

# DCAA 2012 Updates

## National Defense Industrial Association

Roland Wick – Former DCAA Supervisory Auditor  
Consultant, McNew & Associates

Mike McNew – Former DCAA Senior Auditor  
President, McNew & Associates



*“Business Growth Through Effective Compliance”*

# Purpose

- This presentation provides general information on DCAA and related audit issues submitted from your members about DCAA.



***“Business Growth Through Effective Compliance”***

# Reference Data-DCAA Colorado Springs

- Effective November 20, 2011, the DCAA Colorado Springs Suboffice is aligned with the following Branch Office:

Utah Branch Office  
Central Region  
Defense Contract Audit Agency  
1270 West 2320 South, Suite F  
West Valley City, Utah 84119  
Phone 801.975.3555 and FAX 801.975.3599  
E-mail: dcaa-fao3911@dcaa.mil  
Joni H. Youngberg, Branch Manager

**The Utah Branch reports to the DCAA Central Region.**

**The office is still in transition.**

**Org code is 3911, ATK suboffice is 3912, COS suboffice is 3913**



***“Business Growth Through Effective Compliance”***

# Update on DCAA Organization in Colorado Springs

Regional Director	Tim Carr
RAM Utah Branch	Dan St. John
RAM/Virtual Team IC	Martha McKune
Branch Manager	Joni Youngberg
COS Supervisory Auditor	Wendy Medel/Virtual IC
	Rick Olmstead
	2 Temporary from Utah
ATK Supervisors -	Mark Saunders, John Pratt



*“Business Growth Through Effective Compliance”*

# What is DCAA Incurred Cost Audit Activity?

1. Specific areas that DCAA might be focusing on during incurred cost (IC) audits?
2. What are the plans for catching up on IC audits?



***“Business Growth Through Effective Compliance”***

# IC Audits

- New virtual incurred cost teams.
- Incurred costs through 2007 will be completed by the end of 2012. DCAA has established this as a primary audit goal.
- Wendy Medel is IC Virtual Supervisory Auditor in Colorado Springs.
- Due dates for reports must now be met and will be monitored.



***“Business Growth Through Effective Compliance”***

# IC Audits

## Major contractor IC audit program changes.

- *The most significant changes to the audit program include improved detailed audit steps covering areas such as:*
  - *direct labor costs*
  - *contractor compensation costs, and*
  - *excessive pass-through costs*
- *New **walkthrough** of the major contractor incurred cost submission to assure compliance with the criteria of FAR 42.703 and 52.216-7 (Allowable Cost and Payment). The risk assessment procedures have been expanded to better assist in establishing the audit scope and designing the required audit procedures. The risk assessment includes a step to obtain a walk-through of the incurred cost proposal with the contractor to facilitate the process for the auditor to gain an understanding of the basis of the claimed costs and related supporting documentation, significant controls, and the relevant policies/procedures and processes related to significant cost elements.*



*“Business Growth Through Effective Compliance”*

# IC Audits

The November 4, 2011 11-PPD-020(R) also requires the following for non-major contractors:

- *Policy has revised the Guide for Determining Adequacy of Contractor Incurred Cost Proposal to provide a more comprehensive guide for use in determining the adequacy of final indirect cost rate proposals at both major and non-major contractors. The auditors must evaluate the contractor's incurred cost proposal for adequacy upon receipt and immediately notify the contracting officer, and contractor, in writing, of significant inadequacies.*



*“Business Growth Through Effective Compliance”*



# IC Audits

- DCAA established significant increases to the number of sample items required to allow a compliant audit examination.
- Highlights of costs under added scrutiny include:
  - Air travel
  - Health Benefit costs
  - Lobbying
  - Subcontract costs
  - Labor and materials if no concurrent MAAR was accomplished.



# IC Audits

- **Increased subcontract surveillance and audit scope.** DCAA is looking for prime assurance the subcontract billings received are verified prior to passing the billings to the Government. Prime contractors should maintain subcontractor briefing, FAR 31 testing, and proper admin of subcontract.
- Subcontract costs are now getting extensive scrutiny and the adequacy of the subcontract ICE section is critical.
- Demonstrating that the prime has evaluated its subcontract costs will be a future emphasis.
- Consultants must have adequate support for costs.
- Time cards will be a very good idea for consultants and evidence of prime monitoring.
- Reconciliation of labor/payroll to 941s now **will not be overlooked** or minimized.



# Can DCAA have Full and Unaccompanied Complete Access to all Employees and Records?

## DCAA Guidance

December 19, 2008 08-PAS-042(R)

- Support includes access to **personnel**, in addition to the documentation/data supporting the contractor's assertion (e.g., cost records, policies and procedures, management reports).



*“Business Growth Through Effective Compliance”*

## Access to Records (CAM 1-504)

- b. In addition to access to specific cost records, access to records refers to:
  - contractor policies
  - procedures,
  - Systems,
  - management reports,
  - Personnel**,
  - minutes of its board of directors meetings
  - charter and bylaws, and
  - any other information source which affects and reflects the incurrence, control, and allocation of costs to contracts.



# Access to Records

- There is some dispute by contractors over access to personnel. Research shows potential for disagreement over statute language for requirement to provide access to personnel.
- DCAA has always maintained it has the right to interview and directly engage staff and personnel.
- There are legitimate practical reasons for contractors to provide DCAA access to its employees in support of an audit, including to improve the efficiency of the audit.
- Contractors and DCAA are usually able to reach a reasonable compromise.



# Access to Records

- Inherent in audit responsibility is the right of auditors to determine the specific records or other evidential matter needed to accomplish the audit.
- Auditors must adhere to generally accepted Government auditing standards in determining what comprises competent, relevant, and sufficient evidential matter.
- Auditors must use good judgment and rationale in deciding what contractor records or other evidential matter should be sought.
- In determining the sufficiency of evidence needed, auditors must consider the audit objective, the risk, and materiality of an error or misstatement in the area being audited and the effect on the audit opinion (see CAM 1-504.1.d.)



# Access to Records

- According to DoD guidance, **auditors must be prepared to discuss the basis for the request and to explain the underlying audit need** (see CAM 1-504.36.a).
- DCAA stating "**because I want it**" is not satisfactory or compliant with DoD guidance.
- Unusual or extensive requests must be made in writing by someone higher than the auditor (see CAM 1-504.36.e). "Unusual or extensive" is not defined so that could potentially become an issue in itself. Normal requests for labor interviews or process understanding would not be considered unusual.
- Auditors are not permitted to remove original records from the contractor premises. They can make (or request) copies of pertinent records for working paper documentation. However, auditors should not request contractors to reproduce records so that he/she can work at home (or another worksite)



# Access Conclusions

- DCAA has access to records rights under contract clauses and has a long history of access to personnel.
- **DCAA cannot simply have access to staff without specific reason and legitimate audit need.**
- A company management representative should be present in any interview.
- Before failure to release access to personnel make sure you get legal guidance.





## What is the status of moving contractors with an approved accounting system to Direct Bill?

- Contractors that maintain billing systems which meet the criteria in 6-1007.2 will be eligible to submit interim vouchers directly to Defense Finance and Accounting Service (DFAS), National Aeronautics and Space Administration (NASA), Maryland Procurement Office (MPO) and U.S. Army Corps of Engineers (USACE) paying offices.
- Not impossible to get direct billing, but unless DCAA completes internal control assessment, Direct Billing may not be assigned. Current IC audits may be required.



# What is the distinction between a consultant and subcontractor?

## Common understanding

- Consultants are normally individuals providing professional services.
- Subcontractor is one who takes a portion of a contract from the principal contractor or from another subcontractor. Do part of actual work effort.



# What is the distinction between a consultant and subcontractor?

## Under FAR-No difference for direct costs.

### 44.101 Definitions.

As used in this part—

“Subcontract” means any contract as defined in Subpart 2.1 entered into by a subcontractor to furnish supplies or services for performance of a prime contract or a subcontract. It includes but is not limited to purchase orders, and changes and modifications to purchase orders.

“Subcontractor” means any supplier, distributor, vendor, or firm that furnishes supplies or services to or for a prime contractor or another subcontractor.



*“Business Growth Through Effective Compliance”*

# What is the distinction between a consultant and subcontractor?

Things to consider:

- Direct vs indirect Cost
- Accounting policy for determining consultant vs. subcontracts
- FAR 31.205-33 Professional Services for consultants
- All FAR Part 31 for Subcontracts. ICE submissions



*“Business Growth Through Effective Compliance”*

# Subcontract Analysis & Controls

- What constitutes an adequate subcontractor cost/price analysis?
- Subcontract Award?
- Adequate prime contractor surveillance over subcontractors (including subcontract billings)?



# Subcontract Analysis & Controls

- Prime Responsibilities

- The prime contractor must assess all subcontractors to ensure they are responsible offerors in accordance with FAR Subpart 9.
- The prime contractor is responsible for evaluating the reasonableness of the subcontractor prices
- Analytical techniques and procedures described in section FAR 15.404-1 may be used, singly or in combination with others, to **ensure that the final price is fair and reasonable**
- The complexity and circumstances of each acquisition should determine the level of detail of the analysis required
- Price analysis shall be used when cost or pricing data are not required



***“Business Growth Through Effective Compliance”***

# Subcontract Analysis & Controls

- **Prime Responsibilities Continued**

- Cost analysis shall be used to evaluate the reasonableness of individual cost elements when cost or pricing data are required. Price analysis should be used to verify that the overall price offered is fair and reasonable
- Cost analysis may also be used to evaluate information other than cost or pricing data to determine cost reasonableness or cost realism
- The contracting officer, or prime contractor, may request the advice and assistance of other experts to ensure that an appropriate analysis is performed
- Any discrepancy or mistake of fact (such as duplications, omissions, and errors in computation) contained in the cost or pricing data or information other than cost or pricing data submitted in support of a proposal shall be brought to the contracting officer's attention for appropriate action



# Subcontract Analysis & Controls

- **Subcontract Price Analysis**

- You may select any of the following bases for price analysis:
- Other proposed prices received in response to the solicitation;
- Commercial prices including competitive published price lists, published commodity market prices, similar indexes, and discount or rebate arrangements;
- Previously-proposed prices and contract prices for the same or similar end items, if you can establish both the validity of the comparison and the reasonableness of the proposed price;
- Parametric estimates or estimates developed using rough yardsticks;  
or
- Independent Government Estimates.
- These can all be derived through market research.



***“Business Growth Through Effective Compliance”***



# Subcontract Analysis & Controls

- **Subpart 9.1—Responsible Prospective Contractors**
- **9.103 Policy.**
- (a) Purchases shall be made from, and **contracts shall be awarded to, responsible prospective contractors only.**
- (b) No purchase or award shall be made unless the contracting officer makes an affirmative determination of responsibility.
- (c) **The award of a contract to a supplier based on lowest evaluated price alone can be false economy if there is subsequent default, late deliveries, or other unsatisfactory performance** resulting in additional contractual or administrative costs. While it is important that Government purchases be made at the lowest price, this **does not require an award to a supplier solely because that supplier submits the lowest offer. A prospective contractor must affirmatively demonstrate its responsibility, including, when necessary, the responsibility of its proposed subcontractors**



*“Business Growth Through Effective Compliance”*

# Subcontract Analysis & Controls

- **15.404-3 -- Subcontract Pricing Considerations.**
- (b) The prime contractor or subcontractor shall --
  - (1) Conduct appropriate cost or price analyses to establish the reasonableness of proposed subcontract prices;
  - (2) Include the results of these analyses in the price proposal; and
  - (3) When required by paragraph (c) of this subsection, submit subcontractor cost or pricing data to the Government as part of its own cost or pricing data.
- (c) Any contractor or subcontractor that is required to submit cost or pricing data also shall obtain and analyze cost or pricing data before awarding any subcontract, purchase order, or modification expected to exceed the cost or pricing data threshold...
- (3) Subcontractor cost or pricing data shall be submitted in the format provided in Table 15-2 of 15.408



# Subcontract Analysis & Controls

- **44.201-1 –Consent requirements.**
- (a) If the contractor has an approved purchasing system, **consent is required for subcontracts specifically identified by the contracting officer in the subcontracts clause of the contract.** The contracting officer may require consent ...if...it is required to protect the Government adequately because of the subcontract type, complexity, or value, or because the subcontract needs special surveillance.
- (b) **If the contractor does not have an approved purchasing system, consent to subcontract is required** for cost-reimbursement, time-and-materials, labor-hour, or letter contracts, and also for unpriced actions (including unpriced modifications and unpriced delivery orders) under fixed-price contracts that exceed the simplified acquisition threshold.



# Entertainment/Employee Morale What Changed? Holiday Parties?

- **FAR 31.205-14 -- Entertainment Costs 1984 FAR (Effective 1 April 1984)**

Costs of amusement, diversion, social activities, and any directly associated costs such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities are unallowable (but see 31.205-13 and 31.205-43).

- **FAC 84-15 (Effective 7 April 1986)**

Costs of amusement, diversion, social activities, and any directly associated costs such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities are unallowable (but see 31.205-1 and 31.205-13). Costs of membership in social, dining, or country clubs or other organizations having the same purposes are also unallowable, regardless of whether the cost is reported as taxable income to the employees.

- **FAC 90-31 (Effective 1 October 1995)**

Costs of amusement, diversion, **social activities**, and any directly associated costs such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities are unallowable.



# Entertainment

## DCAA Contract Audit Manual 7176 December 23, 2011 7-2104

- (4) Taken together, the statute and the cost principles at 31.205-13, Employee morale, and 31.205-14, Entertainment, expressly disallow costs which some contractors may have considered reasonable and allowable prior to the effective date of the current rule, October 1, 1995. Examples of such costs include, but are not limited to:
- (a) Entertainment provided as part of public relations, employee relations, or corporate celebrations;
  - (b) Gifts to anyone who is not an employee;
  - (c) Gifts to employees which are not for performance or achievement or are not made according to an established plan or policy;
  - (d) Compensation awards of entertainment, including tickets to shows or sports events, or travel; and
  - (e) Recreational trips, shows, picnics, or parties.**



# QUESTIONS?



***“Business Growth Through Effective Compliance”***

# Contact Information

McNew & Associates:

Email: [mcnew@mcnewassociates.com](mailto:mcnew@mcnewassociates.com)

Web: [www.mcnewassociates.com](http://www.mcnewassociates.com)

Mike McNew,

President, CEO

Tel: (719) 685-7897 x1046

Email: [mmcnew@mcnewassociates.com](mailto:mmcnew@mcnewassociates.com)

Gary Henry, CPCM, PMP

Vice President, Operations

Tel: (719) 685-7897 x1049

Email: [ghenry@mcnewassociates.com](mailto:ghenry@mcnewassociates.com)



***“Business Growth Through Effective Compliance”***