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DCAA's Latest Request to Contractors: "Do You want to request a multi-year incurred cost audit?"

By Michael Steen, CPA, Senior Advisor

Although it may appear to be a bit unusual (and somewhat reminiscent of the song from Frozen, "Do you want to build a snowman"), DCAA is now contacting contractors asking: "Do you want to request a multi-year audit?" (and if you answer in the positive, use a DCAA-provided template for this purpose). DCAA initiates this as part of its pre-planning for its incurred cost audits (typically covering two consecutive years' final indirect cost rate proposals submitted as required by FAR 52.216-7(d)) and in so doing, DCAA cites the 2018 NDAA Section 803(b)(1)(E)(B). That section of the 2018 NDAA limits the use of multi-year auditing to that conducted "when the contractor being audited submits a written request, including a justification for the use of multi-year auditing, to the Under Secretary of Defense (Comptroller)". Oddly enough, the 2018 NDAA places this requirement under the topic of "Conditions for the Use of Qualified Auditors to Perform Incurred Cost Audits" (in reference to independent auditors, other than DCAA, to perform incurred cost audits to eliminate the backlog by October 1, 2020). Regardless of its misplacement in the 2018 NDAA, the requirement was effective December 17, 2017 (the date the 2018 NDAA was passed).

DCAA's template (for the contractor to request a multi-year audit) defers (sort of) to the contractor to specify the years (which have already been identified by DCAA) and it also defers to the contractor to justify the request (but conveniently

THIS ISSUE:

Redstone Government Consulting

provides an example justification from the contractor: "We believe it is more efficient to combine multiple years of incurred cost in one audit rather than concurrently supporting two or more individual year audits"). DCAA's suggested justification inserts the word "concurrently" as if DCAA would simultaneously audit two or more years as separate audits (the wording should be: We are requesting DCAA to concurrently perform multiple years of incurred cost in one audit rather than separately performing audits of each year's incurred costs). Perhaps obvious, but a contractor requesting a multi-year audit should consider using its own wording and also recognize that multi-year (concurrent/combined) audits should be more efficient, but there are no guarantees (particularly if the auditor is marginally competent and spends needless hours auditing "in the weeds").

Over and above the requirement for the contractor to request multi-year incurred cost audits, Section 803(g) of the 2018 NDAA also introduced some requirements for "Timeliness of Incurred Cost Audits". In particular, the Secretary of Defense (presumably through DCAA), shall notify a contractor within 60 days after receipt of an incurred cost submission from the contractor whether the submission is a qualified submission (adequate "Final Indirect Cost Rate Proposal" as defined in FAR 52.216-7(d)) and evaluated using DCAA's "Checklist for Determining Adequacy of Contractor's Incurred Cost Proposal". Additionally, with respect to qualified incurred cost submissions received after December 17, 2017, audit findings shall be issued for an incurred cost audit not later than one-year after the date of receipt of such qualified incurred cost submissions (the one-year requirement is subject to waiver by the DoD Comptroller). The timeliness requirements are the topic of a DCAA MRD (18-PIC-001, dated January 29, 2018), a document which accurately states that the one-year requirement (for DCAA to issue the audit findings) is from the date of receipt of the qualified submission versus the date DCAA determines the submission to be adequate.

In general, Section 803 of the 2018 NDAA is good news for contractors, at least those who have (for years) been experiencing the impact of the expanding incurred cost backlog. Unfortunately, it has taken an "Act of Congress" to compel DCAA to get current (although we still don't know exactly how DoD will measure "current" as of October 1, 2020). There maybe some unintended consequences, including DCAA's more stringent adequacy reviews ("more stringent" is code for DCAA adequacy reviews which reject final indirect cost rate proposals for subjective and inconsistent interpretations of adequacy). Additionally, the one-year requirement (for DCAA to issue its audit findings) will translate into shortened response times for contractors to provide documentation and/or explanations in response to DCAA audit inquiries. DCAA auditors will predictably issue audit findings which question "unsupported costs" which might be attributable to contractor in-process responses which miss auditor imposed due dates.

It remains to be seen if improved audit timeliness result in the desired outcome of improving the timeliness of contract close-outs. Unfortunately, timely reporting of audit issues simply does not equate to timely issue resolution of those audit issues, yielding final rates which can then be applied to final (close-out) vouchers.

DoD Waiver on TINA (Truth in Negotiations Act) Threshold and the Interrelated Impact on CAS (Cost Accounting Standards) Applicability—Increased to $2 Million

By Michael Steen, CPA, Senior Advisor

As coincidentally required by the 2018 NDAA (similar to the requirements discussed in the preceding article), DP/PAP (Defense Pricing/Procurement and Acquisition Policy) issued a class deviation which increases both the TINA and the CAS Thresholds to $2 million effective for contracts executed on or after July 1, 2018. The class deviation applies to DoD contracts and will remain in effect until after it is incorporated into FAR or rescinded; hence, contracts with agencies other than DoD will continue to use the lower $750,000 thresholds.

Although this provides some administrative relief to government contractors, that "relief" only applies to those DoD contracts which fall between $750,000 and $2 million and with respect to CAS, small businesses are already exempt from CAS; hence, the only small business benefit is with respect to the marginal relief from TINA. However, there may be a more noticeable benefit to prime contractors to the extent subcontracts below $2 million will no longer require TINA flow-downs. In terms of its practical implications, the increased TINA contract value threshold is unlikely to provide any

measurable benefit to contracting actions which might be subject to a post-award TINA compliance audits. The reason, very low audit risk because DCAA has only been auditing an extremely small number of (very large dollar value) contracts for TINA compliance (DCAA issued 17 Post-award or Defective Pricing Audits for the six-month period ending September 30, 2017). Although DCAA plans to ramp up its post-award coverage, that will not likely occur until DCAA eliminates the incurred cost backlog (resulting in Congressional attention shifting to some other agency or agencies) and even if DCAA ramps up post-award audits, it's unlikely those will drop down to contracting actions as low as $2 million.

One critical take-away, although post-award/defective pricing audit risk is low, compliance with TINA is not a discretionary decision; if it applies, a contractor's estimating policies and procedures need to embed TINA compliance. Similarly, a contractor's purchasing policies and procedures need to consider TINA flow-downs to applicable subcontracts. In either case, failure to demonstrate TINA compliance can generate business system deficiencies along with withholds (where DFARS 252-242-7005 applies) or negative contractor ratings for competitive source selections.

Of passing interest, the DP/PAP waiver (DARS Tracking Number 2018-O0012) is signed by Shay Assad, who is now (or has been) dual-hatted (Director of Defense Pricing and Defense Procurement Acquisition Policy). In fact, the position is exactly where it was until a few years ago when Defense Pricing was split from Defense Procurement and Acquisition Policy. Rest assured that the reconsolidation back to one director did not result in doubling Mr. Assad's salary, coincidentally a reminder that for purposes of contractor executive compensation, benchmarking for reasonableness (FAR 31.205-6(b)) recognizes no additional compensation for a company executive who might be "dual-hatted".

Cybersecurity and Government Contracts—A New World of Contractor Risks

By Michael Steen, CPA, Senior Advisor

Two recent actions highlight some of the new and different risks associated with government contracts which involve cybersecurity.

In one highly unusual case, the OPM (Office of Personnel Management) OIG (Office of the Inspector General) issued a "Flash Audit Alert" asserting that an insurance carrier in California has refused to allow the OIG to perform IT security tests (which require extensive access to the contractor's IT systems). The OIG asserts that the contractor is obstructing the audit because this contractor stated in writing that it:

Would not allow the OIG to conduct vulnerability and configuration management testing and,

Would not provide the OIG with the documentation required to perform testing related to the contractor's ability to effectively remove information system access to terminated employees and contractors.

The OIG asserted that no other insurance carrier (providing services under the Federal Employees Health Benefits Program or FEHBP) has denied similar access and that lacking such access leaves OPM without any means to independently evaluate the contractor's IT security. In particular, the contractor's internal surveillance is insufficient for audit reliance without independent testing by the auditor. As stated by the OPM-OIG, if they had access, they would focus on systems most directly involved with FEHBP claims processing, but ultimately require access to any of the contractor's IT infrastructure which "touches" the FEHBP processing.

It should come as no surprise that the OPM-OIG's Flash Audit Alert gives no explanation for the contractor's access denial, although some information suggests that the FEHBP claims are a relatively minor percentage of the contractor's total business (hence the reluctance to provide wholesale access). At any rate, the reader doesn't have the "rest of the story" which is the contractor's side of the story. It's entirely possible that the contractor does not want any part of an OPM-OIG IT security audit which will lead to a publicly accessible audit report (redacted, but with enough information to let the "bad guys" know if the contractor's IT security is full of gaps/high risk for unauthorized intrusions). After all, this is the same OPM-OIG which publicly reported (for two years) that OPM's own data security was lacking/high risk and the same OPM-OIG that issued a 2015 report with an "I told you so" message (after OPM servers had been breached, exposing millions of federal employees' data to unauthorized access). In that 2015 OIG "I told you so" report, they

continued to highlight OPM IT security weaknesses, notably that OPM will have (or had) up to 23 systems that have not been subject to thorough security controls assessment.

It's entirely possible that the OPM OIG Flash Audit Alert is the result of a contractor which had the audacity to tell a federal agency "no" because that contractor does not want to be the next OPM (the subject of a publicly accessible OIG report which identifies (to anyone and everyone) that the contractor IT security is vulnerable/high risk).

A second event, in this case an ASBCA decision on the contractor's motion for summary judgment, highlights the risks of contractor not meeting contractual requirements for which contractual deficiencies (with relatively nominal contractual penalties) was but the tip of the iceberg in terms of the government's claim for alleged contract overpayments. ASBCA 60332 involves a contract (task order) going back to 2003 for which DISA network assessments identified deficiency areas for which the contract imposed a .5% penalty. Those penalties accumulate to approximately $600,000; however, the deficiencies also generated an agency request for a DCAA audit which then identified $4,037,019 for overcharges for labor which did not meet the contract labor qualifications. In other words, performance issues led to a requested audit which implicitly attributed the performance issues to employees who fell short of the contractually required qualifications (a somewhat common issue with DCAA after-the-fact audits of Time & Material contracts).

Although the issue is far from settled, the contractor stands to lose approximately $6 million on total invoices of $16.4 million for services from 2005-2008 which involved outsourced (a private contractor) with a contract to protect government IT services. This is also a reminder that contractual issues can take on a life of their own, in this case an ASBCA decision in March 2018 related to a motion for summary judgment which could have closed issues that go back 10+ years…and the decision denying the motion for summary judgment didn't resolve any of the substantive issues.

Bid Protests in the News

By Michael Steen, CPA, Senior Advisor

DoD (DP/PAP) issued a FAR waiver for Enhanced Post-award Debriefing Rights, an additional requirement of the 2018 NDAA. The DPAP Memo (DARS Tracking Number 2018-O0011) requires a contracting officer to give unsuccessful bidders the right to submit additional questions (related to the debriefing) within two days of the debriefing and requires the contracting officer to respond to the questions within five business days. The awarding agency shall not consider the post-award debriefing to be concluded until the agency delivers its written responses to the unsuccessful offeror. This class deviation will remain in effect until incorporated into the FAR or the class deviation is rescinded.

The intent of the enhanced post-award debriefing is to address questions with answers which might convince an unsuccessful bidder to forego a bid protest. As with any other new idea, it remains to be seen if the enhanced debriefing will convince an unsuccessful bidder that the awarding agency made the right decision or more importantly, that a bid protest will be unsuccessful. One other slight reason (for an unsuccessful bidder) to rethink a bid protest, the GAO's new electronic bid protest filing system which also includes a $350 filing fee (an assessment to fund the system and not a punitive measure to discourage bid protests). Suffice to say unsuccessful bidders will not flinch at a $350 bid protest filing fee based upon the fact that many of these involve (unsuccessful bidder) bid and proposal costs in the hundreds of thousands.

In terms of new or unexpected bid protest decisions the following:

An unsuccessful bidder protested the award of a contract, focused on an issue involving an imputed price credit based upon IP rights to the government agency. The unsuccessful bidder agreed to provide limited IP rights, whereas the successful bidder agreed to provide unrestricted rights. Per the solicitation, the awarding agency "credited" or imputed a price reduction applied to the bid price of the successful bidder by the full amount stated in the solicitation, but gave the unsuccessful bidder only a partial credit. In the decision, it didn't matter that the credits (imputed price reductions) weren't supported by any computations, the solicitation provided the awarding agency with the discretion to determine the credit up to the maximum amount stated in the solicitation. The moral of the story, the awarding agency was not required to support its quantitative valuation (nor is there any requirement for the successful bidder to actually provide IP rights which can be valued at the effective price reduction). One more complication for a potential contractor on solicitations which allow the awarding agency to somewhat arbitrarily impute the

value assigned to a non-monetary contractor consideration.

An unsuccessful bidder protested the best value award to a contractor whose price appeared to be unreasonably low ($60.8 million versus the bid protester's $112 million). The bid protester noted that the solicitation included FAR 52.222-46, which states that the agency will evaluate the bidders proposed professional compensation. However, the awarding agency never requested any data concerning the respective bidders professional compensation; hence, the agency effectively ignored the requirements of FAR 52.222-46. In its logic-defying decision, the GAO rejected the bid protest because the awarding agency never requested data which would have permitted the agency to evaluate professional compensation. Apparently, the clause is merely a place holder and an awarding agency can summarily ignore it (either intentionally or by oversight).

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Wednesday May 9, 2018 11:30 AM - 1:30 PM-
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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., 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.

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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.

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