GCA REPORT

(A publication of Government Contract Associates)

July - August 2000 Vol 6, No. 4

NEW DEVELOPMENTS

OFPP Issues Guidance on Past Performance Information

The Office of Federal Procurement Policy issued in June "Best Practices for Collecting and Using Current and Past Performance Information." The Federal Acquisition Streamlining Act of 1994 acknowledged the relevance of past performance in contract award decisions and directed the Office of Federal Procurement Policy to establish government-wide policies. The rules have been progressively added to the Federal Acquisition Regulation (e.g. FAR Part 9, "Contractor Qualifications"; 12, "Commercial Item Acquisition"; 15, "Contracting by Negotiation"; 36, "Construction and Architect-Engineer Contracts"; and 42, "Contract Administration") and are being evolved through a growing body of bid protest decisions. The guide, which is not to be mandatory, intends to summarize the regulations and the most recent decisions.

The OFPP envisions a system where contractor past performance information will inform source selection decisions on a majority of government contracts where performance evaluation will eventually be automated and accessible to most government agencies. The guide tracks four basic performance elements – cost, schedule, technical performance and business relations/customer satisfaction – and uses a five-tiered rating system similar to that used by the Defense Department. The ratings will include a high of 5 (for exceptional performance), a low of 1 (unsatisfactory performance) and 4 (very good), 3 (satisfactory) and 2 (marginal). The ratings will correspond to the contractor's performance that exceeds contract requirements (5), somewhat exceeds requirements (4), meets requirements (3), does not meet some (2) or does not meet contract requirements with recovery unlikely (1). Raters are instructed to use narrative explanations to augment the numeric system so other COs may understand the supporting rationale.

A final contractor performance assessment must be prepared at the close of all contracts valued at over $100,000. The themes of "no surprises" and "communication, communication, communication" are stressed throughout the guide where periodic evaluations of contract performance (at least once every six months) and promptly communicating the results will provide fairness and be a significant motivator for contractors to maintain high quality and improve inadequate performance.

A history of claims litigation is not to be used as a basis of downgrading proposals. COs and other officials are advised when making performance assessments to pay attention to how the "role of government" may have contributed to problems in prior contracts. The guide references FAR by making sure contractors have the opportunity to comment on the assessment within a few days of its being finalized. If necessary to reach consensus contractors may seek a face-to-face meeting with the CO and review the evaluation one level above the CO.

Since automated access is envisioned, use of past performance information for source selection should be efficient and convenient for agencies under the guide. Offerors should only be required to identify relevant contracts not more than three years old. During the source selection process, contractors should be encouraged to discuss any adverse past performance issues and identify corrective action taken. The government is encouraged to choose wisely the past performance subfactors it deems relevant to the solicitation and make sure the statement of work and instructions to offerors is reasonable and logical and it is clear how past performance will be evaluated.

In determining how the past performance relates to a solicitation the government is encouraged to use risk assessments (e.g. high risk rating for negative past performance). When past performance is unavailable the offeror cannot be evaluated positively or negatively so the guide recommends a middle score of 3. Past performance related to similar work for commercial or state or local entities should also be considered.

The text is available at http://www.arnet.gov/Library/OFPP/BestPractices/pastperformguide.html. We also refer the interested reader to a recent two part series in the first two GCA REPORT issues of FY 2000 for a summary of regulations and practical advice to maximize your evaluations.

First Reverse Auction Procurement

The Navy became the first government agency to use the reverse auction techniques in awarding a federal contract. Using the secured Internet-based technology, reverse auctions allow suppliers to compete for contracts online by adjusting their prices as they see other offers. Three contractors competed for the Naval Supply Systems Command reverse auction to supply recovery sequencers used in ejection seats valued at $2.38 million. In contrast to often time-consuming standard award procedures, the Navy praised the contract for taking just under an hour and claimed the procedures resulted in a 28.9 percent lower price than if standard procurement practices were used. A Senate subcommittee, obviously interested in its potential, has called for more pilot tests of such reverse auction techniques.

Not surprisingly, the first such procurement generated a protest from one of the unsuccessful bidders who asserted it lost its internet connection before the bidding was complete. Interestingly, the protest did not challenge the legality of the new technique and the protest was subsequently dropped. The protest raised the first concern that a contractor may intentionally terminate its connection to obtain additional time to formulate its bidding strategy even though the entity hosting the auction uses procedures intended to verify when a bidder looses its connection.

DCAA Issues New Audit Guidance

The Defense Contract Audit Agency has recently issued some guidelines to its auditors that should be of interest to our readers.

- **Failure to Analyze Subcontractors Proposal is an Estimating System Deficiency**

DCAA offices have been reporting that prime contractors have not been conducting required cost analysis of proposed subcontract costs when cost or pricing data is submitted. As a result, DCAA has been increasingly citing such contractors with estimating system deficiencies. Many contractors have been responding to such claims stating the FAR does not require it to conduct cost analysis of subcontractor proposals prior to negotiations of the contract but rather prior to negotiation of the subcontract. DCAA issued its guidance as a response to this assertion.

The guidance cites the DCAA Contract Manual (DCAM) Chapter 15.403-14 that states a contractor is directed to obtain cost or pricing data from "prospective sources" (e.g. subcontractors, purchase orders, material orders, etc.) for procurements exceeding $500,000 (unless the procurement is otherwise exempted such as for a commercial item). According to FAR Part 15.408, Table 15-2 ILA, the contractor is also required to conduct a cost analysis of the submitted cost or pricing data. The time frame for obtaining and conducting cost analysis is prior to negotiation of the prime contract since the provision requires the contractor to include cost analysis along with its own cost or pricing data.

The guidance also reminds auditors about rules covering subcontracts that either exceed $10 million or represent at least 10% of the prime contract cost, whichever is less. While subcontractor proposals and any cost analysis usually remains in the contractor's file, if a subcontract meets either of the above thresholds and still exceeds $500,000, the regulation requires the prime contractor to provide both a summary of its cost analysis and a copy of the submitted cost or pricing data along with its own submission. When this condition is not met, an estimating deficiency is also called for.

Responding to why such failures represent estimating deficiencies, DCAA cites DFARS 215.407-5-70 where an estimating system deficiency is considered to be a shortcoming in estimating total cost or major cost elements that results in not providing a basis for negotiating a fair and reasonable price. Since subcontract costs are usually significant and are explicitly listed as one of the deficiencies, failure to conduct cost reviews constitutes an estimating deficiency.

To avoid the burden of conducting cost reviews, prime contractors often apply a decrement factor to proposed subcontract costs usually based on some historical experience of analyzing cost proposals. The guidance addresses this common practice stating such a decrement factor does not eliminate the requirement to conduct cost analysis of subcontractor cost data (00-PPD-048R).

- **New Caps on Executive Compensation**

Alluding to the recent Office of Federal Procurement Policy changes to the executive compensation cap, the guidance states the new cap of $353,010 applies to costs incurred after January 1, 2000 for all federal agencies covered by FAR cost principles, including contracts awarded prior to enactment of the new cap. The cap is also to apply to years beyond 2000 until the OFPP revises the cap. Consequently, multiyear proposals must reflect the current cap (00-PPD-047R).

- **Evaluating Government Property and Material in Contractors' Possession**

To achieve an unqualified audit opinion on the Defense Department's financial statements, one of the financial reporting issues is correctly assessing the value of

property and material in possession by contractors. Since DCAA has a major presence at contractors, DOD has asked them for their assistance in quantifying the property and material costs. DCAA has issued a 40-pages guide to its auditors that includes instructions on how to value the property and material.

Specialists within DCAA have been appointed to work with local auditors in conducting the audits. 31 contractor segments have been selected for initial audits. A sample of one or more contracts will be made to evaluate such items as real property, high dollar plant equipment, other plant equipment, special test equipment, special tooling and material that will be selected on a sample basis. Detailed guidance is provided on how to select these items and how to ascertain their value based on financial auditing standards. The guidance includes a detailed audit program to be followed, rules for adequate disclosure and several pro forma letters (00-PPD-044R).

DOD Gives Audit Rights on Prototype Other Transaction Agreements

The Defense Department issued a rule that provides for government audit access to the General Accounting Office under "other transaction" agreements for prototypes projects relevant to new weapons or weapons systems that exceed $5 million. The audit access rule, which provides for inclusion of an audit access clause in the agreements, does not apply to OTs for research and development. OTs are frequently used agreements authorized by Congress to lessen the government-unique regulatory requirements to encourage participation by companies who usually refuse to do business with the government. Recognizing the need to attract such companies, the rule provides an exemption to OT participants who have not entered into any other contract, grant, cooperative agreement or OT agreement in the year prior to the date of agreement. *(Editor's Note. For a discussion of OT agreements see the GCA DIGEST Vol. 2 No. 3)*

In an unrelated matter, DCAA is establishing a database of government contractors currently participating in OT agreements in order to prevent established government contractors from violating either CAS 402, "Consistency in Allocating Costs Incurred for the Same Purpose" or the Credits cost principle. If contractors account for OT costs differently than its other contract costs, it is vulnerable to a CAS 402 violation. Similarly, if it fails to establish a credit to its research and development pool(s) for the revenue it earns from participating in R&D other transaction projects, it would violate the FAR cost principles related to credits.

Cost Accounting Standards Final and Interim Rules Set

Recent changes to cost accounting standards passed in the 2000 National Defense Acquisition Act have been made into final and interim rule changes in the FAR. Final rule changes made to FAR Section 30 include:

FAR 9903.201-1 (CAS Applicability). A new paragraph exempts contracts and subcontracts (we collectively refer to them as contracts) of less than $7.5 million from CAS coverage if, at the time of award, the business unit of the contractor or subcontractor is not currently performing a CAS-covered contract of $7.5 million or more. Another provision exempts firm-fixed-price contracts from CAS coverage if they were awarded through adequate price competition without submission of cost or pricing data.

FAR 9903.201-2(a) (Full Coverage). It is finalized to revise the dollar threshold for full CAS coverage from $25 million to $50 million and to delete the requirement that to be subject to full CAS coverage, a contractor or subcontractor must have received a CAS-covered contract that exceeded $1 million.

FAR 9903.201-2(b) (Modified Coverage). The definition of modified CAS covered is revised to apply to a covered contract of less than $50 million in net CAS-covered awards in the immediately preceding cost accounting period. If any one contract is awarded with modified CAS coverage, all CAS-covered contracts awarded to that business during that cost accounting period must also have modified coverage. An interim rule change to FAR 30.201-4 (Contract Clauses) has been added to require contracting officers to insert the disclosure clause of 52.230-3 (Disclosure and Consistency of Cost Accounting Practices) in negotiated contracts when the contract amount is between $500,000 and $50 million and the offeror certifies it is eligible to use modified CAS coverage. If, however, the business receives a single CAS-covered contract award of $50 million or more, any covered contract awarded in the same accounting period must be subject to full CAS coverage.

FAR 9903-201-5 (Waiver). A waiver may apply for a contract less than $15 million if the agency official determines that the business unit performing the work is primarily engaged in the sale of commercial items or would not otherwise be subject to CAS.

The CAS Board may also waive all or any part of the CAS upon request of any agency head. Such requests must describe the proposed contract and contain (1) a statement the proposed contractor refuses to accept a contract containing all or any of the prime contract CAS

clauses (2) a statement whether the proposed contractor or subcontractor has accepted any contracts containing the CAS clause (3) amount of the proposed award and agency awards to the contractor in the last three years (4) a statement that no other source is available to satisfy the agency in a timely manner (5) a statement of alternative methods pursued to fulfill its needs and the reasons they were rejected (6) steps being taken to find other sources for future contracts and (7) any other useful information.

FAR 9903-202-1 (General Requirements). Increase the dollar amount for requiring submission of a CAS disclosure statement (written description in a prescribed format of contractor's accounting practices and procedures) from $25 million to $50 million. The rule also requires submission of a disclosure statement when a company received net award of CAS-covered negotiated contracts totaling $50 million or more in its most recent cost accounting period.

BRIEFLY…

Electronic Signatures are Now Law

Congress and the President passed legislation (S. 761) recognizing the validity of contracts signed electronically. The bill does not require contractors to use or accept electronic signatures or records in dealing with the government but gives agencies a framework for encouraging use of e-commerce procedures. The bill does not specify any particular electronic signatures since the technology is rapidly advancing to recognize such things previously considered science fiction such as digital signatures, fingerprints, face shaping, body heat patterns, voice, eye, etc. The measure also provides for some exceptions where only writing will be valid like most court documents and notices of default, foreclosure or repossession.

FTR Per Diem Rates to Cover Fiscal Rather than Calendar Year

The General Services Administration has announced it is shifting coverage of changes to the government per diem rates from the calendar to the government fiscal year (October to September). Consequently, the fiscal 2001 per diem rates will take effect October 1, 2000.

Two Senators Join Opposition to Eliminating Travel and Relocation Caps

In what looks like a final strike against a proposal to eliminate caps on travel and relocation costs, two additional key senators joined other fellow senators in opposition to the change on the grounds that changes would create unequal treatment of government and contractor employees. As we reported in the March-April issue, five key senators stopped passage of a change to travel and relocation reimbursement that would have substituted a "reasonableness" reimbursement standard for detailed federal travel regulations and FAR requirements. The opposition of the new senators should guarantee non-passage for now.

DOE Allows Cost of Money

Since the Department of Energy and its predecessor agencies traditionally accomplished its mission through the use of management and operating (M&O) contracts, it evolved its own set of cost principles and terms and conditions that were better suited to M&Os. In recent comparisons of its acquisition regulations (DEARS) and FAR it concluded that the FAR cost principles adequately addressed most of its interests. Consequently, DOE is amending its DEARS to permit the cost of money as an allowable expense and deleting provisions of the DEAR that are adequately covered in the FAR. The only DOE unique cost principles relate to (1) allowing individual locations to continue determining their own methods of allocating home office/corporate allocations (2) continuing to disallow bid and proposal costs for M&O arrangements (non-M&O contractors can follow FAR) and (3) FAR cost principles related to travel and relocation will continue to be followed even if other agencies switch to a "reasonableness" standard.

NASA Extends Contract Terms as Motivator for Good Performance

The National Aeronautics and Space Administration is testing a new contract type that will allow contractors that deliver excellent performance to win extended contract terms. Under the new pilot program of the "award term contract" (ATC) a contractor will receive a "3/4 incentive" where for each year of performance rated "excellent" it can earn nine months of additional performance up to a limit of 10 years under a normal five year contract. Conversely, the contractor can lose nine months of performance if its score for a one-year period falls below a good or successful range under an ATC.

Administration Commits to 5 Percent of Awards to Women-Owned Small Businesses

President Clinton signed an executive order on May 23 directing federal agencies to take steps to award at least 5 percent of prime contracts and subcontracts to women-owned small businesses (WOSBs). The order requires agencies to develop strategies to expand

opportunities for WOSBs such as: (1) designate a senior official to identify and promote WOSB opportunities (2) require contracting officers to the maximum extent practicable to include WOSBs in their competitive acquisitions (3) implement mentor-protégé programs for WOSBs (4) require a corrective action plan by agencies failing to meet the 5 percent goal (5) develop a single Web site providing procurement information to WOSBs and (6) work with state agencies to share information concerning procurement opportunities.

SBA Changes Standard for Defining Small Business Size

Effective October 1, the Small Business Administration is amending its size standards by discontinuing use of the Standard Industrial Classification System (the so-called SIC code) and replacing it with the North American Industry Classification System. The change is intended to more closely reflect today's small business sector especially the technology sector. We anticipate any changes will be reflected in both SBA publications and the FAR Part 19.

CASES & DECISIONS

Teams Can "Flip-Flop" Prime and Subordinate Member Roles for Multiple Contracts

Two indefinite delivery/indefinite quantity contracts – one a small business set-aside and one unrestricted – were awarded to a team consisting of a small business and large business who flip-flopped their roles as prime and team member. An unsuccessful bidder protested alleging the awards were made to the same entity and hence competition would be precluded for future task orders because the two teams would be "competing against each other." GAO rejected the same entity argument saying the two teams were not the same entity since they submitted a separate proposal for evaluation that included different labor rates, proportions of member participation as well as different management, small business participation plans and past performance information. The GAO went further and said even if they were the same there was no prohibition against making the award to teams even if they were the same (Global Readiness Enterprises, GAO B-284714).

Pre-Award Costs Accepted and Pre-Bid Costs Rejected on Termination Proposal

(Editor's Note. The following helps clarify what precontract costs may and may not be recoverable under a termination for convenience.)

A contractor spent considerable funds on estimating and negotiating a construction contract. When it received notice of winning the contract, the contractor immediately incurred project management costs to set up the work to meet the schedule. The award was made after seven days and was terminated for convenience less than three weeks later after 80 percent of the project management effort had been completed. In its termination proposals it sought to recover 80 percent of what it had included in its price for project management, the pre-proposal costs and 15 percent profit on the amount and the agency rejected all proposed costs on the grounds they were incurred before the contract award. The Appeals Board ruled the contractor was entitled to the project management costs because it had incurred the costs in order to meet the contract schedule and is not precluded from recovering these start-up costs on the grounds they preceded formal contract award. However, the Board rejected the costs incurred prior to submitting its proposal stating such costs are not recoverable as part of a T of C claim (Barish Co., PSBCA, No. 4481).

A Protest Must Quantify Impact of Work Additions to a Solicitation

(Editor's Note. The following decision highlights two interesting points – (1) an agency needs to modify a solicitation when it adds work and (2) a protest should not just assert a change affects one's rates but quantify how it does.)

Three weeks after it awarded a contract for facilities operation and maintenance, NASA modified the contract to add work. NASA admitted it knew prior to award that work would be added to the contract but argued additional work would not exceed 10% and hence was immaterial. An unsuccessful bidder protested the award arguing that had the increased workload been included in the solicitation, it would have substantially reduced its G&A rates and award fee resulting in a win at a lower price. The GAO agreed the solicitation should have been modified but still did not overturn the award because generalized assertions about decreases in G&A rates and fees were not persuasive enough to show the competitive standing of the two offerors would have changed (NV Services, GAO B-284119.2).

Failure to Disclose Lower Subcontractor Quote is Defective Pricing

(Editor's Note. The following further clarifies when defective pricing exists.)

In its post award review of a contract to provide aircraft

repair kits, DCAA asserted the contractor failed to disclose lower vendor quotations it had in its possession prior to price agreement that resulted in a price overstatement of $134,000 plus interest. The contractor responded that though it possessed the lower quote it would have been imprudent to submit it because it did not have time to verify the quote before price agreement. The Appeals Board disagreed stating (1) the contractor did have the cost and pricing data on hand but simply failed to submit it and (2) the Truth in Negotiation Act requires the contractor to disclose all cost or pricing data "which may or may not be part of the total cost of a contract." (GKS Inc. ASBCA No. 47692.)

Three Cases Where Protests are Sustained

(Editor's Note. It's a good idea to know the type of protests that tend to be successful. Here are a few recent ones that may be relevant to our readers.)

The Navy awarded a contract for information technology support and infrastructure services following ratings by offerors, oral presentations and best and final offers. The protester asserted the award was not reasonable because the winner's higher technical rating was not justified. The GAO examined the evaluation record which consisted of only three documents – an "extremely brief and conclusionary" initial evaluation, the committee's revised evaluation virtually unchanged from the earlier one and the CO's source selection memorandum which adopted the committee's findings with little further explanation. The GAO sustained the protest because the Navy did not adequately document its evaluation of the proposals resulting in no way of knowing whether the selection was reasonable (Future-Tec Management Systems Inc., GAO, B0283793.5).

Beneco protested an award of three indefinite quantity engineering and construction service contracts where the solicitation required the awards to be based on a price/technical trade-off and specified that technical evaluation factors were significantly more important than price. Beneco was ranked 36% higher for technical merit versus the awardee of the first contract while its price was 27% higher. In the tradeoff decision, the CO rejected the proposal stating it was unreasonable to pay over $500,000 to have the same project built by a better contractor and also cited FAR 15.611 that requires a selection to be price driven. Having rejected the proposal, the CO did not compare Beneco's proposal against the lower-rated proposals for the other two awards. Beneco protest asserted the government violated the evaluation scheme of the solicitation by not weighing technical merit as significantly more important than price. The GAO agreed with Beneco, stating the record showed there was no consideration of the trade-offs between Beneco's high technical rating and high price against the other offerors but rather a simple unwillingness to pay the 27%. This effectively converted the tradeoff from an evaluation where technical merit was more important than price to a "price competition between two acceptable proposals." (Beneco Enterprises, Inc. Comp. Gen Dec. B-283154.)

In a bidding for a dike renovation contract, the government gave a 40 percent weight to a subfactor in its technical evaluation for an item – "bioengineered slope protection" – never mentioned in the solicitation. An successful bidder protested the award asserting the agency failed to comply with the solicitation's evaluation criteria and used unstated experience subfactors in the evaluation. The GAO agreed and overturned the award, stating it is fundamental that offerors be advised of the bases on which proposals will be evaluated and added agencies may not give importance to specific factors, subfactors, or other criteria beyond that which would reasonably be expected by the offerors (Loyd H. Kessler Inc., GAO, B-284693).

Contractor Can't Recover Unused Leave Due to Contract Extension

A fixed price contract to operate and maintain vehicles at an Air Force base provided for the right of the Air Force to extend performance for short periods and entitled the contractor to price adjustments to reflect increases in wages and fringe benefits. The Air Force extended the contract for several months and the contractor did not schedule vacations for its employees so they would be available but paid them for unused leave. It sought reimbursement but the Air Force refused and in its appeal the Court ruled against the contractor stating the inability to schedule employee vacations was "a management issue" and the increased costs was not brought about by compliance with a wage determination that was provided in the contract (Tecom Inc., ASBCA, No. 51880).

SMALL/NEW CONTRACTORS

Lower Your G&A Rate by Allocating Costs Elsewhere

While the government is more tolerant of overhead expenses it generally considers contractors' G&A costs

as fluff. Many government agencies are taking steps to lower the G&A costs they pay such as conducting studies to determine specific industry G&A costs and refusing to exceed them, putting caps on G&A rates, providing higher ratings to contractors demonstrating lower G&A rates and increasing use of Department of Defense profit guidelines that, in part, eliminate profit on G&A. Reducing G&A rates by reallocating costs is becoming a hot topic and we thought it would be a good time to review some of the more common methods available to contractors to reallocate G&A costs elsewhere without actually eliminating the costs.

Unless contractors are quite small, they usually have at least two indirect cost pools – overhead and general and administrative. Overhead costs are considered indirect costs incurred for producing goods or services and usualy vary with level of producing products or services. G&A expenses consist of administrative costs of running the business and are commonly considered period costs largely unrelated to the level of production or service. Contractors' basis for distinguishing G&A from overhead also vary: all costs incurred at the home office location are lumped as G&A, it was always done this way and a change risks assertions of inconsistent accounting practices, etc. Reallocation of costs from G&A to other indirect cost pools or direct costs may very well not alter the magnitude of costs charged to government contracts (e.g. a lower G&A rate offset by a higher overhead or greater direct costs) but the *perception* of lower G&A rates is key. In addition, reassigning costs for contract pricing and costing purposes need not be consistent with the methods used for financial reporting. When contract costing differs, usually by developing "memo" records, the practice is common and generally accepted by government auditors.

In our experience there are numerous ways to reallocate G&A costs that are considered appropriate practices under contract costing rules:

1. *Reassign specific G&A costs to overhead.* G&A pools commonly include costs that can be considered support of products or services and hence allocable to overhead. For example, personnel who work in such functions as contract administration, purchasing, human resources, accounting, quality control and information services (IS) are clearly in support of end products or services. In addition, portions of functions normally charged to G&A such as legal and insurance costs do support product and services such as costs for labor disputes or third party suits and insurance charges like professional liability. A portion of much of the remaining G&A costs (e.g. rent, utilities, depreciation, etc.) can be assigned to other indirect pools on some pro-rata basis such as square footage used by overhead versus G&A personnel.

2. *Create centralized service centers and allocate them to both G&A and other pools on an appropriate base.* Centralized service centers are accumulation of costs associated with distinct functions that are commonly performed at the home office. Examples include personnel administration, centralized IS, centralized purchasing, centralized warehousing, etc. Sometimes such costs are easily identifiable when a contractor accumulates these costs by departments or cost centers; otherwise, they need to be accumulated on a memorandum basis. Once the costs of centralized service centers are identified, they can be allocated to other indirect pools such as overhead, material handling and even a fringe benefit pool. The method of shifting the centralized service costs elsewhere is to use a base that has a "causal beneficial relationship" to the pool of costs. If precision is desired, then each central service can use its own base such as headcount for personnel services, invoices for purchasing, terminals or CPU time for IS, number of contracts for contract administration, etc. If simplicity is preferred, we find selection of one base (e.g. headcount) or at most two bases adequate and usually accepted by auditors. If challenged, you can usually demonstrate that more precise methods do not yield significantly different results.

3. *Create service centers and allocate such costs to various indirect cost pools as well as directly to contracts.* Service centers are accumulation of costs of various functions that often are or can be allocated as an ODC (other direct cost). Unlike centralized service centers, where they are most often identifiable at the home office/G&A pool, service center costs are more often spread across multiple indirect cost pools. Examples include reproduction, vehicles, small equipment, CAD/CAM, etc. Charge out rates are either established as fixed unit prices or for cost type work, established at provisional rates and sometime adjusted after actual costs are identified. Costs related to these service centers (personnel, depreciation, portions of facilities, etc.) are also accumulated into the service pools and allocated either directly to cost objectives or other indirect cost pools on a usage basis (e.g. number of pages, hours of vehicles use, etc.). Service center costs are extracted from all indirect pools and stand alone and are allocated back to indirect pools only on a usage basis. Revenues from clients do not reduce other indirect cost pools but only reduce the service center costs. The effect is to minimize G&A costs (few service center functions are used at the G&A level) and increase both direct and non-G&A indirect cost pools.

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

Contractors may be reluctant to make changes for fear they are changes to cost accounting practice that would entail onerous burdens of developing cost impact analyses not worth the effort. For CAS covered contractors, the changes described above are cost accounting changes. In our experience, however, the impact is usually not significant and burdensome cost impact proposals are usually not necessary. There is a new emphasis on minimizing these administrative burdens (even proposals for formal change) and we find one page analyses of the overall impact on relevant government contracts to be sufficient. For contractors not covered by CAS (an increasing population due to recent higher CAS covered thresholds from $25 million to $50 million), contractors are free to make accounting changes without the burden of cost impact statements.

(Editor's Note. The comments in this article are necessarily broad and intended to get you thinking about alternatives. If you have questions related to the article or want to discuss their relevance to your firm, feel free to call Bill Lennett at (925) 362-0712 or email him at gcaconsult@earthlink.net.)

QUESTIONS & ANSWERS

Q. Do the regulations prevent us from charging travel time directly to a contract?

A. We could not identify any rules in either the federal travel regulations or FAR that prohibit charging travel time either directly or indirectly. Rather, rules of "reasonableness" (e.g. not charging eight hours for a two hour trip) govern. Of course, a specific contract can limit such costs (e.g. separate labor rates for travel time, maximum limit for international travel) but prohibitions are quite rare in our experience. If anything, the emphasis in government circles on equalizing contractor and government employee travel reimbursement is a good argument for allowing travel time reimbursement. After all, weekday travel by government employees is the norm and weekend travel usually gets reimbursed as either overtime or credit time.

Q. We are buying some items for a government contract from one of our corporate subsidiaries. Since the items represent a considerable portion of the costs, the auditors are asking us to provide a cost buildup for the items. The subsidiary representatives assure me the price is quite reasonable but it would be a major problem for the subsidiary to develop a cost buildup - they never heard of an "unallowable cost" and I don't think they could develop an overhead rate that would withstand an audit. What should I do?

A. It sounds as if the subsidiary either does not do much business with the government or primarily sells commercial items. Consequently, take a good look at FAR Part 12 to identify all the elements that qualify for a commercial item and if one fits, assert the proposed price is a commercial item that does not require a cost buildup. If that does not work, talk to the contracting officer to ask their price analysts to conduct a price analysis of either the item or the major components of the item. Many price analysts are quite skilled in developing a price analysis plan that can by-pass a cost analysis.

Subscription: $125 for one year, $225 for two years.