

Inspector General's Budget Estimates for Audits of Certain Contractors' Costs Need Improvement

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For more information, contact: Kristen Kocielek at kociolekk@gao.gov and Allison Bawden at bawdena@gao.gov.

What GAO Found

Since establishment of its Incurred Cost Audits Division (ICAD) in 2021, the Department of Energy (DOE) Office of Inspector General (OIG) has used its own auditors, as well as auditors from other federal agencies and private accounting firms, to conduct the incurred cost audits. When establishing the ICAD, DOE's OIG did not sufficiently assess the resources needed to implement incurred cost audits of management and operating (M&O) contracts. Specifically, the OIG developed an \$18.7 million per year rough order of magnitude estimate based on limited data in 2021. As a result, the OIG's initial estimate substantially underestimated the resources needed. As of its fiscal year 2025 budget justification, the OIG estimated that conducting incurred cost audits will cost \$43.7 million per year. GAO found that the OIG's 2021 estimate had several limitations (see table).

Limitations of DOE OIG Rough Order of Magnitude Estimate

Limitation	Description
Audit entity	The OIG's estimate assumed that the OIG would use its own auditors. However, the OIG has used other audit entities to conduct audits with oversight by the OIG, and the cost of conducting the audits differs for each entity.
Audit activities	The OIG based the estimate on only the activities required for incurred cost audits and not on the additional audit services required for an effective program, such as reviewing contractor business systems.
Number of M&O contracts	The estimate assumed that the OIG would perform audits for 23 management and operating (M&O) contracts. The estimate did not account for the fact that the number of contracts may change over time.

Source: GAO analysis of Department of Energy (DOE) Office of Inspector General (OIG) documents. | GAO-25-107199

According to GAO's *Cost Guide*, a rough order of magnitude estimate can be helpful for examining differences in high-level alternatives but is not precise and should never be considered a budget-quality estimate. In contrast, developing a life cycle cost estimate entails identifying and estimating all cost elements that pertain to a program from initial concept through execution. The *Cost Guide* states that a life cycle cost estimate can support budgetary decisions, including determining the most cost-effective approaches. Further, using it as a budget baseline helps to ensure that all costs are fully accounted for so that resources are adequate for a selected approach. Developing life cycle cost estimates of the alternatives for conducting incurred cost audits—using its own auditors, using other audit entities with OIG oversight, or both—would better enable the OIG to determine the most cost-effective approach and request adequate funding.

The processes the OIG had in place when it began conducting incurred cost audits were generally consistent with applicable standards, but the chapter for these audits had not been codified in its audit manual. GAO found that the audit manual was generally consistent with generally accepted government auditing standards related to ethics, independence, professional judgment, competence and continuing professional education, and quality control. However, initially, there were some minor inconsistencies related to peer review, fieldwork, and reporting standards for performance audits. During GAO's audit, the OIG updated the manual to address noted inconsistencies and included a chapter for incurred cost audits. As a result, the design of the OIG controls over incurred costs audits is now consistent with applicable standards.

Why GAO Did This Study

DOE is one of the largest civilian contracting agencies in the federal government. In fiscal year 2023, DOE obligated about \$36.7 billion for M&O contracts. DOE's M&O contracts have inherent financial risks, as the contractor is allowed to withdraw funds without first submitting an invoice. To mitigate these risks, in 2021 the OIG established a division to audit incurred costs from these contracts and provide related contract audit services to DOE program offices.

The Joint Explanatory Statement to the Consolidated Appropriations Act, 2023 includes a provision for GAO to review the OIG's strategic planning for incurred cost audits. This GAO report examines the extent to which (1) the OIG assessed the resources needed to effectively implement incurred cost audits of M&O contracts and (2) the OIG's process for planning and implementing incurred cost audits of M&O contracts is consistent with applicable auditing standards.

GAO reviewed OIG documentation and interviewed DOE and OIG officials about the OIG's initial estimate and assumptions. GAO used its *Cost Guide* to identify the type of assessments that the OIG developed. GAO also assessed the OIG's controls to perform incurred cost audits for consistency with applicable audit standards.

What GAO Recommends

GAO recommends that the DOE Inspector General develop life cycle cost estimates of all relevant alternatives for conducting incurred cost audits. The OIG concurred with GAO's recommendation.