GCA REPORT

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NEW DEVELOPMENTS

Get Ready For Sequestration

The general media as well as publications oriented to government contractors are full of information on sequestration where the general consensus as of this writing is there will be significant cuts in government spending but the impact is highly uncertain. The literature is addressing the pricing aspects of sequestration which include:

1. The Defense Department and other agencies will be slowing payments and will notify contractors of changes to its payment processes. DOD has rescinded a class deviation that directed contracting officers to insert the clause FAR 52.232-99 in new solicitations and contracts which require prime contractors receiving accelerated payments to make accelerated payments to subcontractors.

2. To match anticipated government employee furloughs many contractors are reporting that contracting officers are expecting contractors to lessen the work week to 32 hours without reducing personnel. The remaining eight hours would be charged as indirect.

3. Be ready to prepare requests for equitable adjustments (REAs) for contract delays, demands for out-of-scope work or other contract changes to remain whole. Contractors are advised to become familiar with the relevant FAR clauses (e.g. 52.242-14, 15, 17 and 52.243-1).

4. Be prepared to encounter partial or full termination for convenience actions where there are ample opportunities for significant cost recoveries when proposals are properly prepared.

5. Be ready to respond to government REAs for deductive changes to the contract for less work. The government will of course be attempting to maximize the reduction in contract price where contractors need to be aware of the costing rules for such actions.

(*Editor's Note. We have written numerous articles on administrative concerns and how to quantify the maximum amount of costs you are entitled to under REAs and termination proposals as well as how to minimize contract price reductions for deductive changes so use our key word function at our website to find these articles. These actions are often complex where legal and accounting help should be sought and the good news is such help is usually directly reimbursable by the government as settlement expenses under REAs, terminations and deductive changes.*)

Obama Signs FY 2013 NDAA

President Obama signed the $633 billion FY 2013 National Defense Authorization Act. The NDAA contains several acquisition-related provisions that will affect contractors doing business with the Defense Department. Various industry group protests to some highly controversial provisions that passed Senate and House versions of the bills resulted in either removal or watered down versions of requiring DOD to cut contractor and civilian jobs by the same percentage as cuts to military personnel, attempts to lower executive compensation and allowing DCAA access to contractors' internal audit reports. Provisions of interest to contractors include:

1. DCAA access to internal reports (Section 832). Whereas the senate version gave DCAA unlimited access to the reports where if it refused the contractors' internal system could be deemed inadequate the final NDAA ensures DCAA cannot use contractor internal reports for purposes other than assessing risk and evaluating efficacy of internal controls and associated business systems. Many commentators have been stressing that internal audit reports cannot be used to determine whether costs are allowable, if defective pricing occurred or if there is a violation of the cost accounting standards. The NDAA also states that though internal audit reports "may be considered" in assessing a contractors' system of internal controls it shall not be "the sole basis" for finding a system inadequate. Some commentators have asserted the provisions do not give DCAA any right of access to contractors' internal reports but rather only requires DCAA to issue guidance on this topic and certainly places limits on use of these reports. Nonetheless, DCAA will likely but incorrectly state this new NDAA does give it access to the internal audit reports so there

is likely to be some as yet unresolved disputes in this area.

2. Limited use of cost type contracts (Section 811). DoD will be prohibited from using cost type contracts for the production of major defense acquisition programs (MDAPs) unless the Undersecretary of Defense for Acquisitions certifies to Congress it was needed to provide a required capability in a timely manner.

3. Contractor profits (Section 804). DOD will be required to review its profit guidelines to ensure a link between contractor performance and profit. The review must consider appropriate levels of profit needed to sustain competition, contractor risk and incentives for superior performance in delivery of quality products and services in a timely and cost effective manner.

4. Contractor employee compensation (Section 804). Senate proposals for a limit of compensation to the level of the Vice President (about $230,000) were rejected in the final bill where now the GAO is required to conduct a study on the effects of reducing the allowable costs of contractor compensation.

5. Small business (Sections 1631-1699). The NDAA contains numerous provisions aimed at increasing small business opportunities that would (1) authorize the Small Business Administration to establish a mentor-protégé program for all small business similar to that currently in place for 8(a) companies (2) require that small business prime contractors not expend on subcontractors more than 50 percent of the amount paid under the contract with exceptions for subcontractors that qualify as a "similarly situated entity" (3) require an offeror to notify any potential subcontractor it intends to include it in its subcontracting plan and require the SBA to establish a reporting mechanism that allows a subcontractor or potential subcontractor to report "fraudulent activity or bad faith by a contractor with respect to its subcontracting plan" and (4) require the SBA to conduct a study every five years to identify underrepresented small business concerns owned and controlled by women and remove dollar limits that may be subject to women owned small businesses (WOSB). This last effort is viewed as partially correcting limitations of a WOSB program passed in 2011 that applied in only certain industries, did not allow for sole-source contracts and set-asides applied only to manufacturing contracts below $6.5 million and $4 million for all other contracts.

6. Suspension and debarment (Section 861). Requires each DOD military department and the Defense Logistics Agency, the State Dept. and USAID to have at least one suspension and debarment official who is not supervised or reports to acquisition offices or the inspector general office.

7. Contractor conflict of interest (Section 829). DOD must review the guidance on personal conflict of interest for contractor employees performing acquisition functions closely associated with inherently governmental functions. This review function is significantly watered down over earlier provisions.

GAO Says DCAA's Incurred Cost Audit Initiative is Promising But More Planning is Needed

The General Accounting Office issued a report stating the Defense Contract Audit Agency's initiative to focus resources on closing out high-dollar and high-risk incurred costs audits shows promise but adds that DCAA needs to develop a plan to assess the initiative's progress. Under the initiative (reported in the last 4Q12 issue of the GCA DIGEST) DCAA raised the dollar threshold that triggers an automatic audit of a contractor's incurred cost proposal from $15 million to $250 million, revised the criteria used to determine a proposal's risk level and significantly reduced the number of low risk audits that will be randomly sampled. Though DCAA tracks such data as number of risk determinations made, number of proposes deem high or low and number of audits completed the report states they should go further by (1) developing a plan to assess the success of its initiative and (2) the Defense Contract Management Agency should improve its data on closing over-age contracts.

The comments on DCAA were part of a GAO report that addressed DOD's backlog of open contracts that numbers in "the hundreds of thousands" stating DCAA closing its backlog of incurred cost audits was a key factor in DOD closing out its open contracts. GAO recommended DOD and the military department develop better data to monitor contract close outs where the report stated there should be more use of closeout procedures, referencing a FAR deviation authorizing DCMA to use quick closeout procedures more broadly than the FAR 42.202(a) provisions (e.g. unsettled direct and indirect costs not exceeding $1 million or 10% of the contract value).

Final Rule on Not Displacing Service Workers

A final rule was issued by DOD that states succeeding companies on federal service contracts must now be

required to offer employees of the predecessor contractor and its subcontractors a right of first refusal of employment for positions for which they are qualified. The final rule, which implements a prior executive order and Labor Department regulations, adds a part 22.12 to the FAR and a new clause at FAR 52.222-17. The final rules makes a few changes over the prior rule: (1) limits the power to waive the requirement to an agency's senior procurement executive (2) adds a section addressing circumstances when a successor does not offer employment to all displaced workers but only to the number it believes is necessary to do the work and (3) states the offer of employment qualifies even if it is not for a positions similar to the one previously held. The position needs only to be one for which the employee is qualified and can have different employee terms and conditions including pay and benefits. Successors will need to reach out to employees and they must presume that all employees working on the contract in its last month performed suitable work (*Fed. Reg. 75766*).

Venture Capital Backed Firms Qualify for SBIR But Not STTR Awards

The Small Business Administration issued a final rule that makes companies majority owned by multiple venture capital operating companies, hedge funds or private equity firms eligible for Small Business Innovation Research (SBIR) awards but not for Small Business Technology Transfer (STTR) awards. The final rule provides definitions of the three types of entities and states an SBIR contractor must be (a) over 50-percent owned and controlled by US citizens, permanent residents or domestic businesses (b) majority-owned by multiple domestic venture capital operating companies, hedge funds or private equity firms or (c) a joint venture made up of some combination of the above entities. No single domestic venture capital, hedge fund or private equity firm may own more than 50 percent of a SBIR participant. The rule amends SBA rules on affiliation for purposes of SBIR and STTR awards, including rules on minority ownership, common management, multiple persons with identical interests, newly organized firms, ostensible subcontractors and license agreement for products and trademarks. For the time being, the SBA retained the current 500-employee size standard for SBIR and STTR awards. The SBA dispensed with similar ownership rules by venture capital backed firms for the STTR program after comments argued that Congress did not intend to further dilute small businesses participation in the STTR program which already awards funding to universities (*Fed. Reg. 76215*).

DCAA Changes Its Performance Metric

A story we read in Darrell Oyer's February 22 newsletter states the Defense Contract Audit Agency has changed its metric of performance from "questioned costs sustained" to simply "questioned costs." Whereas the "sustained" part means questioned costs must be agreed to by the ACO, contractor and any litigation before they are recognized as valid the questioned costs are rather assertions made by DCAA only. Mr. Oyer states not only is the new metric misleading but it will provide an incentive by DCAA to increase the amount of questioned costs no matter how "unfounded" they are.

DOD May Not Contract With Tax Delinquent or Convicted Contractors

The Defense Department has issued a memo stating it may not use FY 2013 funds to enter into contracts with firms that have unpaid federal taxes or federal felony convictions. Contracting officers are instructed to include provisions to this effect in all solicitations. According to the memo DOD may not contract with corporations (1) that have any unpaid federal tax liability that have been assessed (2) for which all judicial and administrative remedies have been exhausted or lapsed (3) that is not being paid in a timely manner pursuant to an agreement with the authority responsible for collecting the tax liability and (4) may not contract with a corporation that was convicted of a federal felony in the preceding 24 months where the awarding agency is aware of the conviction. However, the memo states COs may still make an award if the agency's suspension and debarment official makes a written determination that these actions are not necessary to protect the government's interest.

FAC 2005-65 Issued

The FAR Council has issued changes to the Federal Acquisition Regulation in the form of FAR Circular 2005-65. Two provisions affecting contractors are:

1. Implementing earlier legislation, excise taxes on certain federal procurement payments to foreign persons are unallowable. If the goods are manufactured or produced in or services are performed in a country that is not a party to an international procurement agreement with the US, then a two-percent excise tax is imposed on payment made to foreign persons.

2. Prohibits the award of contracts using appropriated funds to any foreign incorporated entity that is treated as an inverted domestic corporation or any subsidiary of that entity. An inverted domestic corporation is one

that used to be incorporated in the US or used to be a US partnership but is now incorporated in a foreign country or is a subsidiary whose parent corporation is

CRS Provides Summary of Past Performance Evaluations

The Congressional Research Service Feb. 4 issued a report providing a good overview of legal requirements that apply to contractor past performance, including challenges to agency evaluations, award decisions and responsibility determinations. Though not required to compile past performance evaluations (PPE) before the Federal Streamlining Act of 1994 the FAR Part 42.15 sets the current procedures agencies must follow in compiling, posting and using PPEs. It requires PPE on all contracts worth more than $150,000 ($30K for architect-engineer contracts, $650K for construction) when the contract is completed or on an interim basis in the case of multi-year contracts. Agencies are given broad discretion on the content and are only required to evaluate performance and subcontracting goals though it may consider other factors such as cost controls, schedule delays, record of integrity and ethics and conformance to contract requirements. The report states though agencies were expected to rely almost exclusively on PPE in their source selection decisions, this has not occurred.

The report addresses disputes noting that starting with *Record Steel & Constr*, such disputes have become seen as potential claims under the Contract Disputes Act. Nonetheless, despite these cases it is presently unclear what, if any, relief the courts and appeals boards may be able to grant.

Agencies are prohibited from making awards without a determination of positive responsibility where now PPE is required to be considered as an element of such a determination. Contractors' ability to challenge responsibility determinations are limited where the GAO will hear protests only if it alleges criteria were not met or the CO failed to consider relevant information or violated a statute whereas courts may consider challenges if they are "arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law.".

Recent legislation cited by CRS requires the DOD and FAR Council to ensure PP reports are timely, accurate and complete, give contractors 14 days to rebut or supplement the report, authorizes or prohibits inclusion of certain info of PPEs and increases oversight of PPE issues. The CRS report also addresses recent initiatives to standardize government-wide factors to evaluate PP such as the Contractor Performance Assessment Reporting System. It states increased subjectivity of PPEs are likely to lead to more protests (the report is available at www.fas.org/sgp/crs/misc/R41562.pdf).

Correction…

Last issue we reported that the semi-annual federal interest rate of 1 3/8% incorrectly applied to the second half of 2012 where it actually applies to the first half of 2013. The rate is a decrease from the 2% that applied to the second half of 2012.

CASES/DECISIONS

Six Year Statute of Limitation Starts When ICP is Submitted

(*Editor's Note. The following decision is particularly important due to the large backlog of unaudited incurred cost proposals (ICPs). Under the Contract Disputes Act, the government has six years from the date of accrual to assert a claim against a contractor. FAR 33.201 states that a government claim accrues when the government knows or should know of all events that fix the contractor's alleged liability and courts and boards are barred from hearing disputes from claims that are asserted more than six years after the date of accrual. When this accrual clock starts has been the basis of numerous prior and recent cases where the government has asserted, for example, an ICP must be audited or reviewed before the government knows or should know about the content of submissions. The following case establishes the six year clock starts as of the date of a final ICP submission. This case has generated considerable concern by ACOs and COs where we are now seeing contracting officers' final decision being issued, some hastily and incomplete, to beat the six year clock.*)

DCAA did not challenge Raytheon's compensation plans that were reflected in its 2003 and 2004 ICP submittal but in Sep. 2007 it issued a report questioning several compensation costs for those periods. In Jan 2011, the CO issued a final decision that demanded $20 million as price adjustments and penalty. In a second appeal, DCAA similarly issued a report in July 2008 questioning costs starting in FY 2004 that were deemed to violate the FAR and CAS where in June 2011 the CO issued a final decision demanding $3 million. Raytheon claimed in each case the government asserted claims beyond the six year statute of limitations and hence they were untimely. The Board sided with Raytheon ruling in the first instance the government should have known by Sept 2003 (the date of the FY 2002 ICP submission) about the 2002 unallowable costs where the Sept 2007 was the date DCAA actually knew the 2003 audit was incorrect. The

Board similarly ruled in the second instance that the government should have known before Jan 2005 that the 2003 and 2004 were CAS non-compliant. The board also ruled that government's claims for CY 2005 through 2009 costs were timely because Raytheon submitted its CY 2004 ICP in June 2005, within the six year period of the statute of limitations (*Raytheon Co., ASBCA Nos. 57576, 57679*).

Court to Evaluate "Reasonableness" Criteria

The Court awarded $11 million to KKR on a claim for $41 million for work providing dining facilities in Iraq from 2003 to 2006 asserting the other costs claimed were unreasonable. In a highly unusual step, two industry groups have filed an "amicus brief" arguing the court failed to properly apply the prudent businessperson standard mandated by FAR 31.201-3, reasonableness. The groups asserted the trial court did not follow the FAR provision that a cost is reasonable if its type and amount do not exceed that which would be incurred by a "prudent person" in the conduct of competitive business where a contractor is entitled to exercise its discretion in incurring costs without a contracting officer second guessing and disallowing those costs. Here, the groups assert, the court is attempting to substitute its judgment for that of the contractor which is essentially "renegotiating" the subcontract KKR forged during its 10 years of working under harsh wartime conditions providing the military urgently needed services. The industry groups are challenging the ruling in the court that stated the contractor's discretion is limited to situations over which it has no control and adds that FAR 31.201-3 does not allow for questioning contractors' decisions that are reasonable when it is made but turns out to be incorrect in retrospect. The brief states if the court's decision is affirmed, the clarity of the prudent person principle will be replaced by "arbitrary ad-hoc analyses of what a court or board would have done if it was the contractor" which will encourage COs to second guess business decisions. (The brief is available at http://www.psco.org/News2/NewsRelease/2013/PSC_files_fiend_of_court_brief_in_government_contracts_case_aspx)

Government Failed to Show Damages in its Defective Pricing Claim

(*Editor's Note. Findings of defective pricing – the contractor knew or should have known that data submitted before contract price was established was inaccurate, incomplete or not timely – need not necessarily result in an adjustment to the contract price. Offsets are possible or as the following demonstrates, the contractor shows the defective data did not result in a higher contract price.)*

Lockheed supplied retrofit kits to the Air Force that included modular computers supplied by its subcontractor. DCAA issued a post award report claiming Lockheed had defectively priced the computers by failing to disclose significantly lower prices for computer components, recommending a price adjustment of $14.6 million. The CO issued a final decision stating (1) the contract was defectively priced as a result of the non-disclosure (2) the government relied on the defective pricing data and (3) therefore the contract price was overstated. The Board sided with Lockheed stating though there were some flaws with the computer cost build up estimate the government failed to prove the amount of any price increase. Though the government correctly asserted it was entitled to the presumption that nondisclosure of defective data results in an overstatement of the contract price Lockheed had rebutted this presumption. Furthermore, the government made several errors that undermined its argument such as its analysis failed to account for materially different delivery rates and it improperly applied a "decrement" when comparing contracts' hypothetical prices (*Lockheed Martin Aeronautics Co., ASBCA No. 56547*).

Offeror Waited Too Long to Challenge Solicitation Amendment

Under a set-aside DOD solicitation for IT services a joint venture offeror filed a post-award protest arguing an amendment changed the solicitation to such an extent DOD should have either canceled the solicitation or allowed offerors to submit new proposals. On appeal the court held that the protesters had failed to preserve their challenge to the amendment by not raising the challenge until after the contract was awarded. The court held that a disappointed bidder must challenge a solicitation containing a patent error or ambiguity before award if there is time to do so. In addition, the court ruled the protesters lacked standing because they could not show they had a substantial chance of receiving an award but for alleged errors in the procurement process (*Comint Systems Corp. and Eyelt.com Inc. v US, Fed. Cir., No. 2012-5039*).

Agency Should Have Provided Notice of a Price Realism Evaluation

The government issued a request for task order proposals to provide IT services where award was to be based on technical factors outweighing price. After selecting DB

Consulting, Emergint protested the award asserting the government did not tell offerors that it would conduct a price realism evaluation which meant it would be relying on an unstated evaluation factor. The GAO sided with Emergint explaining that offerors must be told so that their business decision to submit a low price proposal can be considered in assessing their understanding of the work and/or risk associated with the proposal. The solicitation in this case only mentioned source selection officials would evaluate offerors' proposed prices for reasonableness. The GAO also rejected the government's assessment of Emergint's technical factors stating (1) Emergint had not described how it would attract incumbent staff when it did and (2) unfairly penalized Emergint and not DB for including significant information in the appendixes (*Emergint Technologies, Inc., GAO B-407006*).

SMALL/NEW CONTRACTORS

Knowledge of Retention Period Rules May Preclude Paying Some Disallowed Costs

(*Editor's Note. The extensive delays for DCAA to audit long closed out contracts has led to frequent questions by our subscribers on how long must they retain documents. We have addressed this issue over the years but recent FAR changes and court cases have led us to revisit this issue. This article is based on an article in the January 2013 issue of the CP&A Report by Karen Manos.)*

DCAA has a current backlog of nearly 25,000 incurred cost proposals totaling $573 billion where in FY 2011 it completed only 349 incurred cost audits, not to mention new proposals submitted each year. At this rate, it has been estimated DCAA could take 70 years to work through its ICP backlog. So that raises the issues of whether contractors are really required to retain supporting documents until DCAA get around to auditing them and if such documents are not retained beyond specified periods can the government disallow costs for inadequate support under FAR 31.201-2(d).

FAR Subpart 4.7 prescribes policies and procedure for contractor records retention. This section applies to contracts that contain one of the Audit and Records clauses which covers sealed bid contracts for which certified cost or pricing data is required, negotiated contracts in excess of the simplified acquisition threshold and specified categories of contracts and subcontracts.

FAR 4.703 requires contractors to make available records and other supporting evidence to satisfy contract negotiation, administration or audit requirements for three years after final payment or the period specificied in FAR 4.705 (discussed below). There are two significant exceptions: (1) if a contract clause specifies a longer period then that period applies or (2) if the contractor fails to meet the original due date for ICP submission (i.e. six months following the end of its fiscal year) then the retention period is automatically extended one day for each day the proposal is late. FAR 52.215-2, which is a mandatory flow down clause to subcontractors, requires contractors to make available records, material and other evidence until 3 years after payment or for either shorter periods specified in Subpart 4.7 or longer period required by statute or other clauses. In addition two provisions of the clause extends the period for terminations, claims, disputes or appeals until they are settled.

Though some of the clauses applicable to flexibly priced contracts specify some of the records required none extend the period beyond FAR 4.7 provisions. For example, FAR 52.232-7 for T&M and Labor Hour contracts require contractors to substantiate vouchers with evidence of actual payment, individual timesheets, records verifying employees met labor qualification requirements but reference FAR 4.7 for periods prescribed.

Generally, FAR retention periods are calculated from the end of the contractors' fiscal year in which there is cost entry or allocations to the contract. There are three exceptions: (1) if a record contains a series of entries the retention period starts as of the year for the final entry (2) if a latter contract relies on certified cost and pricing data for an earlier contract then the retention period runs from the latter contract and (3) if two or more records are interfiled and it is impractical to screen records for disposal then the entire record series must be retained for the longest period prescribed for the category of cost.

Three subsections of FAR 4.705 specify retention periods for three broad categories of records – financial and cost accounting records, pay administration records and acquisition and supply records. Each category has numerous subcategories. Note that records are identified in terms of their purpose or use and not by specific name. Specific retention periods for most financial and accounting records is four years. So with the exception of labor-related costs, records for most costs within an ICP is four years. Retention period for timesheets and evidence of payment is two years while

the retention period for payroll sheets, registers of salaries and wages paid to individual and tax withholding statements is four years.

The author addresses FAR 31.201-2(d) which was added in 1996 to make explicit what was before implicit that "contractors must maintain adequate cost records in order to be reimbursed for all claimed costs" and "the contracting officer has the authority to disallow costs which are determined to be inadequately supported." The change did not purport to change any contracting record requirements. Neither did the addition change the burden of proof where the author states it is the government's burden to prove costs are unallowable so they must prove that inadequately supported costs are unallowable.

♦ **Case Law Interpretation**

In *JANA Inc. vs. US (936 F.2d 1265)*, DCAA began the audit after the two year retention period required for keeping time cards but before the four year retention period for payroll sheets and salary registers. The Federal Circuit Appeals Court began its analysis stating the issue was how long was JANA required to maintain the records that supported its invoiced labor charges. The Court sided with the government in its assertion that the labor recap sheets should have been classified as the type of records subject to the four year retention period. While a shorter retention period is required for voluminous records like individual time cards a longer period is required for records of a more summary nature like the labor recap records. Consequently, it ruled the government was entitled to recoup apparent overcharges on the two time and material contracts because the contractor failed to retain labor recap sheets supporting the number of hours for the four-year records retention period. Similarly, in *Analytical Assessment Corp., (ASBCA 52354)* the appeals board held the government could recoup amounts provisionally paid to a contractor for subcontract costs because neither the contractor nor subcontractor retained any records supporting the costs for the specified retention period.

On the other hand several cases have ruled that though the contractor failed to retain specific records the government could not disallow the costs for inadequate documentation. In *BearingPoint, Inc. (ASBCA 55354)* the contractor relied on testimonial evidence and corroborating documentation to support labor charges in the absence of time cards that were lost or destroyed where the Board states "the contract clauses do not impose the stringent requirements of either 'nice neat little files' that the CO sought…or contemporaneous records' the government argues is required." In a similar case in *Lockheed-California Co. (ASBCA 28618)* the board rejected the government assertion that Lockheed had failed to comply with the express condition of the Audit and Records clause by failing to provide various records the clause states are required where the board found that other documentation to prove the claimed costs was "sufficient to reflect properly" the expense.

The author concludes that if DCAA conducts an audit after the specified retention periods have expired, the contractors' costs cannot be disallowed based solely on the failure to retain adequate documentation in accordance with FAR 31.201-2(d). At the very least, contractors may rely on alternative evidence. In the absence of supporting or challenging the costs, the costs' allowability will likely depend on which party bears the burden of proof. In alluding to the six-year Statute of Limitation issue that if exceeded precludes recovery of disallowed costs on backlogged audits (see the Raytheon case discussed above), audits depending on documentation that is outside the retention period may also preclude recovery of disallowed costs.

QUESTIONS & ANSWERS

Q. Our price analyst questioned some costs in our proposal that were never questioned by DCAA where his report became the basis of the negotiator's offered price which was well below our costs. Two examples of over ten questionable items were (1) we had to remove 60% of our sales costs in the G&A pool to the G&A base because they had little to do with the government business we were engaged in and (2) we could not include fringe benefit costs in the base.

A. You describe a trend we are seeing lately where proposals that used to be audited by DCAA are now being reviewed by DCMA price analysts where many of our clients are saying they never thought they would be thrilled to have DCAA back in the picture. Many price analysts are either unfamiliar with cost accounting issues and become very "creative" in questioning allowable costs or they are foxes where they purposely put forth "creative" positions that form the basis of their initial negotiating position and then go from there. Many negotiators, with even less knowledge of accounting issues, are simply rubber stamping these price analysts' positions. You need to effectively challenge the price analysts' position point by point so either they or the negotiator will have a justification for realizing the initial position may be wrong where then the likely result will be to offer a more reasonable

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bottom line negotiated price. By the way, both positions you cite are wrong – regulations, court decisions, etc. have clearly established that sales expenses are a legitimate G&A expense whether or not they directly benefit one type of contract as long as they contribute to increasing the overall business base and contractors are free to establish a direct labor plus fringe benefit overhead base.

Q. We are switching to a new computer system. The problem with this system is the job cost ledger does not allow us to burden direct subcontract costs and ODCs with our G&A rate. We can, of course, invoice for the burden on these costs by adding burden sets to the applicable cost elements but the burden isn't visible in the job cost reports. I am very concerned that this will be an issue for DCAA because these costs aren't applied in the job cost ledger. We use the job cost ledger to bill on contracts so how can we say our system is adequate for billing purposes if these costs can't be seen?

A. Though some contractors choose to burden all costs in the job cost records, most simply track direct costs only and then add indirect on their invoices. So there should be no problem with not burdening direct costs in your job cost records. DCAA is concerned that you have the capability of identifying indirect costs and that you monitor them through the year.

Q. Could you point me to the appropriate section of the FAR that discusses requirements for the size of a rental car? I have found similar text regarding air accommodations that "would offer accommodations not reasonably adequate for the physical or medical needs of the traveler," so I need something similar with regard to the size of a car to rent.

A. There is no car size requirement I am aware of - the criteria is "reasonableness." When I was a DCAA auditor, I had a government rate for a med sized car so if it was mid-sized or less there should be no question. That does not mean you couldn't get something bigger if the reason is reasonable - physical limitations, more people, weather conditions, etc. Short of renting Ferrari's I'm not aware of seeing any questioned costs in this area. If you are attempting to formulate a company policy, you may want to limit rentals to mid-sized and require supervisory permission to go higher.

Q. In our Afghanistan contract there was an original CLIN through March 2012 for vehicles and then an additional CLIN was added in July 2012 for additional vehicles. We purchased some vehicles in April which leaves the question of how to treat the costs from April to July.

A. There are clear rules in the FAR addressing consistency of treating costs – "like costs in like circumstances" must be treated either direct or indirectly, not both ways. So if vehicle costs are always treated directly, then they should all be direct. If you anticipate problems being able to recover the April-August costs as a direct charge (remember, you are always allowed to make an adjustment for prior billings and claim the cost after the month they were incurred) then you should be prepared to assert they are "like costs incurred under unlike circumstances." Your written policies should, ideally, provide that certain costs are treated sometimes as direct and sometimes as indirect where an example similar to the vehicles would be provided. If you don't feel they will accept the costs as direct and if you don't have a policy now, I would treat it as an overhead item. Questioned costs due to allocation issues, as opposed to allowability, do not attract penalties so you need not fear penalties.

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