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DCAA Audit Policy on Billing System Oversight

By Michael Steen, CPA, Senior Director at Redstone Government Consulting, Inc.

In late September, DCAA revised its audit policy (14-PPS-017; September 26, 2014) for billing system oversight and with many DCAA audit policies, because of the implementation time lag, contractors are only now beginning to feel the impact of a significant change in a DCAA audit policy. The "billing system oversight" is implicitly a code name for DCAA's pre-payment audits of public vouchers submitted by contractors on cost type or T&M (Time and Material) contracts wherein DCAA now links its incurred cost proposal risk assessment ("high" or "low" for any given contractor) to DCAA's risk assessment of that contractor's invoices. DCAA instructs its auditors to prepare a contractor specific risk determination and pre-payment voucher sampling plan for high risk contractors based upon DCAA's risk determination for that contractor's most recent incurred cost proposal (that risk determination is primarily a function of the last completed audit of a prior indirect cost proposal). For a contractor whose most recent incurred cost proposal has been deemed low risk, that contractor's vouchers are similarly low risk and the sampling plan will be determined by using charts prepared by DCAA Headquarters (influenced by numbers and average amounts of vouchers). Although auditing standards include professional judgment on the part of the auditor, in this case field offices/auditors will not adjust the sampling plan for low risk contractors.

DCAA's policy asserts that one objective is to improve the consistency and efficiency of billing oversight and unquestionably there will be greater consistency to the extent DCAA HQs has provided non-adjustable charts which define the number of vouchers to be audited. However, none of this ensures any improvement in the efficiency of the audit and as evidenced by clients, there is absolutely no (contractor) efficiency in terms of the volume of supporting documents now required to satisfy a DCAA field auditor for this or any other audit. Suffice to say that even if the contractor is considered low risk, if/when DCAA initiates a pre-payment audit of a contractor voucher; the auditor will

THIS ISSUE:

test a cost by requesting multiple forms of documentation to support a single transaction. For example, direct labor is no longer tested at a summary level (e.g. job cost report traced to labor distribution) because now the auditor could also expect timesheets, evidence of the employee's physical existence and evidence of payment (i.e. a cancelled payroll check or equivalent).

DCAA's pre-payment voucher audits are one more example of auditor intrusions which can be very time consuming, diverting significant contractor resources to accommodate the auditors time compressed demands (in many cases, all requested records are required by the next day). It should be noted that this effort and the associated labor costs could be solely related to a cost type contract (or cost type contracts); hence, the question of cost allocability. In terms of how to charge this time, a contractor would be well served if it considered direct charging this time/labor cost to the specific cost type contract. Cleary, the time is for the benefit of a particular cost type contract; thus meeting the definition of a direct cost under FAR 31.201-4). For that matter, similar cost allocability logic would apply to the time/cost to prepare indirect cost rate proposals as well as any time to support contract close-out. As long as DCAA continues to unilaterally increase its demands for contractor resources solely to support DCAA audits, the contractor should consider assigning its costs to the contract or contracts which have caused and which "benefit" from the time and cost to support DCAA audits. Under Government Auditing Standards (GAGAS) DCAA is free to define the scope of its audits; however, the contractor is equally free to record those costs to the benefitting cost objective allowing the government to directly pay for the cost of services which are caused by and solely benefit a particular government contract.

Allowable vs. Unallowable Travel Costs: Avoiding Recurring Issues in 2015

By Darryl L. Walker, CPA, CFE, CGFM Senior Director at Redstone Government Consulting, Inc.

Experience with clients who have undergone audits of claimed incurred travel costs during this past year illustrates a continued disconnect between contractors and auditors in interpretation of FAR 31.205-46, Travel costs. We found that certain contractors seem to repetitively misapply travel cost FAR provisions, resulting in unnecessary exposure to questioned costs and/or a protracted resolution process with the government over the same issues over multiple years.

Many contractor travel cost allowability problems are those which should not have arisen in the first place had they followed the regulations, or (in fairness to some contractors) had auditors correctly applied regulations in examining incurred travel expenses. Nonetheless, it is perplexing that many of the same problems or contractor lapses in identifying unallowable travel costs seem to arise year after year.

A few of the recurring contractor dilemmas in filtering unallowable, or substantiating allowability of, incurred travel costs follow:

- **Per diem ceilings**—Amounts within the definition of per diem include (1) lodging and (2) meals & incidentals (M&I), and government contractors are subject to the total lodging/M&I daily ceiling (stipulated within applicable government travel regulations) and not to the individual lodging and M&I ceilings set forth in the travel regulations. Defense Contract Audit Agency (DCAA) audit guidance has made this clear, nonetheless, a few ill-informed auditors insist on calculating allowability of claimed per diem costs using the individual ceilings; unfortunately, many contractors tend to follow this thinking when calculating allowable and unallowable costs. Message to contractors, read the regulations and the related DCAA guidance (DCAAM 7-1002.3c(2)), and push back when a government auditor insists on using separate lodging and separate M&I ceilings for calculating unallowable costs.

- **Lodging taxes**—Lodging taxes are no longer a component of the per diem value (the allowabiliy of which is subject to per diem ceilings); lodging taxes are treated as a separate reimbursable miscellaneous expense similar to auto rental, parking fees, etc. However some contractors still include lodging taxes within the daily lodging value for purposes of determining excess (unallowable) per diem costs, thus overstating unallowable per diem costs and therefore not billed to the government customer.

Lodging taxes (state sales, county, local, , etc.) are allowable (as long as reasonable and supported by documentation, e.g., lodging receipt), although differing opinions exist as to whether taxes incurred as a consequence of lodging costs in excess of daily per diem values would be unallowable as a "directly associated" cost. The cost principle does not address this condition, although arguably taxes attached to excess lodging costs over the ceiling would be unallowable as long as the incurred tax is assessed using a measurable factor of the base lodging amount (e.g., tax rate(s) x daily base room amount). Where assessment of lodging taxes are not (often as a matter of local or state statute) clearly a measurable value via a correlation to the base amount, contractors may be able to justify allowability of all such taxes (i.e. a fixed daily tax independent of the room rate). Also be forewarned that for most international travel the tax is included in the lodging per diem.

- **General documentation**—FAR 31.205-46(a)(7) states that travel costs are allowable only if information identifying location, purpose of trip, and name of personnel/relationship to company is evident. However, the manner or type of documentation in which this information is displayed is not stipulated, although some government officials have questioned travel costs because, for example, a separate Travel Request (TR), a "signed" travel expense report, and/or trip report were not prepared. Although DCAA has its own list of documentation expectations (book, diary, account book, or similar records), that list is general, and contractors are not held to specifically named travel forms, data displays or accounting records, as long as trip information when viewed in totality is clear as to the employee who traveled, and the date/place of the trip. An employee travel expense report may include all three documentation components, or maybe the addition of a TR is required to enhance the trip purpose.

- **Payment of fixed vs. actual per diem expenses to employees**—Contractors have the option of paying its employees per diem based on actual expenses, a fixed per diem amount (equal to or lower than travel regulation ceilings), or a hybrid of the two (typically actual lodging and a fixed daily M&I). If the company's policy is to pay employees based on actual expenses, contractors should expect the government to require receipts or other evidence of actual expenses incurred. Many contractors elect to pay a fixed M&I amount to employees (using the hybrid method), however still require actual expense receipts be provided by the employees.

  Be aware that requiring actual expense receipts is logical with respect to lodging; however, with respect to M&I expenses reimbursed bases upon fixed per diems, it defeats the purpose of minimizing administrative effort in processing travel expense reports, and invites auditors to unnecessarily request those receipts for audit. DCAA guidance states that where fixed amounts are paid to employees not exceeding the per diem ceilings (for either per diem component), there is a presumption that those costs are reasonable and detailed receipts are unnecessary.

Averting repetitious travel expense challenges can often be achieved through a more precise understanding of relevant regulations and a willingness to challenge audit positions where questioned costs are not correctly connected to the regulations. Repetitively plowing the same ground in overcoming recurring audit issues or incorrectly applying the cost principles is detrimental to the company in terms of time and money.

Where company policies or practices are weak in correctly supporting incurred travel costs, contractors should strengthen practices and internal controls to avert continued self-inflicted wounds. And where companies feel they are steam-rolled by the government via erroneous interpretation of the travel cost principles, those companies should grow a back-bone and consider challenging those issues when they arise.

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Federal Circuit Affirms Government Not Obligated to Purchase ID Contract Minimum Quantities

By Darryl L. Walker, CPA, CFE, CGFM, Senior Director at Redstone Government Consulting, Inc.

The Federal Circuit Court of Appeals (case 2014-1507) affirmed a ASBCA (Armed Services Court of Contract Appeals) decision regarding a breach of contract complaint filed by Day Danyon Corporation and determined that the contractor was not entitled to receive the guaranteed minimum quantity of 1,000 Collapsible Joint Modular Intermodal Containers (JMICs) under an Indefinite Quantity (ID) contract with a two year performance period.

The contract stipulated a minimum ordering quantity of 500 units for each twelve month contract period over two year contract performance time frame or a total of 1,000 units. In case no. 2014-1507, the Federal Circuit ruled that the Day Danyon incorrectly interpreted the contract language with respect to the time frame in which the government should have placed all orders for the two year period. The court stated that contract did not require the exercise of the full minimum order of 1,000 units within an ordering cycle that would have ended four months prior to the end of the two-year contract.

Day Danyon was awarded the ID contract on April 23, 2009 for a two year period, the first and second twelve month periods ending April 23, 2010 and April 23, 2011, respectively. The government placed orders for 500 units before the end of the first twelve-month period, but shipment of completed units was delayed for various reasons. On December 24, 2010, the contractor submitted to the contracting office a $720,700 certified claim, the value for the additional 500 units, asserting that contract language required the government to order the remaining minimum quantity no later than 120 days before the end of the contract (April 23, 2011).

The contracting officer responded that the two year base period had not yet expired stating that the claim was premature and would not be paid. On April 20, 2011, three days prior to the end of the two year ordering period, the contracting officer terminated the contract for default, and thereafter the contractor resubmitted its claim. Day Danyon appealed the contracting officer's decision citing breach of contract, the ASBCA rejected the company's claim yielding to the government's motion for summary judgment, and the company appealed to the Federal Circuit.

In its decision related to the breach of contract complaint, the Federal Circuit determined that the contract language was "clear and unambiguous" stating "orders may be issued on this contract for a period of two years" from date of award, meaning that the government had until April 23, 2011 to place remaining minimum quantity orders. The court agreed that the "120 day period" contract verbiage was ambiguous but rejected Day Danyon's interpretation that contract terms would effectively "prohibit orders placed after December 24, 2010". On the contrary, the court decision found that orders could be placed until the last day of the two-year contract period.

The court's decision under case 2014-1507 did not opine on a separate ASBCA decision regarding the termination for default.

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Arlington, VA

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Hilton Head Island, SC

July 21-23, 2015 – The Masters Institute in Government Contract Costs
Hilton Head Island, SC

August 18-20, 2015 – The Masters Institute in Government Contract Costs
Sterling, VA

August 20-21, 2015 – Government Contract Audits: Dealing with Auditors and Mitigating Audit Risk
Sterling, VA

October 5-6, 2015 – Accounting Compliance for Government Contractors
Arlington, VA

Instructors:

- Mike Steen
- Scott Butler
- Cyndi Dunn
- Asa Gilliland
- Darryl Walker
- Courtney Edmonson
- Cheryl Anderson
- Robert Eldridge

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In achieving government contractor goals, all consulting services are planned and executed utilizing a quality control system to ensure client objectives and goals are fully understood; the right mix of experts with the proper experience are assigned to the requested task; clients are kept abreast of work progress; continuous communication is maintained during the engagement; work is managed and reviewed during the engagement; deliverables are consistent with and tailored to the original agreed-to scope of work, and; follow-up communication to determine the effectiveness of solutions and guidance provided by our experts.

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Specialized Training

Redstone Government Consulting, Inc. will develop and provide specialized Government contracts compliance training for client / contractor audiences. Topics on which we can provide training include estimating systems, FAR Part 31 Cost Principles, TINA and defective pricing, cost accounting system requirements, and basics of Cost Accounting Standards, just to name a few. If you have an interest in training, with educational needs specific to your company, please contact Ms. Lori Beth Moses at lmoses@redstonegci.com, or at 256-704-9811.

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Redstone Government Consulting, Inc.

NEW ADDRESS
Huntsville, AL
4240 Balmoral Drive SW, Suite 400
Huntsville, AL 35802
T: 256.704.9800

Email: info@redstonegci.com
On the web: www.redstonegci.com

