



DCAA and Senator McCaskill – the “Friendship” Continues

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

In her letter dated October 20, 2017 to the DOD Comptroller, Senator Claire McCaskill has become one more source of criticism of DCAA's incurred cost backlog. This “friendship” traces back to 2008-2009 when Senator McCaskill used a GAO Report (GAO-08-857) to publicly berate and belittle DCAA for DCAA's failures to follow government auditing standards. Ms. McCaskill, who fashions herself to be an auditor, was ultimately responsible for the removal of DCAA's Director (April Stephenson), a new Director who came from Army Audit, and major changes to DCAA audit policies (emphasizing compliance with auditing standards at the cost of audit efficiencies). Although DCAA over-reacted with ultra-conservative audit policies (resulting in audits now taking 600 hours versus 60 hours before the McCaskill “intervention”), the fact is that Ms. McCaskill's involvement was a primary factor in DCAA's exhaustive but highly inefficient audits. All too obvious, no DCAA Director wants to endure the public humiliation of appearing before Claire McCaskill (to explain audits which fail to comply with government auditing standards); hence, the end result has been essentially the same number of DCAA auditors producing approximately 10% of the number of audits (44,000 annually before and 4,600 annually after the 2008-2009 McCaskill intervention).

Fast forward to 2017 when Ms. McCaskill, citing the risk of improper payments and inability to reallocate funds as a byproduct of the inventory of overaged contracts awaiting closeout, requested a GAO review. The GAO report (GAO-17-738 issued in October 2017) addressed five civilian agencies (not DOD) and noted that none of them had critical elements to track and oversee contract closeout. Not exactly a DCAA issue; however, the GAO also reported on the lack of timely reimbursable audit support from DCAA (civilian agencies must reimburse DOD for DCAA audit services) including the lag time (885 days) between contractor submission of an indirect cost proposal (ICP) and the audit as well as the number of ICPs awaiting audit (14,208 as of 9/30/2016 which is less than one-half the 31,000 awaiting audit as of 9/30/2011).

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In terms of “helping” DCAA, the GAO recommended that DCAA assess and implement options to reduce the audit time and to assess the effects of multi-year audits on DCAA and contractors. (DCAA note to the GAO, thanks for all of the really specific help). Apparently, Senator McCaskill isn’t going to wait on DCAA’s “assessments” and is tasking DOD with responding to the following questions:

1. What is the current inventory of incurred cost audits at DCAA?
2. What are the plans and expected timeline for reducing DCAA’s audit backlog to 18 months of inventory?
3. The Department (DOD) stated in its response to the GAO that it plans to assess and implement options for reducing the lag-time and to conduct a comprehensive analysis of the use of multi-year audits by March 31, 2018. Please describe the status and timeline for completion of these promised actions.

Regarding the current inventory (reported by the GAO as 14,208 as of 9/30/2016), it is of more than passing interest that DCAA’s 2016 Report to Congress only reported an inventory of 4,716 incurred cost submissions as of 9/30/2016. DCAA also reported that its 9/30/2016 inventory was equivalent to 17.6 months (translated, DCAA receives 3,200 ICPs annually). DCAA’s 2016 Report to Congress also noted that its high-water mark was an inventory of 21,000 ICPs as of 9/30/2011. Perhaps Ms. McCaskill is on to something in terms of asking DCAA for the current inventory of incurred cost audits given that the GAO reported significantly higher counts than did DCAA in its report to Congress (4,716 vs. 14,208...not exactly a minor variance). However, Ms. McCaskill is failing to ask the “other” inventory question, does a simple count of ICPs mask the issue of potentially having an inventory of disproportionately large number of large dollar value ICPs?

Regardless of the potentially valid issue involving unreconcilable differences in ICP inventory count, Ms. McCaskill’s criticisms and impatience are just a tad-bit hypocritical. Her previous inquisition which led to the removal of a DCAA Director is a primary reason why DCAA over-audits. DCAA is not without fault, but its reaction to the early GAO reports became magnified in the wake of Ms. McCaskill’s

public show of in-affection toward DCAA. And now this Senator wants explanations as to why DCAA has an incurred cost backlog, a backlog for which an honorable person would accept at least some responsibility. From DCAA to Senator McCaskill, thanks for your continuing “friendship”.

DCAA’s Latest Adequacy Checklist- CAS Cost Impacts

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

DCAA has created one-more adequacy checklist, in this case the eight-page “CAS Cost Impact Adequacy Tool” to complement other adequacy checklists or tools including:

- Incurred cost submission adequacy checklist (Based on FAR 52.216-7(d)(iv))
- Forward contract pricing bid proposal adequacy checklist (DFARS 252.215-7009)
- Forward pricing rate proposal adequacy checklist (DFARS 215.403-5)
- Pre-award accounting system adequacy checklist (Standard Form 1408)
- Screening checklist for claims or other proposals (not on DCAA’s website)
- Checklist for conducting floor-checks (not on DCAA’s website)

Although DCAA asserts that its ubiquitous use of checklists results in mutual benefits to contractors and to DCAA auditors, the fact is that DCAA will not initiate an audit unless a contractor proposal can first pass the adequacy checklist. Unfortunately and inexcusably, DCAA’s checklists make it all-too easy for an auditor to avoid the audit (i.e. checklists with subjective criteria which opens the door for adequacy or inadequacy interpretations applied to the same facts). In all-too many cases, a contractor corrects the first list of inadequacies only to be notified of other inadequacies (not initially detected by the auditor who would rather do checklists than do the audit).

In the case of the newly minted CAS Cost Impact Adequacy tool (“tool” is code for checklist), a cursory review suggests that everything on the eight-page list is connected to a

contractual requirement (FAR 52.230-6 with links to FAR 30.600). However, the “tool” only provides references and not the explicit regulatory verbiage; thus, DCAA freely paraphrases and/or embellishes. For example, item 6 asks if the cost impact proposal is in accordance with the contractor’s policies and procedures, which begs the questions:

- What FAR Clause requires a contractor to have a policy covering the preparation of CAS cost impacts?
- What if the cost impact proposal complies with FAR 52.230-6, but not the contractor’s policy and procedures?
- Why is item 6 even in an adequacy tool?

Another observation, criteria with inconsistent requirements, for example item 5 “if requested by the CFAO did the contractor provide a list of the affected CAS-covered contracts and subcontracts” while item 10 states “does the contractor’s proposal include the impact on all affected or potentially affected CAS covered contracts and subcontracts”. By implication, even if the CFAO has not requested the list, DCAA will reject the cost impact if it does not include the impact on all affected or potentially affected contracts (and exactly what is a “potentially affected” contract?). Lastly and eerily similar to DCAA expectations for an adequate indirect cost rate proposal, DCAA’s CAS cost impact tool item 13 asks: “Did the contractor provide actual calculations and related formulas in electronic format?” Nothing in any regulation or contractual clause requires electronic formats including formulas (reference to Excel); however, that doesn’t stop DCAA from insisting on these items which make life immeasurably easier for the auditor (hint: making life easier for the auditor is a primary factor built into each of DCAA’s adequacy checklists even if the contractor incurs significant costs to prepare an adequate proposal (primarily to ease the burden on DCAA).

One final observation, DCAA will continue to develop and to utilize checklists which will be an embellishment of the actual contractual requirements. In large part, checklists yield standardized proposal or cost impact formats making it much easier for auditors to understand contractor submissions instead of inconveniencing auditors by requiring them to understand “non-standardized” contractor assertions. It doesn’t matter that streamlining in the 1990s included the elimination of a number of SFs (Standard Forms) and deference to individual contractor formats, we’ve simply returned to standard forms through DCAA’s unchallenged

creation of checklists. As DCAA has continued to deploy this strategy, the effect should have been increased audit efficiencies by cleverly shifting resource requirements from DCAA to the contractors. That said, it’s even more difficult to understand how DCAA could go from issuing 44,000 audit reports in 2007 to 4,600 in 2016.

Miscellaneous Contract Compliance in the News

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

Contractor settles false claim allegations for \$9.2 million. The Department of Justice (DOJ) announced the settlement for a contractor “knowingly overbilling the government for labor on US Contracts” even though the DOJ also stated that “the claims made in the complaint were allegations only and there had been no determination of liability”. In addition to the civil settlement, the DOJ reported that three individuals plead guilty to criminal charges (perhaps confirming the Fall 2015 Sally Yates memo that the DOJ was going to start pursuing individuals in addition to seeking financial settlements with the corporation/contractor). The DOJ reported that the settlement was originally raised in a Qui Tam lawsuit by a former employee of the contractor (the ex-employee received \$1,590,144 as his “finders’ fee”).

Although we have no direct insight into this particular issue and settlement, it is a reminder that false claims act violations (or allegations) most commonly come from “inside information” for which the original source is motivated by his or her percentage of the recovery. Also a reminder that government contractors have more at stake than the amount of the settlement, including unallowable legal costs (FAR 31.205-47) and in some cases unallowable directly associated costs (employees with some involvement in responding to the investigation and its endless stream of civil investigative demands for documents). Lastly, the risk of debarment or suspension (FAR Subpart 9.4).

Coincidentally, there was an indirectly related article (published in *Auditing: A Journal of Practice and Theory*) which stated that financial rewards can actually discourage whistleblowing. Examples included conditions which might be

below award thresholds such as \$1 million for SEC violations and the somewhat perverse logic of delayed whistleblowing to allow the damages to build over time. Per this study, in the absence of knowledge of potential financial rewards, individuals are more likely to be whistleblowers solely to report a wrong...or so we would like to think. In the case of the \$9.2 million settlement and \$1.6 million reward, apparently the whistleblower was good with the amount of his reward or concerned that someone else might beat him to the whistle.

Resolution of DCAA Findings on IRS Contracts---Taxpayers Beware

In what might be a significant understatement of the word significant, Treasury IG (Inspector General) issued an audit report (2017-10-019) titled: *Resolution of DCAA Findings of Questioned Costs Need Significant Improvement*. Highlights (or low-lights) included the following:

- The IRS paid about \$5.7 million to DCAA for DCAA reimbursable audits from 2005-2014
- The IG reviewed 25 DCAA audit reports which had questioned \$80 million and determined that the IRS could only document \$545,000 in recoveries (although a slight over-simplification, for every \$1 recovered, the IRS spent \$10 for the audit services)
- More than \$22 million could not be recovered because of the lack of timely actions by the IRS (which triggered the six-year statute of limitations FAR 33.206). What we have is untimely DCAA audits followed by even more untimely actions by IRS contracting officers
- IRS office of procurement was unable to produce any of the 48 contract files requested by the IG that were related to the 25 DCAA audits

The good news, the IRS agreed with the IG recommended corrective actions; hence, we will never ever see another IG report like this on...at least not until the next one.

Have and Have-Nots: How Does a Small Business Get an Approved System?

Guest Article by Lynn Oakes, Director of Contracts, Interfuze Corporation

I found out recently that in October 2016 Defense Contract Management Agency (DCMA) issued a class deviation to raise the FAR 44.302(a) Contractor Purchasing System Review (CPSR) threshold from \$25 Million to \$50 Million (threshold is annual sales to the government excluding commercial and competitively awarded fixed price). While this approach makes sense to ease the burden on smaller contractors and on DCMA, this approach appears to have unintended consequences in terms of reducing small business contracting opportunities because there will be fewer CPSRs with fewer systems approvals, while solicitations continue to favor companies that have approved systems.

It's been a while since the General Services Administration (GSA) One Acquisition Solution for Integrated Services (OASIS) competition but everyone familiar with that solicitation understood how important approved system were to the scoring; CPSR alone was worth 500 points! And that solicitation set the stage for other solicitations source selection criteria that similarly award points for approved systems. For example, the Naval Air Systems Command (NAVAIR) recently released a second draft solicitation for the Program Management (PM) Contractor Support Services (CSS) Multiple Award Contract (MAC). Interestingly the first draft included a scoring sheet that awarded 500 points for an approved purchasing system And while the second draft removed the points from the self-scoring worksheet for approved purchasing system, Section M.4.3(b) of the draft solicitation still states that "Offeror's who have approved Systems, Certifications and Clearances will be considered more favorably." Although that statement might be removed from the final release, we also have the much-anticipated GSA Alliant 2 and Alliant 2 Small Business draft solicitation evaluation criterion include points for approved Contractor Purchasing Systems.

In a similar vein, the Defense Contract Audit Agency (DCAA) has been performing fewer incurred cost audits and even fewer system audits under the guidance of Class Deviation

2012-O0013 dated July 24, 2012. The Class Deviation sets forth the policy by which DCAA assesses risk associated with incurred cost proposals, and therefore the criterion under which DCAA decides not to select a proposal for audit. This Class Deviation has been instrumental in helping DCAA start to close the gap on the backlog of incurred cost audits (the subject of the first article in this newsletter).

A side-effect of the Class Deviation is that the reliability of a contractor's "approved" Accounting System becomes questionable, particularly for smaller businesses (larger ones generally trip the "low risk" sampling criteria more frequently and therefore have more recent audits). In many cases, small businesses have an Accounting System that was approved five to ten years ago but hasn't been reviewed since because its contracts fall into the low risk category. Theoretically, the lack of an approved system won't prevent an award but may delay it. In the case of a contractor without an approved Accounting System or with a dated approval, the Contracting Officer can request an Accounting System audit and hold the award until the system is approved but in some cases, the solicitations require government approved accounting system (a requisite for a responsive proposal).

In order to address some of DCAA's audit backlog, the 2017 and 2018 National Defense Authorization Acts have or may have sections authorizing final incurred cost audits from certified public accounting (CPA) firms. The move to accept commercial audits of incurred cost proposals will allow DCAA to catch up on their backlog; however, there is another similar fix that DCAA, DCMA, DoD, and Congress should consider.

While allowing (or forcing) DoD and/or DCAA to consider using independent CPA audits of incurred cost proposals, DOD (DCAA and/or DCMA) should allow third party audits of Contractor Business Systems (Accounting, Purchasing, Estimating, etc.). The criterion against which the systems must be audited already exists and therefore is the framework against which the third-party auditors must operate. The third-party auditors would assess companies against the established criterion and determine if a contractor is compliant with the requirements. In essence, it would be like getting an International Organization for Standardization (ISO) certified Quality System. The systems would then be deemed as an "Audited" system instead of an "Approved" system. If DCAA or DCMA still wanted to approve the system, the audit findings themselves could be submitted to DCAA or DCMA for review and approval but that could defeat the purpose of having third-

party audits (particularly if DCAA second-guessed the audit scope).

The benefits of moving to third party *Audited Systems* instead of DCAA/DCMA *Approved Systems* are many:

1. All contractors, as part of doing business, will have *Audited Systems* against government established criterion, resulting in reliable business systems for contracting purposes and removing the "have" and "have not" dilemma that small businesses increasingly find themselves when bidding for work that give additional points or outright requires preexisting systems approval.
2. The government will save money because DCAA will not be required to audit contractor Accounting Systems and DCMA will not be required to audit Contractor Purchasing Systems (at least not initially; they'd still want to do CPSRs for contractors that perform \$50 million or more of purchasing but that justifies the Class Deviation they are pursuing even more). This will in fact shift the cost of these audits from the government to private industry. Interestingly, when I worked for large businesses I was against moving to this but having worked at a small business, I now believe the additional cost is worth it from a business development aspect in that it will allow the business the opportunity to pursue solicitations that require *Audited Systems* (no longer categorized as *Approved Systems*).
3. DCAA will continue to catch up on the backlog of incurred cost proposal audits by shifting more of its workforce from system audits to proposal and incurred cost audits. This will greatly benefit the government because real dollars are connected with programs (before money is spent) and incurred costs (after money is spent) and any savings is a direct savings. DCAA could still do the risk assessment consistent with the Class Deviation, could revise its risk assessment values to expand its samples and therefore its audits on direct dollars, and/or could still consider using independent CPA firms to do some of the incurred cost proposal audits.
4. Agencies and Contracting Officers should be pleased that *Audited Systems* could become evaluation criteria that won't get protested because contractors have the means to obtain it. Without this change, it's

likely that solicitations that require *Approved Systems* will more likely be protested as the gap between the “haves” and “have-nots” increase.

The benefits are many and benefit everyone. DCAA audits less. Contractors will have *Audited Systems*. And Contracting Officers and Agencies can depend on Contractors having these *Audited Systems*.

Training Opportunities

2017 Redstone Government Consulting Sponsored Seminar Schedule

COMING SOON

2017 Federal Publications Sponsored Seminar Schedule

December 6-7, 2017 – [Accounting Compliance for Government Contractors](#)
DC Metro Area

Go to <http://www.fedpubseminars.com/> and click on the Government Contracts tab.

Blog Articles to our Website

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Employee Stock Ownership Plans, Cost Allowability and DCAA Audit Risks (Part I)

Posted by Cyndi Dunn on Wed, Sep 13, 2017 – [Read More](#)

Seminar, Government Employees and Gratuities

Posted by Michael Steen on Tue, Aug 29, 2017 – [Read More](#)

Training Costs on Government Contracts

Posted by Cheryl Anderson on Tue, Aug 15, 2017 – [Read More](#)

Possible Recoveries from a Wage Determination Increase/Decrease

Posted by Charles Hamm, Esq. on Wed, Aug 9, 2017 – [Read More](#)

What to Expect from a DCAA Floor Check

Posted by Kimberly Basden on Thu, Aug 3, 2017 – [Read More](#)

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CFO Roundtable

Redstone Government Consulting, Inc., Radiance Technologies, Inc., and Warren Averett are sponsoring a CFO/Controller roundtable for Government Contractors.

All Government contractor CFO’s or Controllers are invited to participate. The meetings are held quarterly and will include lunch and networking from 11:30am – 1:00pm. The next meeting is TBD. Participants will be notified via email announcements for all future locations and seminar topics.



The CFO Roundtable is **free** to attend. All participants will be invited to share topics of interest and the group will be interactive. Redstone GCI, Radiance Technologies, and Warren Averett will strive to provide speakers on topics that are of interest to the group each quarter. Please provide us your email address and we will notify you 30 days in advance of each meeting. RSVP's are required.

Sign up for CFO Roundtable updates [here](#).

About Redstone Government Consulting, Inc.

Our Company's Mission Statement: RGCI enables contractors doing business with the U.S. government to comply with the complex and challenging procurement regulatory provisions and contract requirements by providing superior cost, pricing, accounting, and contracts administration consulting expertise to clients expeditiously, efficiently, and within customer expectations. Our consulting expertise and experience is unparalleled in understanding unique challenges of government contractors, our operating procedures are crafted and monitored to ensure rock-solid compliance, and our company's charter and implementing policies are designed to continuously meet needs of clients while fostering a long-term partnership with each client through pro-active communication with our clients

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.



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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