June 5, 2008

MEMORANDUM FOR JAMES A. WILLIAMS, COMMISSIONER
FEDERAL ACQUISITION SERVICE (Q)

FROM: DAVID K. STONE David K Stone
REGIONAL INSPECTOR GENERAL FOR AUDITING
GREAT LAKES REGION (JA-5)

SUBJECT: Audit of GSA Fleet's Alternative Fuel Vehicle Surcharges
Federal Acquisition Service
Report Number A070212/Q/5/P08005

This report presents the results of our audit of GSA Fleet's alternative fuel vehicle surcharges. A draft report was submitted to you for comment. The comments were considered in preparing the final report and are included in their entirety as an appendix. We especially wish to express our appreciation for the cooperation and help GSA Fleet provided us.

Section 810, Prompt Resolution of Audit Recommendations, of the National Defense Authorization Act (Act) (Public Law 104-106) directs that management decisions are required within six months of the audit report issue date. Nevertheless, as required by GSA Order ADM P 2030.2C, a time-phased plan of action addressing the report recommendation and the Management Decision Record for Internal Audit (MDR) should be submitted within 60 days. You should complete Section B of the attached MDR and return the complete package to the Assistant Inspector General for Auditing (JA), with a copy to the Internal Control and Audit Division (BEI).

Section 810 of the Act also requires that final action on all management decisions must be completed within 12 months of the audit report issue date; otherwise, the Office of Inspector General must report in its Semiannual Reports to Congress matters on which final actions have not been completed within 12 months of the report issue date. Therefore, it would be most beneficial if, to the extent possible, your time-phased action plan schedules actions to be completed within 12 months of the report issue date.

A Customer Satisfaction Questionnaire, developed to obtain your feedback regarding the usefulness of the audit and the report, is attached. Please have the primary user of the report complete the questionnaire. The completed questionnaire should be returned in the enclosed envelope to:

Director, Operations Staff (JAO)
General Services Administration
Office of Inspector General
18th and F Streets, NW Room 5316
Washington, DC 20405

We hope you find the report helpful to your operations. If you have any questions regarding the report, please contact Franklin Moy, Audit Manager, at (312) 353-6690, or Edward Cullen, Auditor-in-Charge, at (312) 353-6745.

Attachments

AUDIT OF GSA FLEET'S
ALTERNATIVE FUEL VEHICLE SURCHARGES
FEDERAL ACQUISITION SERVICE
REPORT NUMBER A070212/Q/5/P08005
JUNE 5, 2008

AUDIT OF GSA FLEET'S
ALTERNATIVE FUEL VEHICLE SURCHARGES
FEDERAL ACQUISITION SERVICE
REPORT NUMBER A070212/Q/5/P08005

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U.S. GENERAL SERVICES ADMINISTRATION
Office of Inspector General

Date: June 5, 2008

Reply to
Attn. of: Regional Inspector General for Auditing
Great Lakes Region Field Audit Office (JA-5)

Subject: Audit of GSA Fleet's Alternative Fuel Vehicle Surcharges
Federal Acquisition Service
Report Number A070212/Q/5/P08005

To: James A. Williams, Commissioner
Federal Acquisition Service (Q)

This report contains the results of our audit of GSA Fleet's (Fleet) alternative fuel vehicle surcharges. The audit was conducted to help Fleet evaluate its AFV surcharge procedures and to determine if the procedures were in compliance with legal and accounting requirements.

We concluded GSA Fleet's means of recouping the incremental costs it incurs furnishing alternative fuel vehicles to customers meet legal requirements and are reasonable in light of its need to control costs. To ensure sufficient funds are available to cover the added depreciation expense of AFVs, Fleet and FAS will need to monitor the amount of revenue directed to the Replacement Cost Pricing (RCP) account.

A copy of your response to the draft report is provided in Appendix A.

We hope the management and staff of GSA Fleet find the report helpful to their operations.

Sincerely,

Franklin M. Moy
Audit Manager
Great Lakes Region (JA-5)

230 South Dearborn Street, Suite 408, Chicago, IL 60604

AUDIT OF GSA FLEET'S
ALTERNATIVE FUEL VEHICLE SURCHARGES
FEDERAL ACQUISITION SERVICE
REPORT NUMBER A070212/Q/5/P08005

INTRODUCTION

Background

The Energy Policy Act of 1992 directed Federal agencies with fleets of 20 or more vehicles in metropolitan statistical areas to include increasing percentages of alternative fuel vehicles (AFVs) in their yearly vehicle acquisitions for metropolitan areas, culminating in the requirement 75 percent be AFVs in 1999 and thereafter. The Act also stated:

> The General Services Administration and any other Federal agency that procures motor vehicles for distribution to other Federal agencies may allocate the incremental cost of alternative fueled vehicles over the cost of comparable gasoline vehicles across the entire fleet of motor vehicles distributed by such agency.

Based on this legislation, subsequent Presidential executive orders, and business concerns, GSA Fleet (Fleet) established the practice of determining the anticipated incremental AFV charges for each customer agency annually. The incremental costs were collected as lump sums, unique vehicle rates, or surcharges assessed in the monthly billings of customers. Surcharge and lump sum revenues were deferred and amortized over the life of the AFVs. Only agencies that acquired AFVs were charged, and those paying through surcharges formalized the payment process through Memorandums of Understanding with Fleet.

The Energy Policy Act of 2005 amended the Energy Policy Act of 1992 to read:

> The General Services Administration ... shall allocate the incremental cost of alternative fueled vehicles over the cost of comparable gasoline vehicles across the entire fleet of motor vehicles distributed by such agency. (Emphasis added.)

The legal change resulted in Fleet assessing all customers a surcharge, but at varying rates, and in the surcharges no longer being deferred and amortized. Fleet asked for the audit because it was concerned with retaining procedures that allowed it to control AFV costs, while at the same time meeting legal requirements and accounting standards.

Objectives, Scope and Methodology

The audit objectives were to determine:

1. Are AFV incremental costs collected and recorded in accordance with laws, regulations and accounting principles?

2. Are the procedures for collecting and recording the incremental costs efficient and reasonable?

To accomplish our audit we visited the Financial Information Control Division, Payroll, Accounting and Financial Services Heartland Center, Kansas City, Missouri; the Financial Consulting and Analysis Division, Office of Finance, Washington, DC; the Budget and Finance Management Division, FAS Controller's Office, Arlington, Virginia; and the GSA Fleet headquarter offices, Arlington, Virginia to obtain information regarding the surcharges. We also reviewed applicable laws and analyzed GSA Fleet's vehicle data. The audit was carried out between August 2007 and February 2008 in accordance with generally accepted Government auditing standards.

RESULTS OF AUDIT

Brief

We concluded GSA Fleet's means of recouping the incremental costs it incurs furnishing alternative fuel vehicles to customers meet legal requirements and are reasonable in light of its need to control costs. To ensure sufficient funds are available to cover the added depreciation expense of AFVs, Fleet and FAS will need to monitor the amount of revenue directed to the Replacement Cost Pricing (RCP) account.

Finding and Recommendation

Finding – Accounting for Surcharges

The total revenue going into the RCP Account, which is now funded from AFV surcharges as well as RCP charges that are a part of the base lease rates, will need to be properly monitored to ensure the total in the fund is not excessive, and sufficient revenue remains available to cover the added depreciation expense of AFVs. Allowing the RCP charges to change without adjustments in the total monthly lease rates would provide additional revenue to cover depreciation expenses and prevent the funds in the RCP Account from becoming excessive.

The changes dictated by the Energy Policy Act of 2005 resulted in Fleet assessing all customers an AFV surcharge beginning in October 2006. However, many of the fundamentals of the previous system were retained. Although all agencies were charged something, Fleet negotiated with the major AFV users to establish the number of AFVs to be furnished, their anticipated total incremental cost, and the surcharges to be assessed to recover the costs. These negotiations took place through telephone conversations, meetings and emails, but memorandums of agreement or similar formal documents were not executed. Fleet monitored the collections from each agency, and as the desired amounts were collected, the surcharges were terminated.

These procedures allowed Fleet a means of recouping incremental AFV costs from customers that demanded models more costly than the norm for AFVs or quantities in excess of those mandated by Congress, and preventing unreasonable cross subsidizing between customer agencies. The incremental costs of hybrids and compressed natural gas vehicles have approached and exceeded $10,000 per vehicle, so if not monitored the costs can become substantial.

Fleet collects the total incremental costs of AFVs during the vehicles' first year of operation. The charges are recognized as revenue when billed, and added to the RCP account, a capital reserve account developed to cover the shortfall Fleet would otherwise experience in its accumulation of capital for replacement vehicles. It was set up in response to a 1978 Congressional authorization that allowed GSA to include an increment in the prices it charges customers to cover the replacement cost of vehicles. This increment was in addition to the price Fleet charged to recover the purchase price of the vehicle to be replaced. The money placed in this account "...shall be available only for replacement of such motor vehicles, equipment and supplies." Funds in it are not available to cover operating costs.

The depreciation calculations for the AFVs are based on their total capital cost, including the incremental AFV costs. However, the base monthly AFV lease rates do <u>not</u> include the AFV incremental costs. The base lease rates are those established to recover the capital cost for non-AFV gasoline fueled vehicles, not the higher cost AFVs.

For instance, if a gasoline fueled vehicle cost $15,000 and the alternative fueled version cost $17,000, the AFV incremental cost would be $2,000. Fleet collects the entire $2,000 in the year the vehicle is purchased for the customer. It is collected along with the incremental costs of all the newly acquired AFVs furnished the using agency for the current year, through a uniform surcharge added to the base monthly rates for all the vehicles leased to the agency. Once the total incremental charges for the agency's AFVs are collected, Fleet stops the surcharge for the remainder of the fiscal year.

As noted, the base monthly lease rate for the vehicle is the rate for a gasoline fueled vehicle. The lease rate is therefore set to recover the $15,000 (less salvage value) paid for the gasoline powered version of the vehicle, not the $17,000 paid for the AFV version. At the end of the life of the gasoline powered vehicle, Fleet will have recovered its original $15,000 investment through a combination of the monthly lease rates and revenue from sale of the vehicle. However, for the AFV, Fleet will not have recovered the $2,000 in the base lease rates because it was not included in the regular monthly charges for the vehicle. The $2,000 was recovered through the surcharges assessed the agency during the vehicle's first year of operation and added to the RCP account. The surcharges are placed in the RCP account because their purpose is to assist with the purchase of vehicles. The AFV surcharges are in addition to the RCP charge, which is part of the base lease rate designed to account for inflation. Revenue placed in the account is set aside for purchasing vehicles and is not available for operating expenses, including depreciation.

The depreciation schedule for the vehicle is based on its $17,000 purchase price. The depreciation expense for the vehicle over its expected life will be about $2,000 greater than the monthly lease revenue received for the vehicle. Prior to billing changes dictated by the Energy Policy Act of 2005, the surcharges were placed in a deferred account and amortized to current revenue over the expected life of Fleet's ownership of the AFVs. This resulted in the surcharge revenue increasing current income by approximately the same amount as the increased depreciation expense the incremental costs caused.

With the legislative changes that required Fleet to allocate the incremental costs over the entire fleet, Fleet no longer established signed agreements with customers ordering AFVs in a given year. It did negotiate surcharge rates with those customers ordering large numbers of AFVs, but charged a minimum rate for those ordering small quantities, or no AFVs. Even though many of the basics of the previous procedures were kept in place, not all surcharges totaled the incremental cost of AFVs purchased for the agency paying the surcharge. The surcharges also were no longer tied to signed agreements for specific type vehicles. As a result, surcharge revenue was no longer deferred and amortized, but was added to the RCP account. This opens up the potential of excess funds being set aside as reserve capital and not enough being available for the added AFV depreciation expenses. Monitoring the revenues going into the RCP account can avoid this outcome.

Many AFV surcharges are prepayments of part of the cost of vehicles agencies ordered, as was the case prior to the FY 2007 changes, and some are not. That is, while all agencies are required to contribute to AFV funding, not all agencies will order AFVs every year. Further, AFV surcharges are negotiated between Fleet's central office and agency headquarter operations, but vehicle ordering and replacement takes place locally. As a result there is not a precise match between projected and actual AFV surcharges.

Fleet could simplify accounting for AFV incremental costs by including them in overall vehicle rates. This would result in some agencies subsidizing the AFV purchases of other agencies much more than is currently the case. Because of its desire to control AFV costs and prevent unreasonable agency cross subsidizing, Fleet has elected to continue the surcharges.

Total surcharges for FY 2007 were over $11 million. The incremental costs for FY 2008 were anticipated at over $20 million at the beginning of the fiscal year, but actual incremental costs were about $14 million. Fleet's total annual revenue is over $1 billion per year.

After considering:

- the surcharges percentage of Fleet's annual revenue and their relative immateriality,
- the totals paid per agency in relationship to their annual payments to Fleet,
- the added cost of accounting for the surcharges in some other manner, and
- the flexibility provided GSA for setting aside revenue for replacing Fleet's vehicles,

we concluded the current surcharges and their placement in the RCP account are satisfactory. Fleet and FAS will need, however, to monitor the total revenue accumulated in the fund to ensure it is not excessive, and sufficient funds are being made available to cover the added depreciation expense of the AFVs.

Recommendation

We recommend to the Commissioner, Federal Acquisition Service,

1. GSA Fleet continue to add the alternative fuel vehicle surcharge revenue to the Replacement Cost Pricing account and monitor the account to assure the fund balance is appropriate.

Management's Response

The Commissioner, Federal Acquisition Service, concurred with the recommendation in his response to the draft report. A copy of his response is provided in Appendix A.

Internal Controls

No significant control weaknesses were noted during the audit.

AUDIT OF GSA FLEET'S
ALTERNATIVE FUEL VEHICLE SURCHARGES
FEDERAL ACQUISITION SERVICE
REPORT NUMBER A070212/Q/5/P08005

GSA

GSA Federal Acquisition Service

MAY 29 2008

MEMORANDUM FOR DAVID K. STONE
REGIONAL INSPECTOR GENERAL FOR AUDITING
GREAT LAKES REGION (JA-5)

FROM: JAMES A. WILLIAMS
COMMISSIONER
FEDERAL ACQUISITION SERVICE (Q)

SUBJECT: GSA Draft Report, "Audit of GSA Fleet's Alternative Fue Vehicle Surcharges, Federal Acquisition Service" (A070212/Q/5)

Thank you for the opportunity to review the above-referenced draft report. I generally concur with the report's findings and recommendation. Specific comments on some of the findings are provided in the attached statement.

Please call me at (703) 605-5400 if you have any questions. Your staff may contact Ms. Cathy Fick at (703) 605-5452 or catherine.fick@gsa.gov for additional information.

Attachment

cc: Andrew Patchan
Assistant Inspector General for Auditing (JA)

Edward Cullen
Auditor-in-Charge (JA-5)

U.S. General Services Administration
2200 Crystal Drive
Arlington, VA 20406-0003
www.gsa.gov

APPENDIX A

AUDIT OF GSA FLEET'S
ALTERNATIVE FUEL VEHICLE SURCHARGES
FEDERAL ACQUISITION SERVICE
REPORT NUMBER A070212/Q/5/P08005

FAS Comments on the GSA Draft Report,
"Audit of GSA Fleet's Alternative Fuel Vehicle Surcharges"
Report Number A070212/Q/5

Page 3, last sentence in the first paragraph under Finding — Accounting for Surcharges:
"~~Monitoring and adjusting~~ Allowing the RCP charges to change ~~that are part of the base lease rates~~ without adjustments in the total monthly lease rates would provide additional revenue to cover depreciation expenses and prevent the funds in the RCP Account from becoming excessive."

Last sentence on page 3, continuing to page 4:
"It was set as an increment in the prices it charges customers to cover the replacement cost of vehicles."

Page 5, second sentence of the second paragraph:
"That is, while all agencies are required to contribute to AFV funding every year, not all agencies will order AFVs every year."

APPENDIX B

AUDIT OF GSA FLEET'S
ALTERNATIVE FUEL VEHICLE SURCHARGES
FEDERAL ACQUISITION SERVICE
REPORT NUMBER A070212/Q/5/P08005

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