe LLP

October 18, 2018
Washington, D.C.

PAE
Special Purpose Financial Statement
Contract No. SAQMMA15C0003
For the Period December 15, 2014, to September 18, 2017

	<u>Questioned Costs</u>				
	Budget	Actual	Ineligible	Unsupported	Notes
Revenues					
Contract No. SAQMMA15C0003	\$ 74,784,377	\$ 72,193,961			
Total Revenue	\$ 74,784,377	\$ 72,193,961			4
Costs Incurred					
CLIN No. 001, INL Afghanistan Security Base Year (12 Months)	\$ 19,469,798	\$ [REDACTED]	\$965		6 A, B
CLIN No. 002, INL Afghanistan Security Option Period 1 (6 Months)	19,264,475	[REDACTED]			
CLIN No. 003, INL Afghanistan Security Option Period 2	30,813,958	[REDACTED]		\$28,333	C
Total Costs Incurred	\$ 69,548,231	\$ [REDACTED]		\$953	D
Fixed Fee	\$ 5,236,146	\$ [REDACTED]			
Balance	\$ -	\$ -			7

The accompanying notes to the Special Purpose Financial Statement are an integral part of this Statement.

PAE
NOTES TO THE SPECIAL PURPOSE FINANCIAL STATEMENT
For the Period December 15, 2014, through September 18, 2017

Note 1. Basis of Presentation

The accompanying Special Purpose Financial Statement (the "Statement") includes costs incurred under Contract Number SAQMMA15C0003 for the Bureau of International Narcotics and Law Enforcement Affairs ("INL") Security Bridge Contract for the period December 15, 2014, through September 18, 2017. Because the Statement presents only a selected portion of the operations of PAE, it is not intended to and does not present the financial position, changes in net assets, or cash flows of PAE. The information in this Statement is presented in accordance with the requirements specified by the Office of the Special Inspector General for Afghanistan Reconstruction ("SIGAR") and is specific to the aforementioned Federal Contract. Therefore, some amounts presented in this Statement may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Note 2. Basis of Accounting

Expenditures reported on the Statement are reported on the Costpoint accounting system and, therefore, are reported on the accrual basis of accounting.

Note 3. Foreign Currency Conversion Method

For purposes of preparing the Statement, conversions from local currency to United States dollars were required under PAE corporate policies as it pertains to foreign exchange rates. PAE's practice is to utilize the spot rate in effect on the transaction date for purposes of translating costs denominated in a foreign currency to U.S. dollars.

Note 4. Revenues

Revenues on the Statement represent the amount of funds to which PAE is entitled to receive from the Department of State for allowable, eligible costs incurred under the contract and fees earned during the period of performance.

Note 5. Revenue Recognition

The BAS INL Afghanistan program used cost type/percentage of completion accounting throughout the period of performance.

Note 6. Costs Incurred by Budget Category

The budget categories presented and associated amounts reflect the budget line items presented within the final, approved contract budget adopted as a component of the SAQMMA15C0003 Modification MOD014 to the contract dated May 1, 2017.

Note 7. Balance

The balance presented on the Statement represents the difference between revenues earned and costs incurred such that an amount greater than \$0 would reflect that revenues have been earned that exceed the costs incurred or charged to the contract and an amount less than \$0 would indicate that costs have been incurred, but are pending additional evaluation before a final determination of allowability and amount of revenue earned may be made.

PAE
NOTES TO THE SPECIAL PURPOSE FINANCIAL STATEMENT
For the Period December 15, 2014, through September 18, 2017

Note 8. Currency

All amounts presented are shown in U.S. dollars.

Note 9. Program Status

The BAS INL Afghanistan program's period of performance has completed. The period of performance for the contract concluded on 9/18/17 as noted in modification number 14 dated May 1, 2017.

Note 10. Level of Effort per Period

PAE's contract with the United States Department of State requires that PAE provide [REDACTED] productive hours and [REDACTED] non-productive hours in direct labor, including subcontractor direct labor hours. The following table summarizes direct labor hours worked during each applicable performance period under the contract.

	Hours
Base Year	[REDACTED]
Option Period 1	[REDACTED]
Option Period 2	[REDACTED]
Total	[REDACTED]

Note 11. Subsequent Events

Management has performed an analysis of the activities and transactions subsequent to the contract period covered by the Statement. Management has performed their analysis through October 18, 2018.

PAE JUSTICE SUPPORT
NOTES TO THE QUESTIONED COSTS PRESENTED ON THE
SPECIAL PURPOSE FINANCIAL STATEMENT

A. Finding 2018-01 questioned \$724 due to individuals working more than the authorized number of consecutive days, in accordance with Section F-008 of the contract.

B. Finding 2018-02 questioned \$965 due to individuals who worked hours in excess of the maximum daily cap, identified in Section F-008 of the contract.

C. Finding 2018-03 includes \$28,333 in questioned costs due to PAE's inability to provide evidence of competition, a Noncompetitive Acquisition Justification Form, and documentation that adequately supported the reasonableness of costs incurred by the vendor.

D. Finding 2018-06 includes \$953 in questioned costs due to foreign currency translations resulting in an overcharge to the Government. The discrepancies were a result of differences between the rates used at the time of payment and those in effect during the invoice period.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL

To the Chief Executive Officer of Pacific Architects and Engineers, Inc.
1320 N. Courthouse Road, Suite 800
Arlington, Virginia 22201

To the Office of the Special Inspector General for Afghanistan Reconstruction
2530 Crystal Drive
Arlington, Virginia 22202

We have audited the Special Purpose Financial Statement ("the Statement") of PAE Justice Support ("PAE"), and related notes to the Statement, with respect to the Bridge – PAE Security 2015 Contract funded by contract number SAQMMA15C0003 for the period December 15, 2014, through September 18, 2017. We have issued our report thereon dated October 18, 2018, within which we have qualified our opinion.

Internal Control over Financial Reporting

PAE's management is responsible for establishing and maintaining effective internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies and procedures. The objectives of internal control are to provide management with reasonable, but not absolute, assurance that the assets are safeguarded against loss from unauthorized use or disposition; transactions are executed in accordance with management's authorization and in accordance with the terms of the contract; and transactions are recorded properly to permit the preparation of the Statement in conformity with the basis of presentation described in Note 1 to the Statement. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the Statement for the period December 15, 2014, through September 18, 2017, we considered PAE's internal controls to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the Statement, but not for the purpose of expressing an opinion on the effectiveness of PAE's internal control. Accordingly, we do not express an opinion on the effectiveness of PAE's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency* in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying Schedule of Findings and Questioned Costs as finding 2018-04 to be a material weakness.

(Continued)

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as findings 2018-05 and 2018-07 to be significant deficiencies.

PAE Justice Support's Response to the Findings

PAE's response to the findings was not subject to the auditing procedures applied in the audit of the special purpose financial statement and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

Restriction on Use

This report is intended for the information of PAE Justice Support, the United States Department of State, and the Office of the Special Inspector General for Afghanistan Reconstruction. Financial information in this report may be privileged. The restrictions of 18 U.S.C. 1905 should be considered before any information is released to the public.



Crowe LLP

October 18, 2018
Washington, D.C.

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE

To the Chief Executive Officer of Pacific Architects and Engineers, Inc.
1320 N. Courthouse Road, Suite 800
Arlington, Virginia 22201

To the Office of the Special Inspector General for Afghanistan Reconstruction
2530 Crystal Drive
Arlington, Virginia 22202

We have audited the Special Purpose Financial Statement ("the Statement") of PAE Justice Support ("PAE"), and related notes to the Statement, with respect to the Bridge – PAE Security 2015 Contract funded by contract number SAQMMA15C0003 for the period December 15, 2014, through September 18, 2017. We have issued our report thereon dated October 18, 2018, within which we have qualified our opinion.

Management's Responsibility for Compliance

Compliance with Federal rules, laws, regulations, and the terms and conditions applicable to the contract task orders is the responsibility of the management of PAE Justice Support.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Statement is free of material misstatement, we performed tests of compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Questioned Costs as findings 2018-01, 2018-02, 2018-03, 2018-04, 2018-05, 2018-06, and 2018-07.

PAE Justice Support's Response to the Findings

PAE's response to the findings was not subjected to the auditing procedures applied in the audit of the special purpose financial statement and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's compliance. Accordingly, this communication is not suitable for any other purpose.

Restriction on Use

This report is intended for the information of PAE Justice Support, the United States Department of State, and the Office of the Special Inspector General for Afghanistan Reconstruction. Financial information in this report may be privileged. The restrictions of 18 U.S.C. 1905 should be considered before any information is released to the public.

Crowe LLP
Crowe LLP

October 18, 2018
Washington, D.C.

PAE JUSTICE SUPPORT
SECTION I: SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Finding 2018-01: Employee Worked More than the Authorized Six Consecutive Days

Deficiency and Noncompliance

Criteria: Section F-008 of the contract states, "[t]he Contractor shall NOT work more than six consecutive days in any seven consecutive day period."

Pursuant to FAR 31.201-2, *Determining allowability*, "(a) A cost is allowable only when the cost complies with all of the following requirements:

- (1) Reasonableness.
- (2) Allocability.
- (3) Standards promulgated by the CAS Board, if applicable, otherwise, generally accepted accounting principles and practices appropriate to the circumstances.
- (4) Terms of the contract.
- (5) Any limitations set forth within [FAR 31.2].

Condition: During our testing of 95 transactions, we noted two instances in which Employee Number [REDACTED] worked seven consecutive days. The \$724 in compensation associated with the seventh day worked is questioned as an ineligible cost due to prohibition by the audited contract.

Week	Hours Worked on Day 7 (A)	Total Hours Worked (B)	Total Compensation for the Week (C)	Effective Hourly Rate (D = C/B)	Questioned Cost Amount (A * D)
Week 1	12	87	\$2,388	\$27.45	\$329
Week 2	12	76.2	\$2,511	\$32.95	\$395
Total Questioned Costs					\$724

Questioned costs: \$724

Effect: The likelihood that individuals will work more days and/or hours than is considered reasonable and, thereby, suffer declining performance is increased. In addition, the PAE failed to comply with the contract requirements and the FAR.

Cause: PAE did not have an adequate procedure in place to prevent individuals from working more than the authorized number of consecutive days. PAE also lacked an adequate internal detective control to identify instances of noncompliance with the provision and to ensure that the corresponding costs were not invoiced to the Government.

Recommendation: We recommend that PAE:

1. Either reimburse the Government \$724 resulting from the overcharge or otherwise produce alternative documentation that demonstrates the costs are allowable and compliant with the contract's terms and conditions; and
2. Design and implement a process to periodically review days worked for potential violations of contract terms, to the extent the Company has active DOS-funded projects with the same or similar working day restrictions.

(Continued)

PAE JUSTICE SUPPORT
SECTION I: SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Finding 2018-02: Failure to Comply with Working Hours Restrictions

Deficiency and Noncompliance

Criteria: Per Section F-008 of the contract, "The Contractor shall work at least 8 hours per day, but NOT more than 10 hours per day."

Pursuant to FAR 31.201-2, *Determining allowability*, "(a) A cost is allowable only when the cost complies with all of the following requirements:

- (1) Reasonableness.
- (2) Allocability.
- (3) Standards promulgated by the CAS Board, if applicable, otherwise, generally accepted accounting principles and practices appropriate to the circumstances.
- (4) Terms of the contract.
- (5) Any limitations set forth within [FAR 31.2].

Condition: We selected 95 transactions for allowable cost testing. During our testing, we identified two transactions associated with Employee Number [REDACTED], who provided security services. The employee failed to work either the minimum number of hours per day or exceeded the maximum number of hours per day. \$965 in costs associated with the hours worked in excess of the daily cap are in question. Costs are not questioned in those instances where an individual did not work the minimum number of hours per day due to PAE's having invoiced the Government on a per hour basis.¹

Week	Hours Worked in Excess of the 10 Hour Daily Cap (A)	Total Hours Worked (B)	Total Compensation for the Week (C)	Effective Hourly Rate (D = C/B)	Questioned Cost Amount (A * D)
Week 1	20.5	87	\$2,388	\$27.45	\$563
Week 2	12.2	76.2	\$2,511	\$32.95	\$402
Total Questioned Costs					\$965

Questioned costs: \$965

Effect: Working in excess of the maximum number of hours increases the likelihood that the quality of employee performance will decline. In addition, failure to work the minimum number of hours increases the risk that the Government will not receive the expected benefit in return for funding an individual's work in-country. In addition, the PAE failed to comply with the contract requirements and the FAR.

Cause: PAE did not have adequate internal controls over compliance with labor charges. Specifically, PAE lacked a process to monitor compliance with the hours restrictions appearing in the contract. In addition, PAE did not believe that the requirement applied to security personnel.

Recommendation: We recommend that PAE:

1. Either reimburse the Government \$965 resulting from the overcharge or otherwise produce alternative documentation that demonstrates the costs are allowable and compliant with the contract's terms and conditions;
2. Design and implement a process to include supervisory review of hours worked to identify any potential violations of contract terms, to the extent the Company has active DOS-funded projects with the same or similar working hour restrictions.

¹ The errors referenced within the condition pertain to the same employee, work weeks, and compensation that are the subject of Finding 2018-01.

(Continued)

PAE JUSTICE SUPPORT
SECTION I: SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Finding 2018-03: Insufficient Support for Cost or Price Reasonableness

Deficiency and Noncompliance

Criteria: Pursuant to FAR 31.201-2, *Determining allowability*, "(a) A cost is allowable only when the cost complies with all of the following requirements:

- (1) Reasonableness.
- (2) Allocability.
- (3) Standards promulgated by the CAS Board, if applicable, otherwise, generally accepted accounting principles and practices appropriate to the circumstances.
- (4) Terms of the contract.
- (5) Any limitations set forth in [FAR 31.2]."

FAR 31.201-3, *Determining reasonableness*, states:

- (a) A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business.
- (b) What is reasonable depends upon a variety of considerations..., including (4) Any significant deviations from the contractor's established practices.

Per PAE Policy Statement 732 on competition, "[c]ompetitive actions are required for all direct charge orders over \$3,500 (micro-purchase threshold) unless single/sole source justification is provided. Three or more offers should be solicited for any requirement over \$3,500."

Per PAE Policy Statement 731, *Non-Competitive Procurements*, "Any contemplated non-competitive procurements shall be documented on the Noncompetitive Acquisition Justification Form (PAE-PRO-003) and filed in the procurement file.

Condition: Of 20 procurements tested, we identified one for which evidence of competition, a Noncompetitive Acquisition Justification Form, and supporting documentation for cost or price reasonableness was not provided. In the absence of competition and evidence of an assessment of cost reasonableness having been completed, we could not conclude that the actual costs incurred for the vendor's services are reasonable.

PAE's contract (PP-0000189) with the vendor, Pontoon Solutions, Inc., was valued at \$43,800 for the hiring of temporary labor to support existing project staff. Actual costs incurred under the subcontract was \$28,333, which is in question.

Questioned costs: \$28,333

Effect: In the absence of competition or execution of alternative procedures, the likelihood that unreasonable costs will be incurred thus resulting in noncompliance is increased.

Cause: Management lacked internal controls and procedures to ensure that procurement files included required documentation to justify noncompetitive acquisitions.

Recommendation: We recommend that PAE:

1. Reimburse the Government \$28,333 or otherwise produce documentation to support the reasonableness of the costs incurred; and
2. Design and implement a monitoring procedure that will detect instances in which competition is either not conducted or the use of non-competitive procedures is inadequately justified.

(Continued)

PAE JUSTICE SUPPORT
SECTION I: SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Finding 2018-04: Incomplete Level of Effort Reports

Material Weakness and Noncompliance

Criteria: As noted in contract SAQMMA15C003, section H-034,

"The contractor agrees to provide in the performance of this contract [REDACTED] productive hours; [REDACTED] non-productive hours]. Of the total direct labor hours set forth above, it is estimated that (0) hours are uncompensated effort. Uncompensated effort is defined as hours provided by personnel in excess of 40 hours per week without additional compensation for such excess work.

Effort performed in fulfilling the total level-of-effort specified in paragraph (a) shall only include effort performed in direct support of this contract, and shall not include time and effort expended on such things as local travel to and from an employee's usual work location, uncompensated effort while on travel status, truncated lunch periods, work at an employee's residence or other non-work locations, or other time and effort which does not have a specific and direct contribution to the performance of work under this contract."

Within 45 days after completion of the work under each separately identified period of performance hereunder, the Contractor shall submit the following information in writing to the Contracting Officer with copies to the cognizant Contract Administration Office and to the cognizant audit activity office to which vouchers are submitted:

- (1) the total number of direct labor hours expended during the applicable period;
- (2) a breakdown of this total showing the number of hours expended in each direct labor classification and associated direct and indirect costs;
- (3) a breakdown of other costs incurred; and
- (4) the Contractor's estimate of the total allowable cost incurred under the contract for the period.

Condition: PAE provided a copy of the level of effort information used to support the Company's having met the required productive and non-productive hours requirement appearing in Section H-034 of the contract. The report identified the total hours worked per person; however, the supporting schedules did not clearly identify which hours were compensated and which hours were uncompensated. In addition, the supporting schedules did not specify each employee's work location(s).

In addition, we noted that the documentation provided for audit did not identify a breakdown of direct and indirect costs, a breakdown of other costs incurred, and PAE's estimate of the total allowable cost incurred under the contract for each applicable period of performance. Lastly, PAE did not provide evidence that the reports were submitted to the State Department within 45 days of the close of each period of performance, as required by the contract.

Questioned costs: None

Effect: PAE may have improperly recorded and reported non-productive hours worked to the State Department without management's knowledge. In addition, PAE may have failed to comply with the contract terms and conditions.

Cause: PAE did not have a process in place to ensure that hours reported to DOS in support of the level of effort requirement only includes those productive and non-productive hours permitted by the contract.

Recommendation: PAE should design, document, and formally adopt a procedure that requires the individual responsible for compliance with each applicable contract to: 1) identify all reporting requirements applicable to a contract; 2) document how the requirements will be met; and 3) how management will monitor the timely submission of each required report during the contract's period of performance.

(Continued)

PAE JUSTICE SUPPORT
SECTION I: SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Finding 2018-05: Payments to Vendors Not Made Timely

Significant Deficiency and Noncompliance

Criteria: FAR 52.216-7 (b)(1)(ii)(A) Requires payments be made “for supplies and services purchased directly for the contract...in accordance with the terms and conditions of the subcontract or invoice...and ordinarily within 30 days of submission of the contractor's payment request to the Government.”

Condition: We tested 25 transactions to determine if PAE complied with the payment provisions of FAR 52.216-7, which requires that payments for items or services purchased directly for the contract be made within 30 days of submission of the corresponding request for reimbursement to the Government and in accordance with the terms and conditions of the purchase order or subcontract. Of the 25 transactions tested, we noted that 17 of the payments were made more than 30 days after submission of the reimbursement request.

Questioned costs: None.

Effect: The Government disbursed funds to PAE for 17 transactions prior to PAE's being eligible for reimbursement of the corresponding costs. Therefore, the Government's cash was unavailable for other purposes.

Cause: PAE did not implement an adequate monitoring process to ensure that payments were made timely.

Recommendation: We recommend that PAE develop a process that includes an assessment of planned payment dates for non-labor transactions at the time a reimbursement request is submitted. The process should require the assessment to identify which payments will not be made within 30 days of submission.

(Continued)

PAE JUSTICE SUPPORT
SECTION I: SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Finding 2018-06: Foreign Currency Translations Resulted in Overcharge to the USG

Noncompliance

Criteria: The commercial cost principles contained within 48 CFR Part 31 include the following requirement:

31.201-2 Determining allowability

(a) A cost is allowable only when the cost complies with all of the following requirements:

- (1) Reasonableness.
- (2) Allocability.
- (3) Standards promulgated by the CAS Board, if applicable, otherwise, generally accepted accounting principles and practices appropriate to the circumstances.
- (4) Terms of the contract.
- (5) Any limitations set forth in this subpart.

Part 31.201-2(c) goes on to state, “[w]hen contractor accounting practices are inconsistent with this subpart 31.2, costs resulting from such inconsistent practices in excess of the amount that would have resulted from using practices consistent with this subpart are unallowable.”

Accounting Standards Codification Topic 830, *Foreign Currency Matters*, states that, “[a]t the date a foreign currency transaction is recognized, each asset, liability, revenue, expense, gain, or loss arising from the transaction shall be measured initially in the functional currency of the recording entity by use of the exchange rate in effect at that date.”

The Accounting Standards Codification defines “transaction date” as “[t]he date at which a transaction (for example, a sale or purchase of merchandise or services) is recorded in accounting records in conformity with generally accepted accounting principles (GAAP). A long-term commitment may have more than one transaction date (for example, the due date of each progress payment under a construction contract is an anticipated transaction date).”

Condition: During our testing of foreign currency translations, we identified under- and over-charges to the Government due to differences between the rates used at the time of payment and those in effect during the invoice period. The total overbilled amount was \$953, which is in question. When netted against undercharges, the misstatement amount is \$669.

Questioned Costs: \$953

Effect: PAE overcharged the U.S. Government.

Cause: Management may have applied an incorrect transaction date when completing the currency translation.

Recommendation: We recommend that PAE either refund the Government \$953 or otherwise provide documentation indicating that the currency translations were properly completed and adequately documented.

(Continued)

PAE JUSTICE SUPPORT
SECTION I: SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Finding 2018-07: Indirect Cost Adjustment Calculations Not Completed

Significant Deficiency and Noncompliance

Criteria: Pursuant to FAR 52.216-7(e), *Allowable Cost and Payment*, "Billing Rates,"

Until final annual indirect cost rates are established for any period, the Government shall reimburse the Contractor at billing rates established by the Contracting Officer or by an authorized representative (the cognizant auditor), subject to adjustment when the final rates are established.

These billing rates—

- (1) Shall be the anticipated final rates; and
- (2) May be prospectively or retroactively revised by mutual agreement, at either party's request, to prevent substantial overpayment or underpayment.

Condition: PAE did not complete an indirect cost true-up calculation for each year based on actual costs incurred and anticipated final billing rates. Using PAE's anticipated final rates, the anticipated adjustment amounts calculated during the audit follow:

2015 - [REDACTED] credit to the Government
2016 - [REDACTED] undercharge to the Government
Net: [REDACTED] undercharge based on our sample of invoices selected for testing

Questioned Costs: None

Effect: In the absence of a process to calculate and assess the potential indirect cost adjustment amount, there may be a significant under- or over-billing that PAE and the Government are not made aware of.

Cause: As a matter of standard company practice, PAE does not calculate indirect cost adjustments until the audit of PAE's indirect costs for each applicable year is completed by DCAA or the applicable Federal agency. PAE did not conduct the assessment during this contract's period of performance due to delays in the Federal audits being initiated and completed.

Recommendation: We recommend that,

1. After PAE's annual financial statement audit is finalized, the company calculate the anticipated true-up adjustment and correspond with each applicable contracting officer to determine if an adjustment is expected in real time or if it is acceptable for PAE to wait until the indirect cost audits are complete.
2. PAE design and implement internal control procedures to perform true-up calculations in order to calculate actual indirect costs incurred. These calculations should be performed, at a minimum, on an annual basis.

PAE JUSTICE SUPPORT
SECTION II: SUMMARY SCHEDULE OF PRIOR AUDIT, REVIEW, AND ASSESSMENT FINDINGS

Crowe reviewed two prior reports pertaining to audits of PAE and that included seven findings and recommendations that may be direct and material to the Special Purpose Financial Statement or other financial information significant to the audit objectives.

Regarding the identified questioned costs in each report, we noted the following:

1. Evidence of PAE's having reimbursed the Government for \$6,458 in sustained questioned costs associated with SIGAR Financial Audit 15-69 was provided; and
2. Regarding \$506,866 in questioned costs reported in SIGAR Financial Audit 15-22, DOS indicated that it is continuing discussions with PAE and resolution is anticipated by the end of 2018. No further procedures were considered necessary with respect to the questioned costs, as of the date of this report.

Regarding the aforementioned reports that contained findings and recommendations that may be direct and material to the SPFS, we have summarized the results of our procedures below and on the following pages.

Finding No. 2015-01: Equipment Management

Report: Audit of PAE's Special Purpose Financial Statement for the period May 31, 2010, through September 24, 2013, pertaining to the Justice Sector Support Program dated May 12, 2015.

Issue: A material weakness and non-compliance pertaining to property management was identified. Questioned costs totaled \$6,458 relating to 19 items that lacked appropriate documentation and may have been missing from the inventory.

A-T Solutions (now PAE) incurred unallowable/unreasonable costs totaling \$2,376. Costs were to upgrade flights to "Economy Plus" which was deemed unnecessary and therefore unreasonable.

Status: During our testing, we noted that information appearing in the physical inventory for three items did not agree to the information presented in the source documents (e.g., invoices). Crowe concluded that adequate corrective action was not taken with respect to this matter and communicated the matter orally to management.

Finding No. 2014-01: Cash Management Procedures

Report: Audit of PAE's Special Purpose Financial Statement for the period March 31, 2005, through May 30, 2010, pertaining to the Afghanistan Justice Support Program dated October 10, 2014.

Issue: Seven invoices were originally rejected by the Department of State. As a result, PAE revised these invoices with proper documentation and/or removal of ineligible items. One of the reimbursement invoices was missing documented approvals while another expense was not paid within the 30 days of invoicing the Department of State. This invoice was paid 298 days after Department of State was invoiced.

Status: We conducted testing of a sample of transactions to determine if the costs were paid timely in relation to the date of submission of the corresponding reimbursement request. We identified seventeen payments that were made more than 30 days after submission of the reimbursement request throughout our testing. It has been concluded that adequate corrective actions have not been taken to resolve this issue. See Finding 2018-05 in this report.

(Continued)

Finding No. 2014-02: Procurement Practices

Report: Audit of PAE's Special Purpose Financial Statement for the period March 31, 2005, through May 30, 2010, pertaining to the Afghanistan Justice Support Program dated October 10, 2014.

Issue: PAE could not produce support for approvals on four JSSP purchases. These four purchases did not contain proper internal purchase approvals as the requisition was not signed. In addition, these purchases did not include support for proper approval. As a result, questioned costs totaled \$12,251 from the difference in the lowest bid and the second lowest bid. No support was provided to support the decision to award the second lowest bidder the contract.

Status: During our testing of procurement, we did not identify any instances in which PAE did not produce evidence of management approval of procurements. In addition, we did not identify any instances in which PAE could not produce support for its selection of a vendor that was other than the lowest bidder. This matter is not repeated.

Finding No. 2014-03: Allowable Costs – Inadequate Supporting Documentation

Report: Audit of PAE's Special Purpose Financial Statement for the period March 31, 2005, through May 30, 2010, pertaining to the Afghanistan Justice Support Program dated October 10, 2014.

Issue: PAE did not provide adequate supporting documentation for program costs and as a result, it could not be determined if the costs were allowable. For 7 of the 60 items tested, no support was provided and could not be tested for allowability. Also, 17 items had specific exceptions as noted on the table on page 24 of the abovementioned report. Questioned costs total \$239,099 for the period.

Status: During our testing of expenditures, we did not identify any instances in which PAE failed to produce adequate supporting documentation. This matter is not repeated.

Finding No. 2014-04: Improper Maintenance of Equipment

Report: Audit of PAE's Special Purpose Financial Statement for the period March 31, 2005, through May 30, 2010, pertaining to the Afghanistan Justice Support Program dated October 10, 2014.

Issue: PAE could not provide required documentation of the disposition of three equipment items noted as missing or lost. A total of \$2,750 resulted in questioned costs. In addition, PAE did not maintain complete inventory records on four items. These items were missing acquisition costs and unique identifiers

Status: During our testing of property dispositions, we did not detect any instances in which property was not disposed of in accordance with the Contracting Officer's instructions. This matter is not repeated.

PAE JUSTICE SUPPORT
SECTION II: SUMMARY SCHEDULE OF PRIOR AUDIT, REVIEW, AND ASSESSMENT FINDINGS

Finding No. 2014-05: Special Purpose Financial Statement Adjustment

Report: Audit of PAE's Special Purpose Financial Statement for the period March 31, 2005, through May 30, 2010, pertaining to the Afghanistan Justice Support Program dated October 10, 2014.

Issue: An adjustment of \$566,000 was noted to the SPFS and financial records (affecting both revenue and expenses). The adjustment was not identified until Crowe brought the variance between the initial SPFS & DOS reports to PAE's attention.

Status: We conducted testing of the transactions underlying the SPFS to determine if each transaction was adequately supported and accurately reported. We did not identify any instances in which a material misstatement existed. This matter is not repeated.

Finding No. 2014-08: Substitutions to Key Personnel

Report: Audit of PAE's Special Purpose Financial Statement for the period March 31, 2005, through May 30, 2010, pertaining to the Afghanistan Justice Support Program dated October 10, 2014.

Issue: PAE was unable to provide support for the substitution of key personnel.

Status: During our testing of employee labor charges, we did not identify any instances in which PAE did not obtain prior approval for key personnel. This matter is not repeated.

APPENDIX A:
VIEWS OF RESPONSIBLE OFFICIALS



October 18, 2018

Eric J. Russell
Crowe LLP
1455 Pennsylvania Ave., NW
Suite 700
Washington, DC 20004

Reference: PAE Responses to SIGAR audit of Contract No. SAQMMA15C0003

Dear Mr. Russell:

PAE hereby submits the following management response to the audit findings included in the SIGAR audit report dated August 2, 2018, received by PAE on October 2, 2018.

Finding 2018-01: Employee Worked More than the Authorized Six Consecutive Days

The auditor referenced two instances in which an employee worked seven consecutive days and calculated a rate associated with work attributed to the seventh day of work.

PAE had understood the work limitations in section F-008 of the contract to apply to guards, where the likelihood of fatigue and performance has a direct safety impact on the contract. The employee in question is an exempt employee, and there is no overtime or premium pay associated with the work beyond the standard work week. PAE therefore takes exception to the questioned costs of \$724.

PAE values the well-being of all staff members, and we are committed to ensuring that employees have appropriate time to rest. Given that the transaction testing revealed excess labor days in a very small percentage of the labor transactions, as corrective action, PAE will communicate the labor restrictions to the supervisors approving timesheets.

Finding 2018-02: Failure to Comply with Working Hours Restrictions

Similar to Finding 2018-01, the auditor referenced the same two instances in which an employee worked more than 10 hours per day.

As noted above, PAE had understood the work limitations in section F-008 of the contract to apply to guards. The employee in question is an exempt employee, and there is no overtime or

premium pay associated with the work beyond the standard work week. PAE therefore takes exception to the questioned costs of \$965.

PAE values the well-being of all staff members, and we are committed to ensuring that employees have appropriate time to rest. Given that the transaction testing revealed excess labor hours in a very small percentage of the labor transactions, as corrective action, PAE will communicate the labor restrictions to the supervisors approving timesheets.

Finding 2018-03: Insufficient Support for Cost or Price Reasonableness

The auditor referenced a noncompetitive acquisition for a vendor providing temporary support labor and questioned \$28,333 in costs.

Under this vendor agreement, PAE hired services for a senior-level technical recruiter to support the contract. PAE conducted a comparative analysis to determine the resultant bill rate against the market rate for the job category. The rate for the senior-level technical recruiter billed to the subject contract was [REDACTED]

PAE conducted a comparative analysis against job classification HRC-TAC120 (Recruiter III, Senior level) based on the following compensation sources: Kenexa, CompAnalyst, Radford and Western Management Group.

The low-, mid-, and high-range rates for a senior level recruiter in the Washington, DC metropolitan job market are as follows:

Min	Mid	Max
[REDACTED]	[REDACTED]	[REDACTED]

The mid-range rate of [REDACTED] results in an hourly rate of [REDACTED]. Applicable indirect costs include fringe [REDACTED] and facility [REDACTED], result in a total hourly rate to [REDACTED]

In conclusion, the analysis demonstrates that had the senior-level technical recruiter been a PAE employee, the incurred cost to the USG would have been similar. The cost difference of between the two hiring mechanisms is immaterial, and the rate is reasonable, allowable, and allocable. PAE's analysis fully supports and justifies the rate.

Finding 2018-04: Incomplete Level of Effort Reports

The auditor had reservations about the detail provided in the level of effort reports.

PAE provided the labor reports, per section H-034 of the contract. We acknowledge that although there was a process for reporting, there was not a formal standard in place to ensure

consistency across the INL portfolio. PAE agrees to review the reporting requirements for the INL portfolio of contracts and monitor timely submission of required reports.

Finding 2018-05: Payments to Vendors Not Made Timely

The auditor referenced 17 payments made more than 30 days after submission of the reimbursement request.

PAE will review the findings with our internal teams to ensure future payments are made in a timely fashion.

Finding 2018-06: Foreign Currency Translations Resulted in Overcharge to the USG

The auditor referenced inconsistencies in application of currency transactions.

PAE has reviewed the \$953 in questioned costs and netted this against the undercharges. There is a conflict between the questioned cost and the exchange rate underrun. PAE agrees with the auditor that the net cost to the government is \$669.

Finding 2018-07: Indirect Cost Adjustment Calculations Not Completed

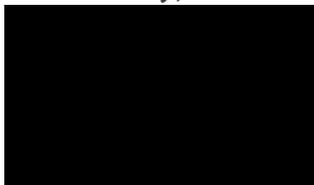
The auditor notes there was no indirect cost true-up for each year.

As noted in the auditor's report, PAE does not calculate indirect cost adjustments until the audit of PAE's indirect costs for each applicable year is completed by DCMA.

In past experience, the Department of State has not accepted indirect rates that are not final, and therefore, have no approved basis in billing.

PAE appreciates the opportunity to respond to this audit report, and we are available to discuss these responses at your earliest convenience.

Sincerely,



Contracts, PAE

APPENDIX B: AUDITOR'S REBUTTAL

Crowe LLP ("Crowe" or "we" or "us") has reviewed the letter dated October 18, 2018, containing PAE's ("PAE" or "the auditee") responses to the draft audit report. In consideration of those views, Crowe has included the following rebuttal to certain matters presented by the auditee. Crowe incorporates a rebuttal in those instances where management disagrees with the facts presented within the condition, does not concur with Crowe's recommendation, or provides additional documentation for review. In those instances where management either agrees with the finding or does not disagree with the facts in the finding, as presented, no rebuttal is provided. Using this framework, Crowe has incorporated one rebuttal to management's comments, below.

Finding 2018-01: Employee Worked More than the Authorized Six Consecutive Days

We have reviewed management's response regarding authorized work days and PAE's interpretation that the requirement only applies to guards and not exempt employees. Section F-008 of the contract states, "[t]he Contractor shall NOT work more than six consecutive days in any seven consecutive day period." The contract language does not differentiate between Contractor labor categories. PAE did not provide documentation explaining why certain employees were exempt from the requirement(s) and should be permitted to work more than six consecutive days in any seven consecutive day period and, therefore, should be excluded from the authorized work days requirement of the contract. In the absence of such documentation, we have not modified the finding. Pursuant to FAR 31.2, the Contracting Officer may review the documentation and make a final determination regarding support provided by PAE.

Finding 2018-02: Failure to Comply with Working Hours Restrictions

We have reviewed management's response regarding work hour restrictions and PAE's interpretation that the requirement only applies to guards and not exempt employees. Section F-008 of the contract states, "The Contractor shall work at least 8 hours per day, but NOT more than 10 hours per day." The contract language does not differentiate between Contractor labor categories. PAE did not provide documentation explaining why certain employees were exempt from the requirement(s) and should be permitted to work in excess of 10 hours per day and, therefore, should be excluded from the authorized work hour restrictions requirement of the contract. In the absence of such documentation, we have not modified the finding. Pursuant to FAR 31.2, the Contracting Officer may review the documentation and make a final determination regarding support provided by PAE.

Finding 2018-03: Insufficient Support for Cost or Price Reasonableness

We have reviewed management's response regarding the per hour rate and consider the information provided to be sufficient for purposes of supporting the rate that would be paid to an employee. However, PAE utilized a vendor to provide the services, which requires separate cost inputs than a direct hire and would not be directly comparable to the procurement process under review. PAE provided salary ranges for a senior level recruiter in the Washington, D.C., metropolitan job market. This is not considered a valid basis of comparison for the services provided by a vendor in Afghanistan. In addition, PAE did not provide documentation to support competitive bidding or a Noncompetitive Justification Form as required by PAE's internal policies.

Per PAE Policy Statement 732 on competition, "[c]ompetitive actions are required for all direct charge orders over \$3,500 (micro-purchase threshold) unless single/sole source justification is provided. Three or more offers should be solicited for any requirement over \$3,500."

Per PAE Policy Statement 731, *Non-Competitive Procurements*, "Any contemplated non-competitive procurements shall be documented on the Noncompetitive Acquisition Justification Form (PAE-PRO-003) and filed in the procurement file.

Therefore, we have not modified the finding. Pursuant to FAR 31.2, the Contracting Officer may review the documentation and make a final determination regarding reasonableness utilizing the alternative support provided by PAE.

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SIGAR's Mission

The mission of the Special Inspector General for Afghanistan Reconstruction (SIGAR) is to enhance oversight of programs for the reconstruction of Afghanistan by conducting independent and objective audits, inspections, and investigations on the use of taxpayer dollars and related funds. SIGAR works to provide accurate and balanced information, evaluations, analysis, and recommendations to help the U.S. Congress, U.S. agencies, and other decision-makers to make informed oversight, policy, and funding decisions to:

- improve effectiveness of the overall reconstruction strategy and its component programs;
- improve management and accountability over funds administered by U.S. and Afghan agencies and their contractors;
- improve contracting and contract management processes;
- prevent fraud, waste, and abuse; and
- advance U.S. interests in reconstructing Afghanistan.

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- Phone DSN Afghanistan: 318-237-3912 ext. 7303
- Phone International: +1-866-329-8893
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