

# DCAA Issues Causing the Greatest Pain to Government Contractors



**Sheri Buchanan**  
Director –  
HR Consulting



**Lynne Nalley, CPA**  
Director – GovCon  
Compliance



Redstone  
Government Consulting



**Phone:** (256) 704 - 9800

**Email:** LNalley@RedstoneGCI.com

# Lynne Nalley, CPA

## Director – GovCon Compliance

- Director with Redstone GCI, advising contractors on audit readiness, CAS, DFARS systems, and cost submissions
- 35+ years with DCAA and DCMA, specializing in audits and regulatory compliance
- Former DCAA Regional Technical Specialist and Assistant for Quality, supporting 20+ field offices and delivering NASBA-certified CAS and audit training
- Extensive audit expertise in pricing proposals, financial capability, accounting/estimating systems, and unallowable costs
- DCMA Commercial Item Group project lead and lead analyst, focused on contractor assertions, price analysis, and CPSR support
- Recognized for guiding contractors through complex audit challenges with compliance-focused strategies



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**Phone:** (256) 704 - 9800

**Email:** SBuchanan@RedstoneGCI.com

# Sheri Buchanan

## Director – Human Resources Consulting

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- Director of HR Consulting at Redstone GCI, advising contractors on compliance, policies, compensation, and labor mapping
- 20+ years of HR experience with a focus on government contracting
- Certified Compensation Professional (CCP) with expertise in pay equity, benefits, and executive compensation reviews
- Supports clients with SCA and DBA compliance, OFCCP requirements, and Department of Labor regulations
- Experienced in compensation plans, reasonableness assessments, and pricing disputes involving DCAA
- Background in HR leadership across compliance, recruiting, investigations, and management training
- Provides project-based and ongoing HR consulting tailored to GovCon needs



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# Learning Objectives

All pain no gain

- ✓ Compensation and Bonuses
- ✓ Relocation Costs
- ✓ Transaction Testing
- ✓ Remote Employee Travel
- ✓ Intercompany Transfers
- ✓ Common Control Buildings/Equipment
- ✓ Billing Issues
- ✓ Home Office Costs
- ✓ Forward Pricing
- ✓ Equitable Adjustments or Claims
- ✓ DCAA Exit Conferences
- ✓ DCAA Reorganization

# Compensation

- What our Clients are seeing:
  - Questioned costs due to
    - Lack of justification for basis
    - Lack of policy and/or not following policy
    - Lack of justification in determining reasonableness
  - Documentation expectations are very high

# Compensation

## FAR 31.205-6 Compensation for Personal Services



- (a) General. Compensation for personal services is allowable subject to the following general criteria...
  - (2) The total compensation for individual employees or job classes of employees must be reasonable for the work performed; however, specific restrictions on individual compensation elements apply when prescribed.
  - (3) The compensation must be based upon and conform to the terms and conditions of the contractor's established compensation plan or practice followed so consistently as to imply, in effect, an agreement to make the payment.

# Compensation

## FAR 31.205-6 Compensation for Personal Services



### (b) Reasonableness

- (2) Compensation not covered by labor-management agreements. Compensation for each employee or job class of employees must be reasonable for the work performed. Compensation is reasonable if the aggregate of each measurable and allowable element sums to a reasonable total. In determining the reasonableness of total compensation, consider only allowable individual elements of compensation. In addition to the provisions of **31.201-3**, in testing the reasonableness of compensation for particular employees or job classes of employees, consider factors determined to be relevant by the contracting officer. Factors that may be relevant include, but are not limited to, conformity with compensation practices of other firms -
- (i) Of the same size;
  - (ii) In the same industry;
  - (iii) In the same geographic area; and
  - (iv) Engaged in similar non-Government work under comparable circumstances.

# Compensation

## FAR 31.205-6 Compensation for Personal Services



- (f) Bonuses and incentive compensation (1) Bonuses and incentive compensation are allowable provided the -
  - (i) Awards paid or accrued under an agreement between contractor and the employees before services are rendered or pursuant to an established plan or policy followed so consistently as to imply an agreement to make such a payment
  - (ii) **Basis** for award is supported (*Emphasis Added*)
- (p) Limitation on allowability of compensation.  
2025 Fiscal Year: \$671,000 compensation cap



# Compensation

## What Redstone GCI Recommends



- Written compensation plan, to include processes and internal ownership
  - Base compensation
  - Bonus and incentive compensation
- Documentation
  - Survey data
  - Details noted

# Compensation

## What Redstone GCI Recommends

- Understand compensation < cap does not mean it is reasonable
- Review Job Descriptions, contractual LCAT requirements and resumes
- Cross-functional awareness and communication



# Relocation Costs

- What our Clients are seeing:
  - Questioned costs due to
    - Lack of justification for basis
    - Lack of policy and/or not following policy
    - Lack of justification in determining reasonableness

# Relocation Costs

FAR 31.205-35  
Relocation costs

- (a) Relocation costs are costs incident to the permanent change of assigned work location (for a period of 12 months or more) of an existing employee or upon recruitment of a new employee. The following types of relocation costs are allowable ...:
- (5) Other necessary and reasonable expenses normally incident to relocation, such as disconnecting and connecting household appliances; automobile registration; driver's license and use taxes; cutting and fitting rugs, draperies, and curtains; forfeited utility fees and deposits; and purchase of insurance against damage to or loss of personal property while in transit.

# Relocation Costs

FAR 31.205-35  
Relocation costs

- (b) The costs described in paragraph (a) of this subsection must also meet the following criteria to be considered allowable:
  - (1) The move must be for the benefit of the employer.
  - (2) Reimbursement must be in accordance with an established policy or practice that is consistently followed by the employer and is designed to motivate employees to relocate promptly and economically....
  - (5) For miscellaneous costs of the type discussed in paragraph (a)(5) of this subsection, a lump-sum amount, not to exceed \$5,000, may be allowed in lieu of actual costs.

# Relocation Costs

## FAR 31.205-35 Relocation costs

(b)(6) (i) Reimbursement on a lump-sum basis may be allowed for any of the following relocation costs when adequately supported by data on the individual elements (e.g., transportation, lodging, and meals) comprising the build-up of the lump-sum amount to be paid based on the circumstances of the particular employee's relocation:

- (A) Costs of finding a new home, as discussed in paragraph (a)(2) of this subsection.
- (B) Costs of travel to the new location, as discussed in paragraph (a)(1) of this subsection (but not costs for the transportation of household goods).
- (C) Costs of temporary lodging, as discussed in paragraph (a)(2) of this subsection.

...

(c) The following types of costs are unallowable: .....  
(e.g. loss on home, real estate brokers fees, property insurance, mortgage life insurance, owner's title policy, property taxes, etc.)

# Relocation Costs

## What Redstone GCI Recommends

- Written policy to include processes and internal ownership
- Documentation of basis and reasonableness
- Cross-functional understanding and communication



# Incurred Cost - Transaction Testing

- What our Clients are seeing:
  - Business/First class travel questioned based on no documentation to support exceptions in FAR 31.205-46(b)
  - Indirect costs below the micro-purchase threshold questioned because no/little documentation (expect same documentation as large purchases)



# Incurring Cost - Transaction Testing

FAR 31.205-46  
Travel costs

- (b) Airfare costs in excess of the lowest priced airfare available to the contractor during normal business hours are unallowable except when such accommodations require circuitous routing, require travel during unreasonable hours, excessively prolong travel, result in increased cost that would offset transportation savings, are not reasonably adequate for the physical or medical needs of the traveler, or are not reasonably available to meet mission requirements. However, in order for airfare costs in excess of the above airfare to be allowable, the applicable condition(s) set forth above must be documented and justified.

# Incurring Cost - Transaction Testing

## FAR 13.203 Purchase guidelines

- (a) Solicitation, evaluation of quotations, and award.
  - (1) To the extent practicable, micro-purchases shall be distributed equitably among qualified suppliers.
  - (2) Micro-purchases may be awarded without soliciting competitive quotations if the contracting officer or individual appointed in accordance with 1.603-3(b) considers the price to be reasonable.
  - (3) The administrative cost of verifying the reasonableness of the price for purchases may more than offset potential savings from detecting instances of overpricing. Therefore, action to verify price reasonableness need only be taken if-
    - (i) The contracting officer or individual appointed in accordance with 1.603-3(b) suspects or has information to indicate that the price may not be reasonable (e.g., comparison to the previous price paid or personal knowledge of the supply or service); or
    - (ii) Purchasing a supply or service for which no comparable pricing information is readily available (e.g., a supply or service that is not the same as, or is not similar to, other supplies or services that have recently been purchased on a competitive basis).
- (b) Documentation. If competitive quotations were solicited and award was made to other than the low quoter, documentation to support the purchase may be limited to identification of the solicited concerns and an explanation for the award decision.

# Incurred Cost - Transaction Testing

## What Redstone GCI Recommends



- Update policy to include travel exceptions for airfare and lodging per FAR 31.205-46(b) and maintain the documentation
- Train staff on exceptions and document contemporaneously on expense report
- Costs below the micro purchase threshold should be documented as fair and reasonable with a simple statement (i.e., three quotes and detailed price analysis not required)

# Remote Employee Travel

- What our Clients are seeing:
  - DCAA found no written policy – cited as internal control weakness
  - Questioned travel costs to and from office as unreasonable and therefore unallowable

# Remote Employee Travel

FAR Part 31 does not specifically address remote employees

So, you must look to FAR 31.201-3, Determining reasonableness

- (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. Reasonableness of specific costs must be examined with particular care in connection with firms or their separate divisions that may not be subject to effective competitive restraints. No presumption of reasonableness shall be attached to the incurrence of costs by a contractor. If an initial review of the facts results in a challenge of a specific cost by the contracting officer or the contracting officer's representative, the burden of proof shall be upon the contractor to establish that such cost is reasonable.
- (b) What is reasonable depends upon a variety of considerations and circumstances, including -
  - (1) Whether it is the type of cost generally recognized as ordinary and necessary for the conduct of the contractor's business or the contract performance;
  - (2) Generally accepted sound business practices, arm's-length bargaining, and Federal and State laws and regulations;
  - (3) The contractor's responsibilities to the Government, other customers, the owners of the business, employees, and the public at large; and
  - (4) Any significant deviations from the contractor's established practices.

# Remote Employee Travel

## What Redstone GCI recommends



- Written policy on remote employees and travel to the office/Government site
- Reimbursement should follow FAR 31.205-46 Travel and document any exceptions (e.g., lodging, airfare)
- When hiring a remote employee address the basis and why remote employee with the additional travel costs is reasonable (e.g., Skill set not available in local area) and put it in the employee's file

# Intercompany Transfers

- What our Clients are seeing:
  - DCAA recommends Contracting Officer obtain certified cost or pricing data when a commercial determination not submitted with the proposal
  - Review actual transfers and question profit if transfer not made at price during incurred cost

# Intercompany Transfers

## FAR 31.205-26 Material Costs



- (e) Allowance for all materials, supplies and services that are sold or transferred between any divisions, subdivisions, subsidiaries, or affiliates of the contractor under a common control shall be on the basis of cost incurred in accordance with this subpart. However, allowance may be at price when -
  - (1) It is the established practice of the transferring organization to price interorganizational transfers at other than cost for commercial work of the contractor or any division, subsidiary or affiliate of the contractor under a common control; and
  - (2) The item being transferred qualifies for an exception under 15.403-1(b) and the contracting officer has not determined the price to be unreasonable.
- (f) When a commercial product or commercial service under paragraph (e) of this section is sold or transferred at a price based on a catalog or market price, the contractor -
  - (1) Should adjust the price to reflect the quantities being acquired; and
  - (2) May adjust the price to reflect the actual cost of any modifications necessary because of contract requirements.



# Intercompany Transfers

## What Redstone GCI Recommends

- Written policy on interdivisional transfers (address cost and price)
- Draft a commercial determination when transfers are at price
- Actual transfer needs to be made at price in the financial records

# Common Control – Buildings/Equipment

- What our Clients are seeing:
  - DCAA questioned the difference between claimed “market rate” and the constructive cost of ownership as unallowable when any common control exists

# Common Control – Buildings/ Equipment

## FAR 31.205-36 Rental Costs

(b) The following costs are allowable:

- (1) Rental costs under operating leases, to the extent that the rates are reasonable at the time of the lease decision, after consideration of -
  - (i) Rental costs of comparable property, if any;
  - (ii) Market conditions in the area;
  - (iii) The type, life expectancy, condition, and value of the property leased;
  - (iv) Alternatives available; and
  - (v) Other provisions of the agreement.
- (3) Charges in the nature of rent for property between any divisions, subsidiaries, or organizations under common control, to the extent that they do not exceed the normal costs of ownership, such as depreciation, taxes, insurance, facilities capital cost of money, and maintenance (excluding interest or other unallowable costs pursuant to part 31), provided that no part of such costs shall duplicate any other allowed cost. Rental cost of personal property leased from any division, subsidiary, or affiliate of the contractor under common control, that has an established practice of leasing the same or similar property to unaffiliated lessees shall be allowed in accordance with paragraph (b)(1) of this subsection.

# Common Control – Buildings/ Equipment

## DCAA Guidance

- Who has the actual decision-making process over lease
- Reasonableness of the lease terms (other comparable leases, market pricing)
- FASB ASC 850-10-20 defines control

# Common Control – Buildings/ Equipment

## What Redstone GCI Recommends



- Written policy on rental costs addressing related party/common control
- Common control not defined in FAR – document percentage of ownership and who has control over decision making
- Documentation of:
  - Ownership cost calculation to support monthly charge or
  - Justification for market rate if unaffiliated company leases building/equipment from company

# Billing Issues

- What our Clients are seeing:
  - DCAA issued an accounting system weakness for:
    - Not withholding fee
    - Not updating billings within 60 days after settlement of final indirect rates

# Billing Issues

## FAR 52.216-8 Fixed Fee

## FAR 52.216-7 Allowable Cost and Payment Clause



## FAR 52.216-8 Fixed Fee

- (b) Payment of the fixed fee shall be made as specified in the Schedule; provided that the Contracting Officer withholds a reserve not to exceed 15 percent of the total fixed fee or \$100,000, whichever is less, to protect the Government's interest.

## FAR 52.216-7 Allowable Cost and Payment Clause

- (d) (2)(v) The Contractor shall update the billings on all contracts to reflect the final settled rates and update the schedule of cumulative direct and indirect costs claimed and billed, as required in paragraph (d)(2)(iii)(I) of this section, within 60 days after settlement of final indirect cost rates.

# Billing Issues

## What Redstone GCI Recommends



- Written policy on fee withhold and submitting adjustment vouchers in the required period
- Individual signing final rate agreement should provide rates to billing for adjustment voucher processing
- Ensure you are withholding fee in accordance with contract terms



# Home Office Costs

- What our Clients are seeing:
  - DCAA questioned corporate allocations based on a fixed amount agreement
  - DCAA questioned using the Total Cost Input of the divisions as the base

# Home Office Costs

## Home Office Costs Allocated to Segment



- **CAS 403, Allocation of home office expenses** to segments
- **FAR 31.201-4, Determining allocability** – A cost is allocable if it is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship.
  - (c) Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.
- **FAR 31.203, Indirect costs**
  - (c) The contractor shall accumulate indirect costs by logical cost groupings with due consideration of the reasons for incurring such costs. The contractor shall determine each grouping so as to permit use of an allocation base that is common to all cost objectives to which the grouping is to be allocated. The base selected shall allocate the grouping on the basis of the benefits accruing to intermediate and final cost objectives. When substantially the same results can be achieved through less precise methods, the number and composition of cost groupings should be governed by practical considerations and should not unduly complicate the allocation.

# Home Office Costs

## What Redstone GCI Recommends



- Even if you have no CAS covered contracts, consider CAS 403 and document what you are doing with wording from CAS 403

# Forward Pricing

- What our Clients are seeing:
  - DCAA questioned costs when cost or price analysis of subcontracts is not included in proposal
  - Determine cost or price analysis inadequate and question part or all the subcontract costs because they used a different approach
  - Take exception to escalation factors used

# Forward Pricing

## Cost or Price Analyses



- **FAR 15.408 Table 15-2** requires cost and price analyses to be included as part of a FAR part 15 proposal submission
- **DFARS 252.215-7009** Proposal Adequacy Checklist states a matrix can be included identifying date of cost and price analyses if they are not available when proposal submitted

# Forward Pricing

## What Redstone GCI Recommends



- Include a matrix of cost and price analyses with expected completion date in proposal
- Still required to perform cost analysis when denied access to subcontractor data
- Ensure escalation factors are not too broad (e.g., Consumer or Producer Price index)
- Try and get quotes instead of escalating historical costs
- Documentation for judgmental factors, learning curves, etc. should be clear in Basis of Estimate

# Equitable Adjustments or Claims

- What our Clients are seeing:
  - DCAA states in the report narrative that “the contractor is not entitled to a cost based on FAR 31.205” instead of questioning the cost and leaving entitlement to the Contracting Officer (this is misleading)

# Equitable Adjustments or Claims

- Requests for Equitable Adjustments and Claims
  - DCAA reviews quantum (dollar amounts)
  - Contracting Officer determines entitlement (legal determination to the claim)
- DCAA's guidance
  - Can include observations on entitlement in Other Matters; however, they do not represent audit findings



# Equitable Adjustments or Claims

## What Redstone GCI Recommends



- During exit conference, request DCAA remove entitlement language from report narrative
- Make the point in your contractor's response that entitlement is to be addressed by the contracting officer and auditor is to focus on the allowability and allocability of costs

# DCAA Exit Conferences

- What our clients are seeing:
  - DCAA doesn't hold an exit conference or provide the draft report
  - Receive a statement of conditions and recommendations (appendices) but not the opinion, which in some cases could recommend system disapproval
  - Factual differences are not provided – (e.g., proposed historical prices and quotes available, proposed a different learning curve then historical curve, etc.)
  - Contractor provides information that existed and resolves audit finding – DCAA won't change the report and says respond to ACO after the report is issued
  - Gives less than a week to respond to report drafts and won't allow extension

# DCAA Exit Conferences

- DCAA Contract Audit Manual on Exit Conferences
  - Provide a copy of draft report (including opinion, exhibits, and statement of conditions)
  - Proposals – discuss factual differences (don't disclose questioned cost)

# DCAA Exit Conferences

## What Redstone GCI Recommends

- Request DCAA provide the opinion paragraph when draft report provided
- When requesting an extension, copy the contracting officer



# DCAA Reorganization

- What our Clients are seeing:
  - New auditor not familiar with their system
  - Audit takes longer
  - Auditor performs audit remotely using email and there are misunderstandings
  - Questions cost that the previous auditor didn't question
  - Auditor uses analytics and tests more transactions than prior auditor

# DCAA Reorganization

- DCAA Reorganizing
  - Restructuring into Land, Sea, and Air Directorates
  - Closing or consolidating 40 suboffices

# DCAA Reorganization

## What Redstone GCI recommends



- Schedule in person meeting with auditor at the entrance conference
- Prepare a walkthrough presentation on any system audit
- Prepare a presentation of organization, rate structure, and other information for new auditor
- If auditor remote, set up zoom call with auditor/supervisor to provide walkthrough
- Stay engaged and be proactive

# Best Practices

- ✓ Make sure you have Written Policies and Procedures – Review them regularly
- ✓ Have walkthroughs on all audits
- ✓ Contemporaneous documentation for high-risk transactions
  - Airfare/Lodging Exceptions
  - Common Control – Buildings/Equipment
  - Intercompany transfers at price for commercial
  - Commercial determinations
- ✓ When an auditor goes dark – assume it is a bad thing



# FAR Part 31.201 Documentation

## FAR 31.201-2(d) states:

- It is contractor's responsibility to properly support proposed or billed costs to demonstrate allowability
- Failure to have adequate documentation to substantiate allowability may result in questioned costs (*Emphasis added*)

**May Equals Must To DCAA**

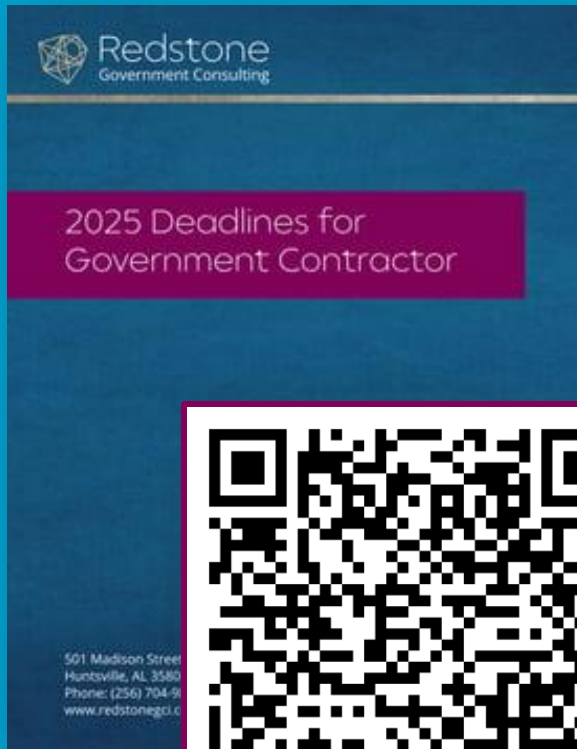
# Questions and Discussion



# 2025 Critical Deadlines for Government Contractors

This guide provides you with all of the essential information and dates you need to know, including:

- Important deadlines for your internal departments
  - Accounting,
  - Human Resources,
  - Contracts & Subcontracts, and
  - Government Compliance
- Contract performance and delivery deadlines
- Deadlines for reporting and compliance requirements
- Deadlines for audits and reviews



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Redstone  
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[info@RedstoneGCI.com](mailto:info@RedstoneGCI.com)

[www.RedstoneGCI.com](http://www.RedstoneGCI.com)

501 Madison Street SE, Ste .100  
Huntsville, AL 35801

(256) 704 - 9800