GCA REPORT
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NEW DEVELOPMENTS

DOD Issues Single Offer Final Rule

The Defense Department issued a final rule on the procedures to be followed when only one "offer" is received under competitive acquisitions. The procedures are contained in Part 215 of the DFARS where the rule applies to several types of procurements identified throughout the DFARS and is different than an earlier proposed rule. The stated goal is to increase competition where possible but where only one offer is received, to ensure the price is fair and reasonable.

The procedures to follow in the final rule are as follows. The first step is to determine if the procurement allows less than 30 days for a response. If so, DFARS 215.271-2 will apply which requires the contracting officer to consult with the reporting activity as to whether the requirements document should be reviewed in order to promote more competition and re-solicit it, allowing an additional period of at least 30 days. (These less than 30 day procurements usually apply to a limited number of procurements – e.g. task orders under IDIQ contracts, commercial item purchases and Federal Supply Schedule buys.)

For procurements with at least a 30-day response time DFARS 215.371-3 applies. The CO will have to determine if the single offer is a fair and reasonable price base on a cost or pricing analysis. If the CO makes this determination the CO must then persuade a person at one level higher that the determination is valid. If so, adequate competition has been found to exist and award can then be made to the single offeror. If either the CO or higher level official believe the cost or price analysis does not support a determination that the price is fair and reasonable, then the CO must then obtain certified cost or pricing data (unless the procurement is for a commercial item) and use that data to negotiate with the offeror. If the procurement is for a commercial item then the CO is required to obtain uncertified cost or pricing data. In either case, there will likely be an extended period since the CO may want to obtain an audit of the data then analyze audit results before negotiations can begin (*Fed. Reg. 39126*).

Controversy Over Proposed Change to "Commercial Item" Definition Continues

The government is considering changing the definition of "commercial item" to lessen the opportunities to offer prices of items that are exempt from the cost buildup procedures of the Truth in Negotiations Act. Before the Federal Acquisition Streamlining Act (FASA) of 1994 was enacted, commercial items were considered to be products and services sold in substantial quantities to the public. Under FASA and other reforms, commercial item pricing was considered to be the preferred method of acquisition where the definition was expanded to include products and services "of a type" sold to the commercial marketplace. Recently, the Defense Department is widely discussing the need to narrow the definition to existing products or services that are actually sold, leased or licensed in the commercial marketplace which would, in effect, eliminate the "of a type" definition. Supporters of the change state that once an item is deemed "commercial" the government no longer has access to meaningful cost or pricing disclosures to negotiate a reasonable price even under conditions of sole source or non-competitive circumstances. Opponents of the change state that technology changes so rapidly that products developed for the commercial marketplace become obsolete which under the change would make them noncommercial requiring either expensive adherence to TINA requirements or loss of providers to the government. The opponents cite the example of making minor modifications to commercial items which though they do not significantly change the nongovernmental function of the commercial item would still lose its commercial item status. So far, the proposed change has not yet been codified in the 2013 National Defense Authorization Act.

DRAP Memo Limits Labor and Overhead Rates to 2010 Levels

In a June 12 memorandum to Defense Agencies sent by the Defense Procurement Acquisition and Policy group, a class deviation was issued limiting negotiation objectives for labor and overhead rates. The limit, which will be included in negotiation memoranda, states that for contracts or task or delivery orders awarded to a contractor in Government fiscal year 2012 or 2013, the labor rates and overhead rates will not exceed those the

contractor used for the same or similar contract services performed under contract with procuring DOD agencies in GFY 2010. An exemption to this rule must be approved in writing by the Secretary of the Military Department or Head of the Defense Agency. It will apply to all contracts, task or delivery orders awarded in FY 2012 or 2013. It would appear that if its overhead rates increase due to decreased work, a contractor can be stuck in a position of not recovering its costs. An interesting comment we came across on the change is that a CO may not have to obtain high level approval if though the rates are higher in 2012 or 2013 the overall cost is lower due to using a lower number of hours being contracted for but that is uncertain at this time.

Senate is Seeking Significant Contracting Reforms Under 2013 DOD Authorization Act

The Senate version of the FY 2013 National Defense Authorization Act contains a number of contract related changes. Significant ones include:

1. Section 824 would require DOD identify profit guidelines in the DFARS that should be modified to ensure an "appropriate link" between profit and performance. DOD is instructed to consider, at a minimum, (a) appropriate levels of profit needed to sustain competition in the defense industry taking into account the contractor's investment and cash flow needs (b) adjustments to address contractors and their subcontractors' level of risk and (c) appropriate incentives for superior performance taking into consideration quality, delivery timeliness, cost reductions, control of overhead costs and effective subcontract management including competition at the subcontractor level.

2. Section 842 would cap executive compensation for 2013 at $230,700.

3. Section 843 would clarify that DOD auditors have access to contractors' internal control audits and supporting documents in order to test and evaluate contractors' internal controls and reliability of its business systems and assess the risk in determining the scope of transaction testing for an audit.

4. Section 845 would require DOD to review the guidance on personal conflicts of interest for contractor employees.

5. Section 801 would require the modification of the DFARS to prohibit DOD from entering into cost type contracts for the production of major defense acquisition programs (MDAPs). An exception would apply if a senior undersecretary certifies that a cost type contract is needed to provide a required capability in a timely and cost-effective manner.

6. Section 802 would require that the acquisition strategy for each MDAP provide for (a) breaking out a major subsystem or subassembly conducting a separate competition or negotiating a separate price and (b) making the subsystem or subassembly available to the prime as government furnished equipment.

7. When the conditions in Section 802 are not feasible, DOD intends to prevent excessive pass-through charges. Section 822 would require DOD to amend the DFARS to (a) prohibit the award of a covered contract or task order unless at least 50 percent of direct labor cost of services will be spent for employees of the contractor or subcontractor that is specifically identified and authorized to perform such work (b) authorization for use of the subcontractor must be based on a written determination by the CO that such reliance is in the best interests of DOD after taking into account the added cost for overhead and profit as a result of the pass-through (c) require the CO to ensure overhead and profit are reasonable when a covered contract or task order having more than 70 percent of the direct labor cost of services are to be provided by others than employees of the contractor. The term "contractor or task order" applies to any performance of services that exceed the simplified acquisition threshold but does not apply to fixed price contracts awarded on the basis of adequate price competition or is for acquisition of commercial services.

The proposals are already generating industry responses saying the emphasis on fixed price contracts will result in excessive risks to contractors and the stress on profit seems to be moving in the direction of single digit profit levels which will create challenges to remain in the DOD industrial base. The Professional Services Council is criticizing the low pay cap stating the current compensation level of $763,000 is set by the market where the low cap will "crimp a company's ability to hire good workers." The Senate version is not yet final where the normal process is for Senate and House representatives to get together and hammer out a final version of the DOD Act.

DCAA Updates its Incurred Cost Electronic Model and its Information For Contractors Pamphlet

The Defense Contract Audit Agency has issued updates to both its electronic ICE model (it frequently makes minor changes so be sure to use the latest versions) and its 99 page "Information for Contractors" guide, both effective June 2012.

Update to ICE

- There have been some renaming of some schedules and format changes to coincide with changes made to FAR 52.216-7, Allowable Cost and Payment.
- Modified Sch. J to include all subcontracts awarded under flexibly priced contracts (e.g. cost reimbursable, T&M, Labor Hour, Fixed Price Redeterminable).
- Modified Sch. K to compute a material overhead rate.
- Removes Sch. P, Computation of IR&D/B&P costs and Sch. R, Reconciliation of Claimed to Corporate Tax Returns
- Corrects certain computational errors such as applying a G&A rate when the base is value added, cost of money when fringe costs are in the overhead base, fringe costs in overhead base at claimed versus G/L Account.
- Adds capability to handle multiple indirect, intermediate and cost of money pools e.g. up to five overhead pools, material handling and fringe pools, up to six intermediate pools and up to seven cost of money rates.
- Incorporates set up sheets to simplify the process of customizing the ICE.
- Allows flexibility to show pool costs by department or in total.
- Worksheets, columns and rows for unusual pools and departments are hid to simply presentation.

ICEManual.doc has been updated to reflect all the changes.

Information for Contractors

This useful guide has not been changed for over seven years. The changes mostly reflect more recent DCAA policies as well as including some clarifications. The new guidelines include "Enclosures" rather than "Chapter" content where the most significant changes include:

Enc. 1 – Introduction to DCAA. It now states its audits are conducted in accordance with Generally Accepted Government Accounting Standards (GAGAS) rather than those of the AICPA which are now incorporated into GAGAS. The enclosure also stresses the need to provide submissions and documentation in electronic form to further its goal of a "paperless environment." (*An interesting comment we saw is this emphasis on electronic submission is contrasted with DCAA insistence on contractors providing "original" as opposed to scanned electronic versions of documents in its audits.*) Also regional contacts are provided if contractors have issues while they are encouraged to resolve matters at the local level.

Enc. 3 – Pricing. Significant changes have been made. In the "DCAA Audit" section, recent policy changes are incorporated such as performing a proposal walk-through and a formal adequacy review before an audit begins and the requirement that contractors are alone responsible for providing adequate documentation to justify price reasonableness. In an expanded "Access to Records" section DCAA stresses that auditor requested documentation and access to contractor personnel must be provided in a "reasonable" period of time and if not, DCAA will notify responsible government personnel that a formal denial of access to records exists. In addition, DCAA states proposed indirect cost rates need to be supported by "long range forecasts/strategic plans." Finally, the FAR 15.408, Table 15-2 has been removed where it is now just referenced in a "Requirements for Submission" section.

Enc. 5 – Contract Financing and Interim and Final Vouchers. Detailed criteria for direct billing privileges has been removed and there has been an expansion of the criteria for billing on an interim basis in accordance with FAR 52.216-7.

Enc. 6 – Incurred Cost Proposals. The fact that DCAA required format (discussed above) be used is now formalized by FAR 52.216-7(d) has been added where there is expanded coverage on supporting documentation, subcontract management and cost accounting practices. Under the "Audit Evaluation" section GAGAS requirements to continually communicate with the auditee has led to emphasis on the requirement for there to be "continuous coordination" between the auditor and contractor to ensure timely resolution of issues and that "significant audit findings" will have been discussed, decreasing the need for long exit conferences. (*Editor's Note. There should no longer be surprised questioned costs.*) At completion of the audit the results are to be provided, in writing, to the contractor where the previous requirement to provide a draft audit report has been deleted. The revised guide also includes new sections emphasizing it is the contractor's responsibility to maintain adequate data to demonstrate its incurred costs are allowable and allocable, it should continually evaluate its indirect cost allocation practices to determine if changes are needed (*we whole-heartedly agree with this*) and contractors should notify the CO and DCAA of planned changes before

implementation (*we disagree where only changes by CAS covered contractors are required to be disclosed*).

The new guide is not yet available in hardcopy but it can be found at www.dcaa.mil.

DCAA Issues Its Annual Audit Plan for 2012 Calling for More ICE Audits

The DCAA audit plan for 2012 states it will now begin audits of incurred cost proposals six months after the end of a contractor's fiscal year as required by FAR 52.216-7. DCAA's goal of being current with ICE proposals is to be accomplished by dedicated incurred cost audit teams where these "virtual" teams will not be limited by geographic area. Comments we have seen in the July issue of Government Contracts Insights, which is consistent with our experience, stresses that contractors used to dealing with a DCAA having a backlog of audits extending back to 2005 in many cases will now be surprised to be facing new challenges in the face of new audit policies like:

1. Requests for "data dumps" (all G/L transactions for all expense accounts) in excel format spreadsheets. The requests are made to facilitate recent guidelines to follow statistical sampling methods for transaction testing.

2. In its new emphasis on strict adherence to GAGAS auditors are expected to be testing massive numbers of transactions where they will drill down from job cost ledgers to subsidiary ledgers (e.g. labor distribution reports) to source documents like timesheets, payroll registers and cancelled checks. DCAA may also be requesting personnel files to avoid the risk that employees do not exist. When contractors lack the documentation DCAA believe is needed contractors may face many more questioned costs than they did in the past.

3. DCAA is questioning more and more bonus and incentive compensation, asserting such costs are not "supported." DCAA is now, for example, requesting employee performance evaluations that are supposed to support the bonus paid which runs counter to most bonus plans that state there are some measurable parameters but usually stress that it is the company's prerogative to determine the amount of the bonus pool and how much is given to each employee. This area will likely be a shocker for most contractors who have not been exposed to many ICE audits due to the backlog and who have not been required to document such costs.

4. The authors point to the disconnect between DCAA requests for old documentation and FAR record retention regulations. The FAR Part 4.7 generally stipulates a three year record retention period after final contract payment where other sections provide for shorter periods for certain records (e.g. FAR 4.705 provides clock cards need to be retained for two years after the year of the transaction). However, DCAA tends to ignore such regulations because GAGAS requires such documentation no matter what the FAR provides.

DCAA Issues Guidance on Attorney-Client Privilege

DCAA has issued a memo to its auditors on what steps to follow when a contractor asserts the attorney-client privilege or attorney-work-product doctrine. The guidance stresses the audit objectives remain the same (i.e. determine if costs are allowable and allocable) and if a contractor denies access to requested information the branch office should pursue access to records until a high-level executive asserts the privilege in writing. When the written assertion is received, the issue is to be elevated to the DCAA regional office for coordination with the contractor's management (*12-PPS-018(R*).

Proposed Rule Removes Potential Barrier for Small Businesses to Receive R&D Contracts

The Defense Department issued a proposed rule Aug 10 that would clarify small business set-aside requirements for research and development contracts. The rule would revise FAR 19.502-2 to state COs must set aside R&D contracts above the simplified acquisition threshold when market research conducted in accordance with FAR Part 10 shows there are small businesses capable of providing the best scientific and technological opportunities. The proposed rule would drop language from the FAR 19.502 that has been interpreted to be additional and unique conditions to be awarded a R&D contract – "consistent with the demands of the proposed acquisition for the best mix of cost, performances and schedules." This clarification is intended to "remove potential barriers" and to emphasize the CO's decision should be based on objective evidence obtained from the market research conducted (*Fed. Reg. 47797*).

Final Rule Requires Public Reporting on Subcontractors and Executive Compensation

A final rule was issued July 27 requiring contractors to report executive compensation and first-tier subcontract

awards on contracts of $25,000 or more. The final rule keeps most of the interim rules in tact such as exempting the requirement if contracts are classified, awarded to individuals and if gross income is less than $300,000. The executive compensation reporting is required only if the contractor or subcontractor receives at least 80 percent of its gross revenue and $25 million of federal awards and if senior executives do not already publicly report compensation information. The rule applies to all businesses, commercial item contracts and commercially available off-the-shelf item contracts. The changes in the final rule provide that the new requirements are to be entered into the Central Contractor Registration when registering, "classified information", not "classified contracts" are exempt, clarifies that the contractor must report information on its first tier subcontractors but continued reporting on the same subcontract is not required unless one of the reported data elements change (*Fed. Reg. 44047*).

President's Small Business Plan Includes Accelerated Payments to Subcontractors

The White House announced initiatives designed to help the nation's small businesses expand and create jobs. The OMB memo issued July 11 directed agencies to make payments on an accelerated schedule to all of their prime contractors for the next year with the explicit understanding these contractors would accelerate payments to their subcontractors. This memo follows an earlier OMB memo a year ago requiring accelerated payment, typically 15 days, to one fifth of contracting dollars going to small business prime contractors (*See the memo at "whitehouse.gov/sites"*).

CASES/DECISIONS

Bond Costs Paid to DOE Contractor are Allocable and Allowable

In its clean-up contract at DOE facilities URS awarded a subcontract to GIT, terminated it for default and GIT sued URS for damages resulting in a judgment for GIT for $5.6 million. With the approval of DOE, URS sought to appeal the judgment where URS had to obtain a surety bond for $7 million to guarantee payment to GIT. The Court's decision ruled against URS where the surety paid GTI $7 million plus interest. URS reimbursed the surety company and then claimed the $7.8 million as a certified claim that the contracting officer denied asserting the costs were neither allocable to the DOE contract nor allowable legal and settlement costs. The Board sided with URS. As for allocability, the Board ruled the litigation and associated costs arose directly from the DOE contract where a "nexus" existed and hence were allocable to that contract. The Board next ruled the legal and settlement costs are allowable where such costs are unallowable only when a FAR cost principle explicitly disallows such costs. The Board alluded to an earlier board case, Hirsh Tyler, which affirms the concept that in a commercial marketplace where third party law suits are an ordinary and necessary function of business, legal and settlement costs to defend themselves are reasonable and hence allowable. The Board stated the claimed costs were reasonable under FAR 31.201-1 where the decision to terminate GIT was not unreasonable and the costs paid were not excessive (*URS Energy & Construction Inc., CBCA No. 2260*).

Charging Salaried Employees at Their Established Hourly Rate for Hours Worked Is Proper

The contracting officer denied payment to GaN for employee labor it asserted was improperly billed for certain employees, withholding $72,378. Though GaN never asserted it actually paid its salaried employees for each hour billed, the government asserts that evidence of actual payments under the payments clause meant GaN could only charge for hourly costs actually incurred and paid where if salaried employees were not paid for working extra hours, GaN could not charge the government for those extra hours. The Board disagreed with the government's interpretation of the payments clause finding the contract clearly provided that employees would receive a firm fixed price computed by multiplying appropriate hourly rates by the number of hours worked. It added other contract provisions relied upon by the government did not prohibit GaN from collecting its hourly rates for work performed by salaried employees (*GaN Corp., ASBCA No 57834).*

Costs of an REA Prepared by Employees are Unallowable

F. Versar's project manager and its QA/QC manager prepared and submitted a request for equitable adjustment where their costs were included. Referring to several prior cases, the Board noted that "costs of professional and consultant services incurred for the genuine purpose of materially furthering a negotiation process and rendered by persons who are not officers or employees of the contractor" are allowable contract administration costs. But here, where the REA was prepared by employees, the Board ruled "there is no evidence that appellant paid for any consultant or

professional services in connection with the REA preparation" (*F. Versar Inc., ASBCA 56857*).

Appeals Board Refuses to Reconsider JF Taylor Case

The ASBCA denied a request by the government to reconsider its position on the JF Taylor case we have reported on extensively where the board ruled that DCAA's normal approach to evaluating executive compensation levels was "statistically fatally flawed." The government put forth four reasons for the board to reconsider its decision: (1) the board ignored statutes that establish caps on exec comp (2) its decision ignored two seminal cases – Techplan and ISN – that allowed for a 10% range of reasonableness that was the major successful challenge by JF Taylor (3) JF Taylor's expert witness which the board relied upon exclusively was not a compensation expert but rather a statistical analyst expert and (4) the government had successfully rebutted evidence that was presented by JF Taylor but it was ignored by the board. the board ruled all four assertions were insufficient for revisiting its decision. How this decision will affect DCAA's approach to evaluating exec comp is still up in the air – DCAA has shown no inclination to alter its approach to these audits while attorneys are indicating the JA Taylor and Metron cases (we will cover this latter case in depth in the next DIGEST) provide strong grounds to challenge government positions in litigation.

ASBCA Denies Claim For Anticipatory Profits and Unabsorbed Overhead

When it received only three delivery orders on its custodial services contract compared to nine provided to another firm, Paradigm filed a claim asserting the Army negligently estimated requirements. DCAA audited the claim for unrealized anticipatory profits and unabsorbed overhead damages where it questioned $95,000 for the profit and $33,953 for the unabsorbed overhead. The Board agreed, disallowing the anticipatory profits on the grounds that Paradigm had refused several delivery orders where the performance work statement required the contractor to show it was ready, willing and able to perform throughout the contract period. The Board rejected the assertion of negligent estimates ruling the vagaries of troop deployment during the Iraq war caused the estimates to be inaccurate. Finally, the board denied Paradigm's claim for unabsorbed overhead based on personnel waiting for delivery orders noting the firm performed other work during the performance period and had no permanent employees besides the owner which showed Paradigm could not have had employees on standby status (*Paradigm II LLC, ASBCA No. 55849*).

NEW/SMALL CONTRACTORS

Sequestration is the Number One Hot Topic

The literature is dominated by sequestration news. As of this writing, there is no decision on what will be happening. The following is a summary of the news we have been following and some practical advice on how contractors can respond.

The Budget Control Act (BCA) of 2011 mandates sequestration on Jan 1, 2013. Sequestration is a simple mathematical proposition requiring automatic budget cuts. The BCA sequestration reduces federal expenditures by $1.2 trillion over nine years. The BCA assumes $216 billion will come from debt service savings leaving $984 billion or $109 billion per year which is to be evenly divided between defense and non-defense cuts. So absent congressional intervention sequestration will require $55 billion in automatic cuts to DOD which translates into 10 percent across-the-board reductions in 2013 spending.

The following is a summary of most of the highlighted sequestration news we have been following:

1. In July the House Armed Services Committee invited CEOs of some large contractors to ask how they are preparing for sequestration. Lockheed Martin said it must issue layoff notices to workers within months stating that DCAA has criticized it for not issuing immediate layoff notices. EADS North America said the cuts would ripple through the defense industry increasing the costs of defense equipment, putting many suppliers out of business and resulting in layoffs. Contractors' claims were supported by an Aerospace Industries Association report estimating across-the-board reduction could cost the country 2.14 jobs and increase unemployment 1.5 percentage points.

2. A DOD representative told Congress that in mid-July it was unaware of any DOD planning to prepare for the sequestration cuts. He estimated that cutting DOD civilian jobs would take a minimum of 105 days, including 60 days' notice to the affected individuals and 45 days' notice prior to that to Congress. To be prepared for this reduction in force (RIF) DOD must notify Congress by mid-September where RIF notification rules, labor agreements and unions must work together. Congress has told DOD it should

prepare for sequestration since it is the law of the land unless Congress votes to change it.

3. Another DOD official said they have not seen Pentagon purchasing officials delaying their buys even though many companies are reporting spending slowdowns in advance of sequestration. The official said it is not holding back any more than if sequestration was not occurring stating to do so would result in considerable inefficiencies and waste. The official also denied that the government would terminate a wide range of programs noting that many can move forward with funding that has already been approved.

4. Congressional representatives have pointed out sequestration would result in the elimination of 128,000 civilian full-time equivalents most of which would be permanent causing irreversible damage to the workforce. These reductions added to the current estimate of 30 percent of DOD's civilian workforce being eligible to retire (90 percent of senior managers) by 2015 will represent severe problems for the future workforce.

5. An Office of Management and Budget report states starting in Oct 2012 a share of funds might be withheld to ensure agencies do not spend money that would be sequestered. DOD must sequester "all budgetary resources" including prior year money not put on contracts and war funding. Money that is put on contracts starting in October would be subject to the sequester where about $572 billion will be subject to the $55 billion (9.6%) in cuts. Though DOD has said it does not intend to cancel contracts those with FY 2013 funding could be on the chopping block. Less drastic DOD actions may include (1) delaying signing of contracts with FY 2013 funds until January (2) signing contracts for FY 2013 budget amounts minus 9.6% and (3) using contract clauses similar to Limitation of funds clause.

6. The Department of Labor has issued guidance to federal contractors that they will not be required to provide advance notice to employees laid off from sequestration. DOL states the 1988 Worker Adjustment and Retraining Act (WARN) that requires 60 days' notice before mass layoffs will not apply. DOL have said efforts are under way to avoid sequestration and it remains uncertain whether budget cuts will be imposed as scheduled where federal agencies will have some discretion in implementing reductions if sequestration does occur. However, others have asserted DOL's letter is not definitive and contractors' legal representatives are saying they need to issue the WARN letters.

7. The Obama Administration has stated it will exempt military personnel accounts from across-the-board cuts meaning the 9.6% overall cuts will be more in other areas of defense.

8. There has been a lot of stories saying House Republicans and Senate Democratic leaders have indicated they may have a deal with the administration to pass a continuing resolution for six months to remove the threat of a government shutdown as the election nears. However, there are significant questions being raised about such a deal.

Darryl Oyer in his newsletter of Aug 7 provides some "Practical Considerations:"

1. For new awards, he says there will likely be delays on major procurement, an increased use of Limitation of Funds type clauses to limit costs and attempts to negotiate certain percentage reductions from prices where contractors should use discretion in agreeing to such reductions.

2. Under existing awards Mr. Oyer states the government may be inclined to do several things:

a. Don't fund where there is a limitation of funding clause where contractors may be reluctant to work "at risk."

b. Options may not be exercised.

c. Recission of contracts or termination for default to the maximum extent possible where contractors need to be extra diligent to remain in compliance to defend against allegations that could justify recission.

d. Termination for convenience where a contractor and the government should be prepared to analyze the cost versus benefit between continuing performance and termination costs to the government. For example, a termination for convenience can result in no delivery of product or service yet expenditures of 90% of funding for a completed item.

e. Directed deductive changes to contracts will mean contractors will need to diligently pursue requests for equitable adjustments (e.g. higher unit costs due to lower volume) where without sequestrations they may have been inclined to treat changes on a "no cost" basis.

Other commentators have stressed the need to review their contracts and subcontracts for termination rights, to see which contracts are at more risk (e.g. remaining work left, susceptible to delay or termination), review their performance assessments making sure to correct

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unfair ratings, bone up on delay and termination procedures and make sure cost accounting systems are in place to accurately track delay related costs. Our advice is to monitor congressional actions for progress in resolving sequestration but prepare for the worse.

QUESTIONS & ANSWERS

Q. I read your article about material handling and was wondering if you could provide some guidance. Let's say the base of the material handling pool is subcontractor and direct material costs. My thought is that as a result of this base, the labor for the purchasing department can only be allocated if their labor relates to purchasing of direct material or subcontracts or can I just put the entire purchasing department labor in the pool?

A. I think there is considerable room for flexibility but be aware putting in the entire purchasing department might tend to raise a red flag but could be justified. The red flag occurs because purchasing might be considered to be involved in all purchasing decisions such as supplies, facilities, etc. that are not direct material and/or direct subcontracts. However, if you can demonstrate the vast majority of effort is related to direct material and direct subcontracts then yes, you might prevail. Or you might allocate a large proportion to the handling pool by using a surrogate measurement like total purchases or invoices or something like that where still the bulk of purchasing could still be allocable to the handling pool.

Q. Many rental cars now come with the option of a GPS device. I can't find any guidance in the regs. regarding allowability of such expenses in indirect pools or on cost reimbursable contracts. Are GPS expenses allowable?

A. I think that is one of those questions where the guidance has not kept up with the new technologies (DCAA guidance on timekeeping is still primarily oriented to manual timesheets). Each individual auditor will likely have their own take on it. You should be able to support the cost by showing there is a legitimate business purpose for the extra costs (e.g. needed to locate business meeting and hotels) and consider including a discussion of this in your written policy.

Q. We recently went through our first CAS 409 audit where DCAA disagreed with our method for calculating our useful lives and basically said that we needed to recalculate our depreciation using their (DCAA) guidelines. For example, whereas we use five years on all categories of equipment DCAA said we should use 12 years for hardware, 16 years for software and 17 years for office equipment and furniture. We highly doubt that DCAA auditors maintain their software and hardware for 12-16 years.

A. DCAA's seem to be extraordinarily long periods so I would ask them to see the basis for them (I doubt whether they have it). Put the burden on them to justify the periods they are attempting to impose on you. As you know, for CAS 409, you are supposed to do your own analysis to determine the useful life of each major category of asset and then use that as the basis for the useful life. It looks like you are using default IRS guidelines which is fine for non-CAS covered contractors but you have to take the extra step of doing an analysis.

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