
GCA REPORT

(A publication of Government Contract Associates)

March - April 2002

Vol 8, No. 2

NEW DEVELOPMENTS

FAC-04 Issued

The Federal Acquisition Circular 2001-04 was issued February 8 amending the Federal Acquisition Regulation. Significant changes taking effect February 20 include:

1. *Extension of simplified procedures for commercial items.* Extends through January 2003 authority of agencies to use the simplified acquisition procedures to acquire commercial items valued at more than the simplified acquisition threshold (currently \$100,000) but not in excess of \$5 million (including options). This final rule terminates a prior class deviation that extended test procedures for defense contracts only.

2. *Formalizes the CO's right to unilaterally determine final contract payments.* Any doubts about a contracting officer's right to unilaterally determine the final contract payment amount if a contractor fails to submit a final invoice or voucher on time has been removed with the change to FAR Part 42. Under the final rule, COs will have the right to issue a unilateral modification determining the amount due on a contract if the contractor fails to submit a completion invoice or voucher within 120 days (longer if approved by CO in writing) after settlement of the final annual indirect cost rates for all years of a physically complete contract. The rule will apply to all existing contracts as well as those awarded after February 20. The final rule does accommodate the contractor in two ways: first, the CO's determination can be appealed under the Contract Disputes Act and second, the final rule provides examples of circumstances justifying an extension of the 120 day due date such as pending closeouts with subcontracts awaiting government audit, pending claims by any contracting parties and delays in contract reconciliation.

3. *Eliminates the need to divulge small impact CAS non-compliances for proposals.* Amends the FAR Table 15.2 instructions for submitting price proposals that require contractors to state whether they have been notified they are or may be in noncompliance with cost accounting standards. The new rule deletes this notice

requirement when the cognizant federal official has determined the cost impact of a CAS noncompliance is "immaterial." If the noncompliance goes uncorrected and later materially increases costs to the government, the contract adjustment provision of the "CAS" clauses will be enforced. The change is considered quite positive when "technical noncompliances" with CAS had to be divulged, sometimes putting offerors at a competitive disadvantage with a "CAS issue" hanging over them.

SARA Introduced

Rep. Tom Davis introduced the long-anticipated Services Acquisition Reform Act of 2002 intended to "assist federal agencies in adopting better practices common in the private sector to promote greater government efficiencies." Highlights of the proposal include:

1. *Speed up payments.* Revise the FAR to promote biweekly and monthly payment of invoices. Biweekly invoices would be submitted electronically, all invoices would be accepted or rejected within five days and paid no later than 30 days from invoice date.

2. *Increase threshold for purchase cards.* Streamline the "micropurchase" process by increasing the threshold for use of the purchase card from the current \$2,500 to \$25,000.

3. *Agency-level protests.* Establish an agency-level acquisition protest process where a "stay" of the award or contract performance during a 10 day period will be imposed to decide on the protest. The rights of filing protests with the GAO will not change.

4. *Expanded use of share-in-savings contracts.* Expand use of governmentwide share-in-savings contracts where agencies would enter into such contracts for up to 10 years. Such contracts would provide an incentive for contractors to find technological or management approaches to save money where contractors are paid from some of the savings realized and government retains the rest.

5. *Expand applicability of commercial items.* Three measures to encourage participation of more commercial firms

in the government marketplace includes: (a) redefine commercial items to clarify that a commercial item places services on the same level as supplies (b) amend the FAR to include time and material, labor-hour or similar contract types for services could, under appropriate circumstances, be used for acquiring commercial items and (c) further clarify in the definition that commercial items would include products and services provided by commercial entities whose primary customers are other than government. This conditions is met if 85% of its sales in the past three years are to non-government enterprises or have been commercial items defined under FAR Part 12.

6. *Adjust simplified acquisition threshold for inflation.* The Office of Federal Procurement will adjust the threshold level every three years to account for inflation for using simplified acquisition procedures (currently \$100,000).

7. *Raise threshold for A&E small business set-asides.* The FAR will be amended to raise from \$85,000 to \$300,000 the threshold under which architectural and engineering service acquisitions must be set aside for small business concerns.

8. *Preference for performance-based contracting.* To encourage use of performance based contracting a performance based contract or task order may be treated as a contract for a commercial item if it sets forth each task to be performed, defines it as measurable, contains mission related terms, identifies specific products or output and the source provides similar services to the public under similar terms to those offered to the government. The special simplified procedures provided in the FAR would apply to all such contracts or task orders valued at \$5 million or less.

DCAA Guidance on Contracts Cumulative Cost Data

The Defense Contract Audit Agency issued additional audit guidance to provide clarification on the purpose, use and requirements of the Cumulative Allowance Cost Worksheets (CACWS) as well as how they should be prepared. The focus on CACWS is apparently the result of a recent DCAA study that their proper use can lead to significant savings of audit hours for closing out contracts.

The guidance states auditors should verify receipt of cumulative cost and closing data in the contractor incurred cost submission (generally Schedules I and O). If not submitted, the proposal should be rejected as inadequate. The data should be examined and verified where the scope of examination will depend on the

strengths and weaknesses of the contractor's billing system. The lack of acceptable cumulative cost data should be viewed as a billing system deficiency where auditors will follow procedures for such deficiencies. If prior submittals lacked adequate data but the contractor is willing to provide the information prospectively, auditors will work with the contractors to establish a mutually agreeable process for closing old contracts where cumulative data is absent.

Auditors are also told to be flexible on the format of the information where contractors need not adhere strictly to the DCAA recommended format of the CACWS. The basic data required for the CACWS to be used by the CO to close out a contract includes (a) contract number and delivery/task order number (b) whether or not the contract is subject to the FAR penalty (c) whether or not the contract is ready to be closed (d) prior years' settled costs (e) current year(s) costs (f) contract limitations on contracts ready to be closed (g) any unresolved assist audit amounts (h) if level of effort contract, actual hours incurred and (i) fee for contracts ready to close.

Once the information is compiled by DCAA, the CACWS should be attached to the rate agreement letter. The auditor should make it clear to contractors that their concurrence to rates also means they are concurring with the CACWS data and that that data will be the basis for closing out contracts. A signed rate agreement with the CACWS must be included in the incurred cost audit report. Most of the time the CACWS should be acceptable to the CO to close out contracts without requiring a contract close out audit (01-PPD-084R).

New Measures to Expand Small Business Contracting Opportunities and Pressure for Contractors to Meet its Subcontracting Goal Plans

Effective as of February 22, 2002 the Small Business Administration has adjusted its monetary-based small business size standards to account for a 15.8% increase in inflation since 1994. The inflation adjustment to size standards that are based on receipts, net income and net worth (standards based on number of employees are not affected) is expected to benefit 8,600 newly-designated small businesses (Fed. Reg. 3041).

In separate moves, Congressman Alfred Wynn has proposed a trio of bills designed to help small business win more awards and get paid on time. The three bills are designed to:

1. Increase the governmentwide goal of contracting with small business from 23 percent to 25 percent.

2. Under the “Prompt Payment Improvement Act”, tighten up prompt payment rules for subcontractors by requiring agencies to give all contractors a copy of a prompt payment policy to be issued by the Office of Management and Budget and have all contractors provide the policy to each of their subcontractors. Penalties for untimely progress payments will be highlighted and a senior employee contact person will be identified for each contractor to discuss and resolve subcontractor progress payment questions.

3. Under the “Subcontractor Protection Act” there would be penalties established for prime contractors that fail to live up to their subcontracting plans for small disadvantaged businesses. Under the proposal, a federal agency would withhold up to 5 percent of the contract amount if a contractor failed to achieve the percentage goal of utilizing socially and economically disadvantaged businesses contained in its negotiated subcontracting plans. In addition, the bill (a) requires written justification if a contractor does not enter into a subcontract or substitutes another subcontractor for a specific small business concern identified in its small business plan (b) establishes a telephone hotline where a small business identified in a subcontracting plan may communicate its concerns regarding major deviations of a contractor from its obligations to use small business subcontractors and (c) require agencies to take into account a contractor’s past performance in meeting its SDB subcontracting goals when determining responsibility for a new contract.

OMB Revises A-76 Cost Comparison Inflation Factors

The Office of Management and Budget has updated the projected annual inflation factors government proposals should contain and when cost comparisons are conducted under OMB Circular A-76 rules for contracting out competitions between government and private entities. For FY 2003, OMB assumes a 2.6 percent employee pay raise and a 4.1 percent military employee pay raise. For FYs 2004 through 2012, OMB assumes a 3.4 percent annual pay increase for both civilian and military employees. The inflation rate assumptions for non-pay categories range from 1.9% to 2.3 percent. (Fed Reg. Mar. 4, 2002).

GAO Overhauls the Yellow Book

Extensive revisions to the Government Auditing Standards (GAGAS) commonly known as the “Yellow

Book” are being made. In addition to streamlining the standard and achieving more consistent application of the standard to various audits there is more emphasis on auditor independence in the shadow of Enron. Because the changes are so extensive, the new Yellow Book will replace the 1994 edition once the changes are finalized. A red-lined version of the exposed draft is available at www.gao.gov.

TRAVEL...

FTR Relocation Policy Reads in Plain English

Effective February 2002, the Federal Travel Regulation Part 302 covering relocation has been amended to convert the text into plain language.

Not Entitled to Weekend Lodging When Employee Goes Home

The employee was on temporary duty (TDY) for 120 days and asked his supervisors if he could be reimbursed for trips home on weekends while still maintaining his temporary lodging during those trips. His supervisor agreed and authorized reimbursement for using his car for the weekend trips. When the first travel voucher was submitted charging \$69 per night for lodging costs including the weekends he was away, the agency rejected the weekend reimbursements. When the employee stated it had prior approval the supervisor claimed he thought the employee was receiving a reduced rate from the hotel as a result of a long term lodging arrangement when no such deal was negotiated. The Board denied the employees appeal ruling though the JTR allow employees who return home when on TDY to be reimbursed per diem and mileage for the travel the regulations prohibit “lodging expenses at the TDY station for those days when the employee is absent from that location.” Even if long term lodging rates are negotiated employees are not entitled to reimbursement for night spent away from the TDY location. Rather, according to FTR 301.11-14, the long term rate may simply be used to calculate the average daily cost of a hotel room by prorating the cost of the long term lodging over the number of nights the employee actually occupies the lodging (GSBCA 15676-TRAV).

Board Clarifies Commuting Expenses

(Editor’s Note. The following identifies some of the discretion individual agencies – and by inference, individual contractors – have.)

A Social Security Administration (SSA) employee was directed to work Saturday morning in Newark, a site shorter than his normal commute to his permanent duty station in NYC. The SSA denied his voucher informing him employees are not entitled to commuter expenses between home and work. In his appeal, the employee argued he does not incur travel costs on Saturday and hence his travel costs should not be considered commuting expenses. The Board sided with the SSA even though it rejected its rationale. The Board said SSA was wrong in asserting the travel costs were nonreimbursable commuting costs since the commute is the distance between the NYC duty station and his home and Newark was not his official duty station. The Board explained that the employee was not entitled to reimbursement because agencies have the discretion to limit payment to employees for local transportation costs in excess of their normal commute and since SSA had that policy the shorter travel distance to Newark precluded excess commute time. The Board also rejected the employee's assertion that commuting costs occur only on weekdays citing a 45 year old GAO decision ruling employees can incur commuting costs on "any day of the week." (GSBCA 15655-TRAV).

CASES/DECISIONS

Contractor is Responsible for Subcontractor's Underpayments

(Editor's Note. The following case demonstrates the need of prime contractors to monitor their subcontractors' compliance with labor laws.)

The Department of Labor ruled that \$143,000 be withheld from payment to the general contractor to pay employees of the subcontractor who had been underpaid according to Davis Bacon Act requirements. In ruling the underpayment was properly computed, the DOL Administrative Review Board confirmed the contracting agency was required to withhold the amount determined to be underpaid from the general contractor and turn the money over to the Labor Department's wage and hour administrator for distribution to the underpaid employees (Thomas and Sons Bldg Contractors, DOL ARB, 00-050).

Government Rejects Defective Pricing Allegations

(Editor's Note. The following sheds some light on what does and does not constitute defective pricing data.)

In claiming \$496,000 in defective pricing plus interest on its contract for 592 retrofit kits, the government asserted Lockheed failed to provide cost data (1) to estimate the labor hours required to assemble five circuit cards (2) to indicate it had incurred program administration hours at half the rate it proposed and (3) to indicate labor hours for testing semiconductors would be reduced due to the transfer from inventory of previously tested semiconductors. In addition, the government argued Lockheed had overestimated the number of semiconductors to be tested by 30 percent, thus inflating labor.

The Armed Services Board of Contract Appeals rejected each allegation. For the labor required to assemble *five circuit cards*, Lockheed used its average labor dollars for assembling all of the 40-45 cards used in each system while the government said it should have used an estimate based on the five cards being furnished under the order. The Board concluded data for the five cards was available to all parties but neither party knew that a computation based on the five would have yielded a significantly different result. The Board stated the contractor only had the obligation to point out the significance of the different five card results if it knew or reasonably should have known and otherwise, both parties were able to calculate card specific data if they had realized their significance.

As for *program administration*, the Board rejected the government contention that though Lockheed had divulged data for program administration it failed to point out the significance of it. The Board concluded Lockheed neither knew nor should have known of the shortfall since program administration hours were never evenly incurred and greater hours were incurred later in its projects. Under both circuit card labor and program management, the Board ruled the purpose of the Truth in Negotiations Act (TINA) is to "establish a level field for price negotiations by requiring a prospective contractor to furnish factual cost or pricing data significant to the price negotiations known to it so the CO will have the same knowledge during negotiations." It concluded both the government and Lockheed were at a "level bargaining position" and "on equal footing."

As for the labor hours for *semiconductor testing*, the Board stated the number of parts listed in the proposal to be tested was an "estimate or judgement" by Lockheed which was not cost or pricing data under TINA because it was not factual and verifiable. Further, the Board claimed both parties knew the semiconductors were being transferred from inventory and neither party had ever considered the impact of these inventory transfers

on testing labor hours. The government had already agreed to pay Lockheed for 100 percent testing of all semiconductor parts when it accepted Lockheed's proposal – to later obtain a price reduction under TINA would enable the government to obtain these parts without paying for their testing, resulting in a violation of contract terms (Lockheed Martin Corp. ASBCA No. 50464).

Questions to Improve Proposal, Even if Technical Leveling, is Appropriate

After several discussions resulted in award of a contract, the unsuccessful offeror protested asserting, in part, the government improperly engaged in “technical leveling” where the three rounds of discussions resulted in improving the awardee's proposal that otherwise did not meet the solicitation's requirements. The GAO rejected the protest. It stated that technical leveling – helping an offeror bring its proposal up to the level of others through successive rounds of discussions – is no longer specifically prohibited since major revisions to FAR Part 15 were made a few years ago. Now, asking questions to improve a proposal and correct aspects which may not have met requirements is a legitimate goal of discussions (Imagine One Tech. & Management Ltd., GAO B-0289334).

Omitted Restrictive Legend Precludes Claim Eligibility

The contractor submitted an unsolicited proposal to the government to provide a variety of services. The title page contained a restrictive legend warning the government not to disclose proprietary data contained in the proposal. After its proposal was rejected the government issued a solicitation for the services and the contractor filed a \$72 million claim alleging the solicitation contained actual proprietary data contained in its proposal. The government rejected the claim asserting its failure to include a restrictive legend *on each page* containing the proprietary data violated the FAR confidentiality provisions. The Court alluded to FAR 15.608(b) which prohibits the government from disclosing “restrictively marked information” in unsolicited proposals. To qualify for “restrictively marked information”, FAR 15.609 requires a restrictive legend on the title page and each subsequent sheet containing the proprietary data. The legends must state the proposal contains data that “shall not be disclosed outside the government. The Court concluded the failure to include the restrictive legend on each page was “fatal to its claim” (Xerxe Group, Inc. v. U.S., 2002 WL 130708).

E-mail Equivalent to Oral Advice

Though the RFP asked for 81 horse power engines for a contract for motorized gliders, the Diamond Aircraft emailed the Air Force to ask whether its 100-hp engines would satisfy the RFP even though the contractor could not certify the larger engine would meet all technical specifications. The Air Force responded by email that the 100-hp engines would be acceptable. The 100-hp glider failed several minimum requirements specified in the solicitation and when the Air Force awarded the contract to another offeror, Diamond protested, saying its 81-hp glider would have satisfied the Air Force but it was misled by the Air force in proposing its 100-hp model. The Comp. Gen. rejected Diamond's argument, noting oral advice that conflicts with the solicitation is not binding on the government. Although the Air Force emailed its response, the advice was still informal, making it equivalent to an oral representation that Diamond accepted at its own risk. Rather, Diamond should have sought a written amendment to the solicitation enabling all offerors to compete on an equal basis (Diamond Aircraft Indus., Inc., Comp. Gen. Dec. B-289309).

Final Decision Followed by Negotiations Did Not Trigger Appeal Period

After receiving a final decision from the contracting officer, the contractor sent a note to the CO inquiring why the government had not responded to certain of the contractor's correspondences. The CO re-sent her decision that included a cover letter that included a proposed resettlement modification and offered to discuss some of the issues. When the contractor sought a meeting to resolve some of the dispute informally, the CO not only said it was receptive but expressed the “sincerest hope” for an agreement. The Board ruled it was only after the CO later reaffirmed her original decision – more than 90 days after the contractor received the first decision – that the decision becomes final and the statutory 90-day appeals period starts to apply (DK&R CO., ASBCA, No. 53451).

Termination for Convenience Affects IDIQ Minimum

An indefinite delivery indefinite quantity contract to provide jet fuel contained a provision that 75% (20 million gallons) of the maximum purchase quantity (27 million gallons) would be a minimum guarantee. Eight days before the contract expired, the CO partially terminated the contract for convenience, reducing the maximum quantity by 3.8 million gallons. The

contractor filed a claim for \$5.8 million for the difference between the original minimum guarantee and what the government actually purchased. The Board rejected this argument, stating that where the minimum guarantee is tied to an estimated maximum quantity (as in this case), a convenience termination reducing the maximum quantity also reduces the minimum quantity by a like amount (Hermes Consolidated, Inc. d/b/a Wyoming Ref. Co., ASBCA 52308).

Evaluation Credit Not Required for Unsolicited Technical Enhancements

(Editor's Note. The following demonstrates the strategy of offering more should be carefully considered.)

Under a solicitation whose evaluation factors were, in descending order, "technical", "management" and "price", both G&N and BMAR received an "outstanding" technical rating and since BMAR submitted the lowest price, it was awarded the contract. G&N, who had voluntarily offered solutions exceeding the technical requirements protested, asserting it should not have received the same score since G&N merely matched the solicitation's technical requirements. The Comp. General rejected G&N's arguments stating (1) protests concerning definitions of adjustments for technical scores should have been filed before the time set to receive proposals and (2) even if the protest was timely, the RFP did not provide for awarding extra credit for exceeding the solicitation's technical requirements (G&N, L.L.C., Comp. Gen. Dec. 285118).

NEW/SMALL CONTRACTORS

Some Indirect Rates You May Want to Adopt – Part 2

Since many of our clients and readers have been asking us about adopting different indirect costing methods, we thought we would identify some of the common practices found in both manufacturing and service organizations. This is the second article in this series and we have relied on both our own experiences and one of our favorite texts "Accounting for Government Contracts."

Service Cost Pools

In addition to actual manufacturing activities, services are often provided within the manufacturing facility. For example, an engineering group may provide producing

and designing services. When the costs of these services are included in indirect manufacturing pools, they can lead to problems with government auditors and customers who are seeking the lowest possible price. For example, if an indirect manufacturing pool includes both manufacturing and engineering services, a direct labor dollar base could assign a disproportionate amount of indirect costs to engineers due to their higher salaries. The government might object if a government contract receives a high amount of allocations due to an unusually high use of engineering services. Allocating excessive indirect costs to engineering services could result in non-competitive prices for contractors seeking government business. The solution might be to accumulate engineering expenses into a separate pool (or even multiple pools for, say product, design and software engineering) if the resulting rates would be significant.

Or, consider a service firm with multiple offices. If the government furnishes office space, utilities or supplies it could be inequitable for facilities costs to be included in an indirect cost pool and allocated to contracts for which the government furnishes some or all of these things. Not only would the government object to being overcharged but the contractor would likely not be cost-competitive when trying to win new business. In this case, it is quite common for contractors to keep two types of indirect costs: (1) indirect cost pool(s) at the home location and (2) indirect cost pools at the sites of specific customers. Overhead costs (we will get to G&A costs later) common to all contracts would be accumulated at the first category and costs specific to particular sites at the second category. For example, the home site pool might include rent paid for the home-office space plus fringe benefits for all indirect home office employees while the customer specific site might include no rental costs but all fringe benefits of indirect employees working at that site.

The allocation base for the services we have been discussing is usually direct labor hours or dollars. This is consistent with CAS 418 which prefers use of a labor allocation base when the indirect costs consist of management or supervision activities. Either a labor dollar or hour base is appropriate and if the benefits outweigh the effort, two separate pools – one with a labor dollar and the other a labor hour – may be used. Few other bases are usually appropriate though one variation might include fringe benefit costs of direct employees in the direct labor dollar base. Though the amount of costs allocated to a particular contract would most likely not be significant, it would have the cosmetic appeal of a lower indirect cost rate.

Fringe Benefit Pools

Fringe benefit costs include payroll taxes, pension contributions, medical plans, life insurance, employee welfare, etc. Often fringe benefits are not segregated in a separate pool but simply accumulated with other indirect costs. For example, the fringe benefits for both direct and overhead labor are accumulated in an overhead account and the fringe benefits for G&A labor accumulated in a G&A pool.

Whether it is to appear to lower indirect rates, focus management attention or achieve a higher level of precision, contractors may often decide to use a separate fringe benefit pool. Use of a direct labor dollar base is customary even though it is rarely precise. Unless multiple fringe rates are adopted (which is quite rare) everyone becomes accustomed to some level of imprecision since some benefits vary according to the number of employees (e.g. fixed medical insurance per employee) while other benefits vary according to salary (e.g. pension costs based on employee earnings).

Multiple fringe benefit rates may be desirable when fringe benefit rates vary significantly between groups of employees. Common examples include varying state related taxes (unemployment, workers compensation) or different union agreements between sites. Probably the greatest incentive for more sophisticated treatment of fringe benefits is the increased use of less than full time employees (*see GCA DIGEST Vol. 1 No. 1 for a detailed discussion in how to handle the fringe benefit costs of these different employees*). Full time employees may receive all fringe benefits while other less than full time employees may receive a limited range of benefits – say vacation and taxes but no health benefits or pension and still others (sometimes called "variable" or temporary employees) may receive no fringe benefits except payroll taxes. One solution might include accumulating fringe benefits in layers or tiers where the first pool would consist of only statutory benefits applicable to all employees, the second pool would consist of benefits applicable to the less than full time employees and the third pool to full-time employees.

Support Pools

Both manufacturing and service firms have a wide variety of potential support pools. Rather than include support costs in overhead pools and crediting the cost portion of revenue to the pools, contractors (or auditors' insistence) can eliminate both the associated costs and revenue of certain support functions from overhead and G&A pools and treat them separately as service centers. Some of the more common support pools include:

Occupancy costs. Occupancy costs include building depreciation, amortization of leasehold improvements, maintenance costs, utilities and other related costs. The occupancy pool is usually an intermediate pool that is allocated to other indirect cost pools rather than directly to final cost objectives. Square footage is the most common allocation base. Though less common, number of employees (when area and type of space used by each employee is similar) or cubic space (when utilities costs are significant and areas with high ceiling use more than those with low ceilings) can be used when the basis is reasonable.

Computer Operations. The costs include computer operations for equipment, supplies and personnel and are commonly associated with (1) business applications such as accounting and payroll or (2) scientific or engineering applications. A large computer operation might justify creating two pools where accounting functions could be charged to G&A and scientific functions charged to cost objective that benefit most. Selection of appropriate allocation bases for the second type of costs can be problematic – use of computer time can be difficult because computers process several jobs at once while other usage measures (e.g. central processing time, number of input or output channels, amount of core storage, number of lines printed, number of records handled) need to be carefully selected and monitored.

Other Support Services. Other frequently used indirect cost pools collect a wide variety of service costs. Common examples include: (1) reproduction cost pools consisting of costs of copying machines, machine operators, supplies allocated on copies made (2) graphics, art and photographic departments allocated on items produced (3) communications costs such as telephone, cell phones, etc. allocated on headcount or on number of telephone lines (4) vehicle related expenses allocated on mileage. In addition, special facilities (e.g. wind tunnels, heat treatment, environmental chambers and microelectronic centers) are also common and a usage allocation base such as time spent or number of items processed are usually preferred by auditors over labor bases.

Charge Rates. In the past, the government preferred that all costs in each support center be allocated to benefiting users using a provisional rate that was adjusted at year end for actual costs by charging or crediting the center's costs for over or under allocations. Methods used to accumulate pooled costs and allocation bases have always been a major bone of contention between auditors and contractors so establishing charge rates

using commercial prices has gained in popularity. This is generally acceptable as long as contractors can show their costs are similar or above commercial costs.

General and Administrative Pools

G&A costs, sometimes referred to as the remaining costs, are those expenses not identifiable with particular cost objectives but necessary for the overall operation of a business that include the costs of management, legal and accounting, public relations, business taxes, selling and marketing and similar costs. In a corporate structure, the firms' G&A expenses may consist of costs at the business unit as well as allocations from the group and corporate level. G&A expenses are allocated based on some measure of the activities of the entire organization. CAS 410 states the preferred bases are the total cost input base, the value added base (excluding material and/or subcontracts) or a single element base (commonly direct labor).

Convincing the government to accept other than a total cost input base for manufacturing firms can be a challenge while having them accept such a base for service firms can equally be a challenge. To do otherwise, the contractor needs to establish a distortion exists and use a multiple regression analysis to help illustrate the historical relationship. The contractor should not attempt to justify the change based on competitive reasons – this may be a motivator for the contractor but the auditor ignores this and looks only to the concept of good accounting.

QUESTIONS & ANSWERS

Q. We are a small company and need to conserve cash so we don't want to pay out the full amount of salary

due to our two senior executives. The executives have enough savings to wait but we are worried about getting credit on our cost type work this year for their salaries. What do you suggest?

A. The fact they earned the salaries this year (assuming the salaries are "reasonable") and you are paying them in a later period would qualify as deferred compensation. (Year end accruals for salaries, wages and bonuses that are paid in a reasonable period of time after the end of the accounting period are not considered deferred compensation). You are right about worrying how to get credit this year since you could not claim their compensation in the period you pay them but rather it must be claimed in the year they earned it – i.e. this year. You should account for the deferred compensation in accordance with CAS 415, "Accounting for the cost of deferred compensation" that basically requires (1) the assignment of costs to the period when the obligation was incurred and (2) the use of the present value of future payments as a means of determining liability for the deferred compensation. Make sure you establish the liability this year for the future payments.

Q. In a previous Q&A section addressing how to burden IR&D costs and assign them to the G&A pool, you seemed to imply that you do not always have to burden the costs. Is that true?

A. Good observation. Our answer did seem to leave the door open for either treatment but after researching bid and proposal costs for an article in the last GCA DIGEST issue we realized we made a mistake. CAS 420, "Accounting for independent research and development costs and bid and proposal costs", applies to both CAS and non-CAS covered contractors in this respect and it requires all direct and indirect costs (excluding G&A) be included as part of IR&D and B&P costs.