GCA REPORT

(A publication of Government Contract Associates)

January - February 2003 Vol 9, No. 1

NEW DEVELOPMENTS

DCAA Says Timely Submittals of Final Vouchers are a New Condition for Direct Billing

The Defense Contract Audit Agency issued new guidance in November stating contractors who fail to submit completion invoices on completed contracts on time may loose their ability to participate in the direct billing program. The memo cites FAR 52.216-7(d)(5) that requires contractors to submit completion invoices within 120 days (longer if approved by the CO) of settling their annual indirect cost rates of a physically completed contract. Auditors are reminded that failure to submit a timely final voucher can result in the CO determining the amount due and unilaterally modifying the contract while timely submittals can issue release of, at least, 75 percent of all fee withholds.

The guidance states untimely submission of final vouchers create additional risks of the government being overbilled and slows the closing of physically completed contracts. Hence, the guidance adds the timely submission of final vouchers to the criteria for direct billing buying agencies. Prior to participation in the direct billing program, auditors need to determine if contractors are late. For contractors already approved for direct billing, DCAA branch offices need to notify contractors of the new conditions for direct billing. Contractors may continue direct billing if they submit to the CO, with a copy to DCAA, an "acceptable plan to get current within 60 days" after notification by DCAA. The contractor must become current no later than three months after the plan is deemed acceptable (longer if a written extension is granted by the CO). Contractors who do not submit an acceptable plan to become current or who have not been granted an extension by the CO will have their authorization to direct bill rescinded (MRD 02-PPD-081(R).

SBA Amends Size Determination Rules

The Small Business Administration recently published a proposed rule to amend its size regulations and rules applied to size determination appeals. The changes focus on definitions of "affiliations", "annual receipts" and "employees."

Affiliation. One of the proposed changes stipulates that "control", for affiliation purposes, may be affirmative or negative and may be exercised indirectly through a third party. The proposed rule states that affiliation may exist under the "totality of circumstances" even though no single control-related factor is sufficient to constitute affiliation. Further, the affiliation rule would be amended to state only voting stock is considered in determining affiliation, rather than the current rule that references "stock". The proposed rule also provides that where a concern's voting stock is widely held and no single block is larger compared to others then a firm's Board of Directors and its CEO or president is considered to have the power to control the firm in the absence of other individuals.

The SBA is proposing to add a new section entitled "Affiliation based on the newly organized concern rule." This new section provides that affiliation may arise where former officers, directors, shareholders, managing members or key employees of one concern organize a new concern in the same or related industry and the first concern provides contractual, financial or other assistance to the new one.

Joint Ventures and Teaming Arrangements. The SBA adds definitions of "joint venture" and "teaming arrangements" found in FAR Part 9 and 19. The proposals add language stating that for size purposes, a concern must include its proportionate share of the joint venture's receipts in its revenue and its proportionate share of joint venture employees in its total number of employees. Also, the SBA proposes to adopt a rule allowing two or more small businesses to form a joint venture for specific contracting opportunities and still get an exclusion from affiliation for unrelated contracts.

Relevant Date of Size Determination. The SBA is proposing two additional exceptions from the general rule that size is determined on the date the concern submits a written self-certification that it is small as part of its initial offer. For concerns applying for 8(a) status, the firm must qualify as small as of the date of its certification by the SBA. Also, a firm must qualify as small on the date it certifies it is small for purposes of a subcontract.

Reselling items often making changes. The proposed rule provides that firms adding substances, parts or components to an existing end item to modify its performance will not be considered the end-item manufacturer if those identical modifications can be performed or are available from the manufacturer of the existing end item. But if the firm adds something the existing end-item manufacturer does not provide, then the concern is considered the manufacturer of the ultimate end item i.e. the item plus the addition.

OHA jurisdiction. The proposed rule will limit the persons eligible to include a size determination appeal to the SBA's Office of Hearings and Appeals from the current "any offeror" to "any offeror the contracting officer has eliminated for reasons unrelated to size" (Fed. Reg. 70339).

Can't Downgrade Past Performance for Exercising Rights

Defense Department head of Procurement and Acquisition Policy Deidre Lee issued a December 16, 2002 memo advising DOD personnel that it is against policy to penalize contractors who file protests or claims or refuse to use alternative dispute resolution procedures in making past performance evaluations or making source selection decisions. The DOD memo was accompanied by an earlier released memo written by Angela Styles, the head of the Office of Federal Procurement Policy, stating contractors' past performance evaluations may not be (a) "downgraded" for availing themselves of their rights by filing protests or claims or deciding not to use ADR or (b) rated more "positive" for refraining from filing protests or claims or using ADR. The memo is in response to Defense contractors expressing concerns that filing protests or claims could affect their past performance rating since they could be viewed as being uncooperative with the government customer.

OMB Proposes Changes to A-76 Competitions

The Office of Management and Budget is proposing revisions to Circular A-76 intended to expand and improve public-private competitions used by agencies to determine whether outsourcing of commercial activities should be performed by federal employees or private contractors. The proposed changes define a "commercial activity" as "a recurring service that could be performed by the private sector and is resourced, performed and controlled by the agency through a contract". The proposed changes would create the "presumption" that an activity is commercial, putting the burden on agencies to define an activity as "inherently governmental" that would preclude outsourcing to the private sector.

The proposed changes are intended to put more reliance on FAR-based practices. For example, in-house offers (offers by government) would have to respond to solicitations within the same timeframes required of private offerors, the source selection boards would simultaneously evaluate all tenders, agencies would be allowed to conduct cost/technical tradeoffs in accordance with FAR 15 rather than lowest price, eliminate agency offers from the competitive range, communication exchanges between offerors and the agencies would be governed by the same FAR principles and in-house providers would need to track changes and actual costs and could be terminated for non-performance.

Industry Group Urges Changes for FAR Quick Closeout Procedures

The influential Council of Defense and Space Industry Association made recommendations for speeding up the contract closeout process. Currently, FAR 42.7 provides procedures for closing out contracts where indirect costs are "insignificant" – less than $1 million allocable to a contract provided the cumulative indirect costs to be allocated to the contract do not exceed 15 percent of the estimated total indirect costs allocable to cost type contracts for the fiscal year. CODSIA says these requirements are "too restrictive" and should be increased to $10 million and the percentage limitation to 50 percent. CODSIA also criticized the 20 percent decrement approach called for by DCAA and DCMA where both indirect and direct costs of a contract would be unilaterally reduced when incurred cost submissions are more than six months late and recommended, instead, similar language to the administrative clause for CAS at FAR 52.230-6 where a 10 percent withhold against current contractor requests up to a general dollar magnitude for the government's financial exposure.

(Editor's Note. In a recent letter from DCAA's Director Bill Reed to an industry group criticizing the 20 percent decrement guidance, DCAA said it was standing its ground. The letter indicates the 20 percent decrement is not high and is consistent with its surveys. Both direct and indirect costs should be decremented because it is easier to apply a factor to total contract

costs rather than a higher and difficult to apply decrement to only indirect costs. The letter concluded the decrement factor would apply only after contractors were notified several times and contractors could eliminate the problem by simply submitting its required incurred cost proposals on time.)

Other recommendations include (1) establishing time frames for government actions such as initiating an audit of a contractor's proposal, providing audit reports of subcontractors' costs, initiating discussions, etc. and (2) in addressing delays in obtaining assist audits of subcontractors' portions of contract costs, a new provision would require a contract closeout plan be included in the subcontract plan or the requirement to closeout subcontracts as part of the prime contract closeout process could be deleted.

FAC 2001-10 Finalized

The Federal Acquisition Regulations was amended to make elimination of the "paid cost rule" a government-wide final rule. The rule provides that large businesses can include in their billing to the government most vendor and subcontractor costs that have been incurred but not yet actually paid. The rule is intended to improve prime contractors' cash flow by making the paid cost rule that is applicable to small businesses the same for large ones.

The FAR change also includes a final rule that lifts a hold the current administration had placed on implementing a February 2001 Executive Order regarding use of project labor agreements on federal and federally funded construction projects. In February 2001, President Bush issued an EO that negated a previous EO by then President Clinton requiring use of project labor agreements on federally-funded projects above $5 million. (Under a PLA, unions representing the prime contractor's employees and contractor agree to terms and conditions for a specific project and the contractor agrees all workers will either join the union or the union will have jurisdiction over the functions the unionized workers provide including agreement to pay all union wages and benefits.) The Bush EO stipulated that COs or managers working on their behalf could neither require or prohibit offerors, contractors or subcontractors from entering into a PLA – in effect, be neutral toward one. After the February 2001 EO was issued, the AFL-CIO successfully won an injunction against the EO where in July 2002, the Appeals Court ruled Bush had properly exercised his authority and overturned the injunction. The FAR amendment implements the Bush EO.

BRIEFLY…

New Contract-Related Interest Rate Set for First Half of 2003

The Treasury Secretary has set a rate of 4.25% for the period January 1 through June 30, 2003. The new rate is a decrease over the 5.25% rate applicable in the last six months of 2002. The Secretary of the Treasury semiannually establishes an interest rate that is then applied for several government contract-related purposes. Among other things, the rates apply to (1) what a contractor must pay the government under the "Interest" clause at FAR 52.232-17 and (2) what the government must pay a contractor on either a claim decided in its favor under the Contract Disputes Act or payment delays under the Prompt Payment Act. The rate also applies to cost of money calculations under Cost Accounting Standards 414 and 417 as well as FAR 31.205-10 and when a discount factor is used to calculate the present value of future payments (e.g. deferred compensation). (Fed Reg 44264)

GSA Lowers Mileage Allowance a Half Cent

Reflecting current costs of operating a vehicle as determined in its cost studies, the General Services Administration has decreased the mileage reimbursement rates for privately-owned vehicles used on official travel. The final rule, effective January 1, 2003, decreases from 36.5 to 36.0 cents per mile the mileage allowance (Fed. Reg. 493).

Small Business Must Re-Certify Size Status Each Option Period Under FSS

The General Services Administration approved a class deviation from the FAR which requires firms holding Government contracts to re-certify their size and status each time an option is exercised. The action is intended to remove a "loophole" under GSA schedule contracts allowing businesses to retain their "small" status after they are no longer small. Previously, the FAR language was interpreted to mean vendors who initially certified as small businesses kept that status for five years under a GSA contract where after the initial term vendors were able to retain the small business status into each of three, five-year option periods without re-certification. Now, holders of GSA multiple award schedules will have to re-certify their status *each time* their contracts are open for renewal.

GSA Lowers Industrial Funding Fee by Quarter Point

The General Services Administration Supply Service announced that as of January 1, 2004 it is lowering the industrial funding fee for multiple awards schedule programs to .75 percent from the current 1 percent. The IFF is a charge applied for use of MAS contracts which is supposed to fund operation of the MAS program. Prices of products and services listed on the schedule reflect the IFF which essentially means the agency buyers pay the IFF to the scheduled contractors as part of their contract price and then the contractors remit the fees collected to the GSA on a quarterly basis. The reduction follows recent criticism that the fee revenue is well above the amount needed to fund operation of the schedule program.

PPA Interest Required On Interim Payments of Cost Type Service Work

Effective December 30, 2002 the Office of Management and Budget issued a final rule requiring agencies to pay a Prompt Payment Act interest penalty whenever they make an interim payment under a cost reimbursement contract for services more than 30 days after receiving a proper invoice for payment. The new requirement applies to all invoices due on or after December 15, 2000 under any cost reimbursement service contract regardless of when it was awarded (Fed. Reg. 79515).

SBA Launches E-Procurement Pilot Program

The Small Business Administration, in a contract with NEXGEN's Solutions, Inc., recently announced the launch of SBAExchange Pilot Program – "an electronic purchasing tool designed to facilitate small business e-procurement opportunities and improve the efficiency and accountability of current government procurement processes." The SBA believes the program will enable them to award simplified acquisitions up to $100,000 – around 98% of federal purchases – and allow them to make purchases and payments electronically with the government purchase card. The pilot program's performance period will last from October 2002 through September 2005 and includes a "cost of entry" fee of $1,500 per year. Information can be obtained at "http//www.sbaexchange.com/sba/home.nsf/home."

Donations of Unused Leave Time No Longer Allowable Cost

Effective January 1, 2003 the Defense Department will no longer permit contractors to claim employee donations of unused vacation and personal leave to charitable organizations as an allowable cost under FAR 31.205-6, compensation for personal services. Though such costs have traditionally been unallowable contributions under FAR 31.205-8, Contributions and donations, the DOD in February 2002 permitted such unused leave donations to be considered allowable in the wake of the September 11th attack. The motive for discontinuing the allowance was that the IRS would not extend its November 2001 Notice facilitating the donations.

CASES/DECISIONS

Teaming Agreements Terms are Binding Not Just Agreement to Agree

(Editor's Note. The following case is a landmark case where, for the first time, a court has held a teaming agreement can bind a contractor to specific performance on a subcontract. Commentators say it marks an "important milestone for subcontractors and the enforceability of teaming arrangements.")

A contract was awarded to the prime contractor partly –if not largely – on the basis of its subcontractor's experience. During definitization of the subcontract, the prime contractor brought up two new major points – a proposed cap on the subcontractor's G&A rate and a termination for convenience clause without limitation. The prime contractor disputed these provisions and sought specific performance of its contract.

The prime contractor argued the teaming agreement between itself and the subcontractor did not constitute a subcontract but merely an "agreement to agree" where the agreement was a formal vehicle with a single purpose to establish an exclusive relationship to prepare and submit a winning proposal. In support of its position, the prime subcontractor alluded to *W.J. Shafer Associates* that held a teaming agreement to be merely an agreement to agree in the future in the event the prime contractor won the contract. The judge disagreed, stating all the pieces were in place for a legally binding agreement between the parties. The Court ruled the cited case was different since there was no mutual commitment by the parties, no mutual obligations between the parties to buy or sell, no agreed to purchase price and no assurance the products would be available when needed. Unlike that case, the judge said the facts here supported a finding there was a mutual commitment between the parties with respect to the amount of the subcontractor's involvement and amount of work it would perform. The judge concluded the two disputed items were never part of the teaming agreement and were not left open for negotiation. It sided with the subcontractor stating it should "live up to the bargain" it made in the agreement (*EG&G Inc. v. The Cube Corp. VA Cir. CT. Chancery No. 178996*).

No Breach of Requirements Contract In Spite of Actual Orders Less Than 80% of Estimate; When Breached, No Entitlement to Profits

(Editor's Note. Though we have seen from prior cases discussed here that requirements contracts do not guarantee the government will buy an estimated quantity (only that they procure all their needs from the contractor), the government must still provide a "realistic" estimate of the total quantity based on most current information. That is, it cannot merely "haphazard a guess" because contractors rely on the government estimate to prepare their bids.)

The contractor entered into a time and materials repair contract to furnish all necessary labor to repair equipment where 3,620 service call hours were estimated to perform the work even though the actual contract omitted the word "estimated" above the quantity column and the contract did not identify what type it was. Though the Army ordered all its requirements from the contractor its actual service-hour orders for the base period and two options years were 67% to 80% below the estimated quantities stipulated in the contract stating less repair was needed because new equipment was purchased and the original warranty on old equipment was extended. The contractor asserted it was due an additional $360,000 arguing its contract constituted a "definite-quantity" contract for 3,620 service hours.

The Board disagreed, finding the contract was a "requirements" type contract and that the government satisfied its obligations under the contract by ordering all its needs. The Board noted a "definite quantity" contract is used when the government can determine in advance that a definite quantity of services or supplies will be needed. Here, however, the contract required service hours only when equipment needed repair. The contract was also not an indefinite quantity contract because it lacked a guaranteed minimum. It concluded it was a "requirements" type contract even though certain FAR clauses (e.g. 52.216-21, Requirements) were not incorporated which are used when the government anticipates recurring requirements but cannot predetermine the precise quantity. The Board concluded no price adjustment was called for in spite service hour requests being 67%-80% below estimated quantities because the estimates were not prepared negligently or in bad faith nor were they "unreasonably inadequate" *(Centurion Electronics Serv., ASBCA 51956).*

In another case, the government provided the contractor a price adjustment under its requirements contract when actual orders were 10% of estimated quantity when it was shown the government's estimates of needs were flawed because it determined prior to the contract award that its estimate was greatly overstated. In computing the amount due, the case allowed the contractor to receive additional compensation based on unabsorbed overhead (i.e. fixed costs that could not be recouped over the negligently prepared estimated quantify of items) but refused payment of anticipatory profits. The Board rejected profits on the grounds not only because the contractor could not show it would have "definitely" realized the profit but also the recovery of lost profits would effectively have converted the requirements contract into one in which the government guaranteed the contractor a certain level of business (*Secretary of Defense v. Applied Companies Inc. Fed. Cir., No. 01-1630*).

Contractors are Entitled to Payment Under T&M Contracts Even if All Services Not Completed

The contractor entered into a Time and Material contract under a Federal Supply Service information technology contract to provide nine tasks and nine key deliverables required to support the tasks, stipulating a not-to-exceed amount of $359,000. The government refused to pay five submitted invoices for $142,000 asserting the contractor did not perform all the services contemplated by the order. The Board sided with the contractor stating the nature of the time and materials contract, in contrast to a fixed price contract, falls within the "broad genre of cost reimbursement type contracts" that requires only the contractor use its best efforts to provide the goods and services. The contractor is entitled, as a matter of law, to be paid for its costs of performance up to the contract ceiling, whether it succeeds in fully performing the contract requirements or not.

The Court did note that if the government believes it was overcharged, it is not obligated to pay in full all invoices submitted if it has a valid reason to believe it was overcharged (*CACI Inc. – Federal v. General Services Admin, GSBCA, No. 15588*).

Court Rules Collaboration Agreement Revenue Belongs in Indirect Rate Base

(Editor's Note. If there was ever any doubt about how theoretical cost allocation issues can represent big bucks, the following should dispel any such notions.)

An appeals court has reversed an earlier board decision on whether revenue sharing payments should be included in the allocation base. Collaboration agreements used by Pratt & Whitney in manufacturing jet engines for its commercial customers had foreign parts suppliers pay an up-front fee based on their share of the engine program and receive a corresponding share of the revenues derived from the sales by P&W. Title to the parts stayed with the suppliers until the parts were delivered to the engine customer but immediately prior to delivery, title transferred to P&W which then passed to the customer. P&W allocated indirect costs on a direct material base where purchased parts from traditional suppliers were included in the base but the parts acquired under the collaboration agreements were not considered "material cost" and accordingly, was excluded from the allocation cost base.

The government contended the collaborators were essentially subcontractors or vendors and not including those dollars in the base violated several cost accounting standards (e.g. CAS 418, 410 and 420) and hence they demanded P&W repay $157.6 million plus interest of $102.7 million for the impact of excluding those items from the indirect cost base. P&W appeals to the ASBCA held the collaboration parts were not a "cost" and hence their accounting practices did not violate the Cost Accounting Standards (CAS). The Board determined that CAS does not define "cost" so generally accepted accounting principles (GAAP) could resolve the issue where it accepted extensive expert testimony indicating the "economic substance" of the agreements should control and the agreements were properly considered joint ventures rather than subcontracts.

Under the government's appeal, the Court sided against P&W. The Court asserted that the law of CAS, not GAAP, should rule which was subject to interpretations of "experts" whereas the terms "cost" and "material cost" used in CAS was "clear and unambiguous." CAS 410 requires that the cost input base represent all significant elements of cost representing the total activity of the business and since material cost is the base for allocation, all significant elements of the cost of material need be included in the base. Though CAS does not define cost, the Court turned to FAR which defines material costs to include "raw parts, sub-assemblies, components, and manufacturing supplies whether purchased or manufactured by the contractor." The Court stated there was a "purchase" by P&W, relying on the Uniform Commercial Code which defines "sale" as "the passing of title from seller to the buyer for a price." There is no question P&W took title to the part and they paid a "price" for the part. The collaborative agreement provided the sharing of gross revenue from the sale of engines would be "in consideration of the parts manufactured" and receipt of revenue would be linked to the delivery of the collaborators' share of production. The fact a particular revenue share was not assigned to individual parts as part of the company's accounting practice did not prevent the payments from constituting a price. Consequently, the revenue share payments should be included in the base and to exclude it would "cause a substantial distortion of overhead allocation" *(Secretary of Defense v. United Technologies Corp., Pratt & Whitney, Fed. Cir. No. 02-10781)*.

Only Original, Not Faxed, Invoices Start PPA Interest Clock

Its contract stipulated, in part, contractor would be entitled to Prompt Payment Act interest if payments were not made by the government 30 days after submission of a proper payment request. On January 7, contractor faxed its first invoice and since it did not receive payment until well after the 30 day period, it sought interest. The Board ruled faxed invoices were not an original so the interest clock did not start on January 7. Thought the FAR does not define "original" the Board noted the dictionary defines it as a "source from which a copy…can be made" while FAR indicates a FAX is a "reproduced" invoice and therefore not the original (*General Construction Co. DOTBCA 4137*).

NEW CONTRACTORS

What Do They Mean By "Adequate Internal Controls"

Government auditors consider contractors' "internal controls" to be a critical area of investigation but there is often confusion what they are and what constitutes adequacy. The increased emphasis stems partially from recent guidance established by the audit profession and specific emphasis from the government audit community. The latter stems from the fact that decreasing resources requires more audit coverage with less people so greater productivity translates into more attention to contractors' internal controls so those with better controls generally require less labor intensive transaction testing.

The Defense Contract Audit Agency December 11 issued new guidance to auditors in evaluating contractors' system of internal controls. We find the new guidance helpful to contractors because it alludes to specific internal controls that will be evaluated. The guidance is intended to apply to non-major contractors with government work between $10 million and $80 million and may apply to contractors with less than $10 million at auditors' discretion. The guidance is primarily in the form of a questionnaire (Internal Control Questionnaire or ICQ) designed to help the auditor obtain an understanding of the contractor's internal controls and assess the "control risk." If the control risk is considered high, the auditor can decide to perform substantive tests of sensitive accounts and transactions or can go into more intensive testing of specific systems such as accounting, estimating, billing, etc in which there is further guidance for each system.

The ICQ is expected to be completed or updated as part of the auditors' periodic visits to the contractor and a new ICQ should be completed every year if a field visit is required as part of a current audit. The ICQ has four parts: Part A, Basic Organization provides general understanding of the contractor's organization structure, size and complexity. Parts B through D are intended to cover the five basic components prescribed by various audit standards (e.g. Yellow Book, AICPA) – control environment, contractor's risk assessment, information and communications, monitoring and accounting system control objectives and activities.

The criteria for adequate controls seem to be heavily weighted on the existence of written policies and procedures. Contractors have often felt ambivalent about such written policies. Yes, their existence does establish policies for the company and "gets the word out" but their existence creates the basis for citing noncompliance when practice does not match policy. The increased emphasis on these written documents may change contractors' views.

Part B. Control Environment and Overall Accounting System. It asks:

- Are there current deficiencies identified by either external CPAs or other DCAA audits
- Are there adequate written policies and procedures addressing the general accounting system, screening unallowable costs, direct versus indirect charging practices, preparing incurred cost submittals and forward pricing proposals, allocation of indirect costs to contracts, approvals and documentation of journal entries, establishing account numbers and contract charge numbers and allocation of various credits (e.g. rebates, refunds, income)
- Are cost accounting records (e.g. job cost) reconciled and controlled by the general accounting system on a current basis i.e. postings made at least monthly.
- Are costs identified by contract

Part C. Contractor's Risk Assessment, Information and Communications and Monitoring

- *Risk assessment.* Is there a "risk assessment process" for relevant risks associated with preparing submissions to the government and are there any prior identification of risks of having noncompliant submissions
- *Information and Communication.* Are there written policies and procedures covering either manual or computerized controls over transactions and journal entries from the time they occur to the time they are included in the accounting records? Do the written policies and procedures address individual roles and responsibilities pertaining to controls over accounting information? Are the policies and procedures disseminated to employees and are there records of prior failures to implement these policies?
- *Monitoring.* Are there any ongoing monitoring procedures to ensure internal controls are followed (e.g. internal audits).

Part D Accounting System Control, Objective and Activities

- *Labor System.* Is there a training program covering proper time charging? Are there written policies and procedures in place to identify labor documentation/work descriptions that identify work to be performed? Are labor charges tracked to final cost objectives whether or not they are allowable or unallowable direct or indirect costs? Are there written timekeeping policies and procedures and do they reasonably assure labor hours are accurately recorded, corrections documented and proper approvals maintained?
- *Materials/Purchasing.* Does the contractor maintain written policies and procedures to describe the major manual or automated systems that cover the material management and accounting system?
- *Estimating.* Are there written estimating policies and procedures addressing employee training, assignment of authority and responsibility, cost

GCA REPORT
P.O. Box 1235
Alamo, CA 94507

estimate development and estimating system process, activity and functions.

- *Billing*. Do written billing policies exist addressing employee training, contract briefing to identify special billing provisions and limitations and management review of billings.
- *Compensation*. Do written compensation policies and procedures exist that address salary structure and administration, description of fringe benefits provided and a system for determining pay increases, bonuses and promotions. (*Editor's Note. Since compensation levels have become a major focus for audit scrutiny, we refer the interested reader to our GCA DIGEST Vol. 5 No. 1 that address further compensation controls examined during audit reviews of compensation.)*

QUESTION & ANSWERS

Q. I live about 300 miles from Chicago and always fly in and out of Chicago when flying home. I have two business trips planned with a few days in between and rather than flying home I was wondering if I can fly to Chicago and stay there a few days before heading out on my next trip. What do the travel regulations say about this?

A. We recently came across an appeals case similar to your situation and it appears that you can charge the government for the Chicago stay (hotel and per diem) as long as the savings of not flying home exceeds costs of the Chicago stay.

The related case allowed a civilian employee of the government to stay two days in Atlanta – authorizing payments of hotel and per diem expenses for $144 – which saved the government $433 on reduction of airfare for flying into Atlanta rather than home. The Board ruled (GSBCA 15847-TRAV) since the stay in Atlanta resulted in combining what would have been two separate trips into a single longer one saving the government money, the employee was entitled to not only the hotel expenses requested but also per diem and incidental expenses for the two days.

Q. We are a systems engineering, professional services firm and are considering breaking up our overhead rate into separate rates – one for fringe benefits and one for non-fringe benefit overhead costs. Is this common and are there any benefits for doing so?

A. Yes it is quite common to have a fringe benefit and overhead rate. As for benefits, it depends. For example, if the fringe benefits for direct labor "follow" the direct labor (i.e. are charged directly to the benefiting contract) then your direct charges may be higher and your overhead rate would be lower. Your customers may or may not like the changes depending on who gets charged the higher direct costs or who get the benefit of the lower indirect rate.

Q. We accrue for our estimated state income taxes in the current year and I intended to reflect the accrual in both our incurred cost submittal and forward pricing rates. Our controller said the income taxes are unallowable. Who is right?

A. You and your controller are both right, or wrong, depending how you look at it. State income taxes, as opposed to federal income taxes, are allowable according to FAR 31.205-41, Taxes. Claiming the accrued taxes (that is, the estimated amount) on your incurred cost proposal would be improper – you need to include the *actual* taxes paid. For the forward pricing proposal, estimated taxes should be acceptable since forward pricing rates are primarily estimates of future expenses.