NEW DEVELOPMENTS

Commentators Discuss Strategies to Win Business During Tough Times

We have seen a proliferation of articles addressing sensible actions contractors should take in this environment of significant budget cuts. Here are a few examples:

Olessia Smotrova of OST Global Solutions has many recommendations to identify a “pipeline” of business opportunities. She suggests (1) subscribing to databases of business opportunities such as Bloomberg Government, Deltek and Centurion Research that show what contracts and task orders are expiring, customer information, values of previous contracts, etc. (2) register with customer procurement websites where though FedBizOpps theoretically is supposed to post each agency’s opportunities the Army has its Single Face to Industry and the Navy uses Navy Electronic Commerce Online and smaller agencies such as Sandia National Labs may not even post (3) build trusted advisor relationships with prospective customers who will see your firm as a source of indispensable advice where you may want to offer unsolicited proposals the agency may need but has not yet asked for or “wire” the RFP requirements to your competencies (4) train your workforce who work on projects to look for business opportunities rather than rely solely on a CEO or one business development person (5) seek out small purchases or sole source awards if you are small and new to the government marketplace (6) team with a prime contractor to provide irresistible value and make sure you are registered as a small business on prime contractors’ websites and (7) leverage social media such as Linked In.

Mike Lisagar of Centurion Research advises to first be aware of trends in your area of expertise such as trimming of professional services, construction delays, re-competes that are bundled and awarded to lowest price bidder, de-scoping current contracts and extending contracts through options to avoid costly acquisitions. He said as the government turns away from war new presidential priorities that are likely to be funded are job creation, high tech manufacturing, clean energy and energy efficiency, science and research, climate change, infrastructure, cybersecurity and veteran health, education and job opportunities. “Hot” agencies likely to get more funding include Departments of Human Health Services (e.g. 10 year ID/IQ IT services contract, NIH award of $20 billion to 54 companies via 10 year contracts), Homeland Security (e.g. EAGLE II worth $22 billion, PACTS worth $1.4 billion), Veterans Affairs (e.g. paperless disability claims processing), Energy (e.g. $153 million for electricity delivery, $80 million for integrating clean energy into the grid, $615 million for clean energy and $365 million for lower energy manufacturing) and Defense ($5 billion for cybersecurity, $2.5 billion for intelligence and surveillance).

Other articles have pointed out the need to hone in the proposal and “capture” management functions such as gathering proposal intelligence, developing and monitoring a proposal budget, facilitate other corporate resources in proposal development, develop “price-to-win” strategies, be more familiar with clients’ organization and technical requirements, key staff and buying habits and obtain greater knowledge of competitors’ contract awards and their performance, core competencies, costing practices and technical abilities.

DOD Sets New Thresholds for Past Performance Evaluations

The Defense Department has set new higher thresholds for determining when past performance must be evaluated in all source selections and when agencies are required to evaluate contract performance. The new thresholds were established as a class deviation from the current FAR Part 15 and 42 provisions that basically provide for the evaluations when the simplified acquisition threshold is exceeded. The revised past performance thresholds also are to be applied to individual task or delivery orders in accordance with FAR 42.15 when they provide more useful information than just contract evaluations. Past performance will now be evaluated in all source selections for negotiated competitive systems and operations support acquisitions expected to exceed $5 million, services and IT acquisitions expected to exceed $1 million and ship
repair and overhaul expected to exceed $500,000. Past performance need not be evaluated if the contracting officer documents the reason why it is not an appropriate evaluation factor. The thresholds for construction contracts at $550,000 and architect-engineer services contracts at $30,000 are not changed by the deviation (Fed. Reg. Sept 24).

**DOD Drops Dollar Threshold That Prohibits Bundling of Contracts**

In a move to lessen the extent of bundling contracts that tends to lessen opportunities for small businesses, the Defense Pricing and Acquisition Policy (DRAP) issued an Oct 1 class deviation to the FAR and DFARS that lowers the threshold that DOD agencies may not bundle contract requirements from $6 million to $2 million. DFARS 207.170-3 prohibits agencies from consolidating requirements with estimated totals above the threshold unless an acquisition strategy includes market research results, an identification of any alternative approach with less consolidation and the senior procurement executive’s determination that contract consolidation is necessary and justified. Market research may indicate that bundling is justified if costs, quality, schedule or other benefits “substantially exceed” those of the other alternatives. Administrative or personnel cost savings alone do not justify bundling requirements unless savings are “expected to be substantial in relation to the total cost of the procurement”.

**Industry Group Opposes New Executive Compensation Changes and Proposals**

The influential Council of Defense and Space Industry Associations (CODSIA) submitted comments opposing the proposed and interim rules on senior executive compensation. A June interim rule amending the FAR expands the executive compensation caps to a broader group of contractor employees on contracts awarded to DOD, NASA and the Coast Guard after Dec. 31, 2011 and a proposed rule would have the caps applied to contracts awarded before that date. CODSIA says the rules would be a “retroactive application of a change to a cost principle which is a breach of contract” entitled a contractor to damages. CODSIA said the breach of contract would apply to both the interim and proposed rule and in addition, would impose significantly more recordkeeping by requiring more than one billing rate structure for 2012 and 2013 and “perhaps more in the future.” (Go to “r.reuters.com/vam82v” to see the comments.)

**DCAA Guidelines and Staffing Needs for 2014 Are Issued**

**Testing Reliability of Scanned Images**

The guidance first summarizes the requirements covering scanned images in FAR 4.703. It allows contractors to duplicate and store original records in electronic form where they are not required to maintain or produce original records during an audit if the contractor provides photographic or electronic images of the original records. To qualify, FAR 4.703(c) requires the contractor (1) has established procedures ensuring the imaging process preserves accurate images of the original including signatures, written or graphic items and the imaging process is secure (2) maintains an effective indexing system to permit timely access to the imaged records and (3) maintains the original records for a minimum of one year, and after imaging has occurred to permit periodic validation of the imaging system. FAR 4.703(d) allows contractors to transfer images from one reliable computer medium to another if the transfer maintains the integrity, reliability and security of the original images. So how are these requirements met?

Auditors are to test the contractors scanned images annually as part of their audits such as incurred costs, proposal, etc. The testing will cover the previous 12 month period so it should be conducted in one of the first audits of the fiscal year. By testing the previous period it should be easy for auditors to determine if they can rely on the images for subsequent periods. Though the guidance states the previous 12 months should be reviewed if incurred cost audits are being conducted for several years auditors are told to follow the steps below for those years of the ICP audit if scanned docs are reviewed.

For the planning process auditors will request a demonstration walkthrough and whether a transfer from one computer medium to another has or will take place. At a minimum, auditors are to (1) test a sample of images to original documentation and determine whether timely access to the imaged records exist and (2) if a transfer has taken place make sure there is an audit trail. If the transfer is planned for the future, auditors are encouraged to assess compliance on a real time basis as the transfers are taking place. If no deficiencies are found then those tests can generally be relied on for concluding the scanned images accurately reflect the original documents and no further testing of internal controls are required. If tests were taken in the previous year auditors are still to test subsequent years but may avoid the walkthrough if they are satisfied
that no changes have occurred. These steps will be taken at all contractors with a minimum auditable dollar value of $100 million and less at the auditor’s discretion, taking into account contract mix, whether the contractor is high or low risk for ICP audits and whether electronic images are usually provided for audit documentation.

However, concerns can be raised with DCAA management calling for more testing of internal controls. Though internal controls reviews are not encouraged the guidance does remind auditors that the absence of internal control reviews does pose the risk that hardcopy documents could have been altered and auditors “must consider fraud indicators and other known risk factors” that alterations could have occurred similar to the thought process that any hardcopy document can be altered. If no testing occurred in prior years, auditors are told to determine if original docs have been preserved. If they were, auditors are told to conduct a test sample of imaged docs against the originals. If the originals do not exist, auditors are told to examine the permanent files to determine if there is risk the scanned docs cannot be relied upon. Assuming no risk then the auditor is to finish his audit and “at a minimum” qualify the report.

The guidelines replace earlier DCAA guidance on scanned documents going back to 2008. Comments we have encountered have praised the new guidelines saying they are far superior to the older guidance that were burdensome on contractors and went far beyond what FAR Part 4.7 required (13-PPS-016(R)).

♦ DCMA and DCAA Guidance on Forward Pricing Rate Proposals

The guidance informs auditors that new Defense Contract Management Agency policy now encourages completion of DCMA Forward Pricing Rate Proposal (FPRP) audits within 30 days and negotiation of these rates within 60 days. The audit guidance states “technical specialists (including DCAA) are not necessary to complete” DCMA’s audits and negotiating process. Interestingly, the DCAA guidance does not mention the need for it to speed up its audits stating for its FPRP audits “the ACO will assess any findings, determine any effect on an existing FPRP and resolve any significant findings.” Some comments we have seen state DCMA’s highly expedited approach is a disguised (or not so disguised) criticism of DCAA’s failure to provide timely FPRP audits to help expedite the acquisition process (13-PSP-019(R)).

♦ The DFARS Proposal Adequacy Checklist

The guidance alludes to the new DFARS Proposal Adequacy Checklist at DFARS 215-408(6) issued March 28, 2013 and includes a copy of the new checklist. The guidance states DCAA’s Criteria for Adequate Contract Pricing Proposals will be retired. Auditors are told to review the checklist that is required to be submitted with proposals and identify concerns and noncompliances. Many commenters praise the new checklist and note its superiority over DCAA’s checklist (13-PSP-020/R).

♦ Employee Testing When Audits are Late

The new guidance addresses what happens when DCAA audits of timekeeping and labor charges are not timely. Though DCAA guidance states employee testing should occur yearly, labor audits along with incurred cost audits have fallen behind where up to seven year lapses are not uncommon. Noting that verification of direct costs can be made only for the year being audited, employees’ time will need to be for the year being audited even if many years have elapsed. For employees still working, auditors are to physically observe them and ask when was their start date. For employees no longer working, auditors are to review employee personnel documents (e.g. drivers license, passport, parking badge), validate payment to bank records and review other documents such as travel expense reports and work authorizations. When DCAA has not conducted real time testing of labor, auditors are told to issue a qualified opinion or a disclaimer opinion.

♦ DCAA Issues its 2014 Staffing Plan

DCAA issued its staffing plan for the period of Oct 2013 through Sep. 2014 which is useful for identifying its priority audits over the next fiscal year. Requested (called demand) audits for such things as proposal audits will continue to be the No. 1 priority. Next, will be closing the backlog of incurred cost proposals. In addition, there will be DOD mandated “high risk” audits such as closing out overseas audits which are largely incurred costs and post award (defective pricing) audits. Details include:

• The staffing plan notes that fixed price proposals must exceed $10 million to be audited by DCAA and cost type contracts must exceed $100 million. Pre-award accounting system audits in conjunction with proposal audits will be considered equal priority to proposal audits.

• For ICP audits, the goal is to complete 2008 and a portion of 2009 ICP audits and, at least, all ICP audits ending Dec. 2007 by March 31, 2014 so, though not mentioned, running up against the six year statute of limitation claims can be avoided where recent cases
have ruled the six year clock starts at the time of ICP submission. Dedicated ICP audit offices will be used to conduct only ICP audits and the number of contractors selected for audit will be significantly reduced due to recent DCAA audit guidelines we addressed in earlier newsletters. Audits of ICP for 2010 and later are not anticipated.

- The overseas contingency audits will cover all ICPs submitted through FY 2009 which will include home office and service center audits for costs that are allocable to those contracts.
- Defective pricing audits will be those currently in progress plus other audits identified by DOD has high profit or otherwise high risk.
- Unaudited changes to CAS Disclosure Statements where they are considered to have a high impact to contract costs. CAS compliance audits which normally are conducted on a cyclical basis will now be conducted only for contractors considered to be the highest risk to the government.
- Billing and accounting system audits and other business system audits that are carryovers from 2013 will be conducted but no new audits for 2014 have or will be identified.
- Assistance to DCMA conducting Earned Value Management System (EVMS) will be provided when requested by them.
- Follow up system reviews for corrective action will be conducted on a case-by-case basis in coordination with contracting offices.

DCMA’s Letter Addresses Corrective Action Requests and Inadequate Business System Allegations

In response to issues raised in an April Industry/Government conference the Defense Contract Management Agency issued a letter to the National Defense Industry Association (NDIA) addressing corrective action requests (CARs) and the role of DCAA in asserting a contractor business system is inadequate. If contractors self identify non-compliances and take timely actions to fix them CARs “are normally not needed” which should be “the ultimate goal.” As for how CARs should be dealt with at the subcontract level, the letter states CARs should no longer be issued at the prime contract level but directly to the subcontractor. In situations where subcontractors do not implement CARs in a timely and effective manner, a Level III CAR will be issued to the prime. In response to complaints that DCAA has been calling COs/ACOs to say they cannot award a new or follow-on contract due to deficiencies found in a contractor business system (CBS), DCMA stressed that only a CO may approve or disapprove a CBS. If a subcontractor’s inadequate CBS is having a negative impact at the prime level DCMA will notify the prime meaning it will be the duty of the prime to address the issues with the subcontractor.

Standards for Security Clearances Will Likely Change

The head of the Professional Services Council (PSC) Alan Chvotkin stated that contractors can expect tougher security clearance investigations following the Sept. 16 Navy Yard incident where 12 people were killed and the leaks of classified information by Edward Snowden. Chvotkin said in the midst of congressional and DOD reviews of security granting procedures, the federal government will tighten eligibility for security clearances as well as investigations. He said these clearances and investigations will be outsourced because the cost of hiring more government employees will be too high but Defense Deputy Secretary Ashton Carter states they may be in-sourced.

Deltek Issues White Paper on GSA Contracting

The accounting software company Deltek has issued a white paper providing advice to offerors for GSA schedules that we find addresses some key issues many GSA contractors are confronted with. First, you must decide what products and services you will be providing, the nature of the government market for them and which schedule or schedules would be most effective. Next, you need to decide what pricing and discounting you want to offer where the GSA contracting officer must be assured your prices are fair and reasonable and understand what commercial discounts you provide to your commercial customers under specific conditions. Much of the white paper addresses the two most problematic areas - basis of award and the price reduction clause (PRC) contained in the GSA Federal Acquisition Regulation.

The PRC provides that the offeror and GSA CO must agree on the customer or group of customers that will be compared which is known as the basis of award (BOA). The parties must always ensure that what prices and discounts the government receives are equal to or better than the BOA so the selection of the BOA is critical. The PRC addresses price reductions and discounts during the life of the contract. A price
reduction can occur for many reasons – e.g. revise the catalog or list price, giving a BOA a more favorable price or discount than the government or granting a special discount to a BOA. If a reduction occurs, the CO must be told within 15 days and offered the same discount during the same period of time. Failure to comply can result in penalties including a breach of contract claim, termination of the contract or a false claims act claim resulting in treble damages.

Getting the BOA right in the first place is critical. Factors that can cause a price to a BOA to be different than that offered to the government should be spelled out explicitly so the CO can see clearly why there may be a difference in price. You don’t want the BOA to be so broad that you must offer each and every price discount given to a commercial customer to the government. The BOA wording and discount price relationship must be clear in case of audit by an auditor unfamiliar with the contract. The white paper recommends informing the CO of everything and then mention caveats and qualifiers that explain why a customer’s price or discount may not be comparable.

GSA Approves a Slight Increase in Per Diem Rates

Ending a long freeze on federal travel reimbursement rates the General Services Administration has raised the per diem rates slightly for 2014. The standard lodging rate for locations within the US has increased from $77 to $83 while the standard rate for meals and incidentals remains the same at $46. The standard rates are for those non-designated areas not specifically identified. GSA also announced, in reaction to the scandals related to government conferences, it will eliminate the conference lodging allowance that allowed travelers to spend 25 percent above the established per diem rates for conferences.

CASES/DECISIONS

“Would Have Cost” Rule Should be Used to Quantify Deductive Changes

(Editor’s Note. The following case is particularly timely since it addresses how to cost deductive changes that we see proliferating in response to government budget cuts. Comments on this case all state the proper method of computing contract price adjustment for deductive work is the “would have cost” method described below and the importance of having an adequate accounting system even when most contract work is fixed price.)

EJB hold a firm fixed price, indefinite quantity contract where the Navy deleted certain contract requirements such as receiving, storing and delivering Navy property. EJB argued the Navy was required to calculate the price reduction using the “would have cost” rule (what it would have cost to complete the deducted work as measured by the actual historical cost of performance) where the reduction would have cost $565,000. The Navy argued it was entitled to use EJB’s original contract price resulting in about $1.8 million due. The Navy argued first that a prior case – Control Line, ASBCA No. 50235 – provided an exception for the would have cost rule where the Board disagreed saying in that case, there were unit prices not based on estimates of costs where here EJB had estimated the costs at the time of the deductive change. Next, the Board rejected the Navy’s assertion that the original proposal price was “a sufficient measure of the downward adjustment” stating deductive changes are usually the result of contractors’ current estimates or “would have cost” projections. The Navy also contended EJB’s accounting system was inadequate because it “failed to segregate the actual costs of the change.” To this argument the Board stated there was no duty to segregate the costs where if it was desired it should have been part of the contract. Further, the Board noted that DCAA had found its accounting system to be adequate for accumulating contract costs (EJB Facilities Services, ASBCA No. 57547)

How to Incur Over $300,000 of Non-Reimbursable Expenses on a Cost Type Contract

(Editor’s Note. The following case, particularly important to new contractors, is a useful reminder to comply with the Limitation of Cost clause and that cost type contracts do not automatically provide for reimbursement of all costs.)

The US Army awarded a cost type contract to PHI to develop a fluorometer to detect weapons where the contract set an estimated total cost of $37,730. Like all cost type contracts it contained the limitation of cost clause requiring it to notify the CO when within the next 60 days it will exceed 75 percent of the cost specified in the schedule. The government paid the first two invoices totaling $36,184 where soon after DCAA conducted an audit where it noted PHI had invested in an accounting system allowing them to track contract costs where it had spent $300,000. Several invoices were submitted to the CO for costs allocable to the contract, to develop the accounting system and to respond to the audit but were not paid. The Board ruled against PHI stating it was only entitled to $1,546 plus interest, the difference between the original estimated amount and what it had
been paid. It found that PHI had failed to adhere to the limitation of cost clause noting the clause is intended to “benefit both the government and contractor by both limiting the government obligations to pay and the contractor’s obligation to perform to the agreed contractual ceiling.” The Board rejected PHI assertion that it could not have met the 60 day notification because it had experienced cost overruns very soon after work began stating the clause required it to notify the government whenever it had knowledge of potential overruns even if the 60 days could not be met (PHI Applied Physics, ASBCA No. 56581).

Inadequate Discussions Led to Flawed Award

Sentillion bid on a Marshal Services proposal seeking security services at over 900 courthouse facilities where the agency planned on awarding either three awards covering three regional areas or one nationwide award based on the lowest price, technically acceptable bid. When Tyco won a $265 million contract, Sentillion protested asserting the agency failed to inform it of certain license applications it had considered to be incomplete. Sentillion said discussions with the agency were misleading because its post-discussion adjustments did not prevent it from being deemed technically unacceptable. The GAO agreed, stating though the agency raised deficiencies under the business license subfactor it did not advise Sentillion the agency believed the applications were incomplete. The GAO concluded that the failure to convey all its concerns ultimately led to Sentillion’s unacceptable rating under the application subfactor category. The GAO ordered the competition be reopened, conduct meaningful discussions with all bidders in the competitive range, request revised proposals and make a new source selection (Sentillion Corp., GAO, B-406843).

Oral Agreement Not Valid Without a Written Contract Mod

Following a termination for convenience Sigma submitted a request for equitable adjustment for delays prior to the termination that caused it to incur additional costs. The parties, according to Sigma, agreed to a $485,000 settlement in a telephone conference. Subsequently, the CO told Sigma the regional office did not accept the settlement and an audit was required. After unsuccessfully pursing claims with the agency Sigma filed a complaint. The government moved to dismiss the complaint asserting it did not sufficiently allege the existence of a separate, enforceable settlement agreement. The court said though some oral agreements can be binding, FAR Part 49 states that a settlement for a termination for convenience requires a written contract modification executed by the contractor and CO. Since FAR 49 defines a settlement as a written agreement in the form of a contract modification, the alleged oral agreement did not create a binding final agreement (SIGMA Constr. Inc. vs US, Fed. Cl. No. 12-865).

QUESTIONS & ANSWERS

(Editor’s Note. We are waiving our usual feature article to catch up on the many questions we have received over the last couple months.)

Q. I am not sure if we are CAS covered and if so, whether we are fully covered or modified. Could you remind me of the rules?

A. First, a contractor is not CAS covered but particular contracts and subcontracts are. In practice, if you expect to have a CAS covered contract then you should ensure your accounting practices comply with CAS. The trigger for CAS coverage is a $7.5 million negotiated contract that does not meet the exemptions discussed below. If you do not meet this threshold, no contract or subcontract is CAS covered. If you do, then you have to next decide if it is fully or modified CAS covered. If the current award is $50 million or more or if it is less than $50 million but the total of CAS covered awards in the prior fiscal year were $50 million or more, then the award is fully CAS covered and all future awards exceeding $700,000 are also fully CAS covered (this dollar amount changes periodically). If the $7.5 million threshold is met but not the $50 million one then the contract award is subject to modified CAS coverage. Fully CAS covered contracts are subject to all 19 standards while modified CAS coverage is subject to only four – CAS 401, 402, 405 and 406. If the dollar thresholds are met certain contracts and subcontracts are still exempt such as if the contractor is a small business, contracts are for the acquisition of commercial items, fixed price awards are made on the basis of price competition where no cost data is submitted. If the thresholds are not met don’t be lulled into believing the cost accounting standards do not apply. Many FAR provisions essentially duplicate many of the standards or require computation of costs in accordance with CAS. In addition, most auditors consider CAS to be the essential criteria for indirect cost allocations so if one of your practices are clearly inconsistent with general CAS requirements it will likely be considered an improper practice.
Q. Our system was originally setup (nearly 20 years ago) to track government marketing costs separately from industrial marketing costs. We have always considered industrial marketing as unallowable. In reviewing the current FAR regs we are confused as to whether or not this is still true.

A. I think you have been wrong for nearly 20 years – that may be a record. Marketing costs, whether for commercial or any government purpose, are normally allowable unless they are considered lobbying, influence pedaling or “unreasonable.” The justification, confirmed in numerous court cases, is that marketing costs contribute to increasing the business base of the firm which leads to lower indirect cost rates which, in turn, benefits the government. This, of course, does not prevent some uninformed auditors to question marketing costs – we have often seen them question either commercial related marketing or government marketing as not benefitting government contracts but such reasoning is wrong. You may want to consider revising prior ICPs where audits have not been initiated.

Q. We have multiple indirect cost rates which we apply to direct supply costs of our contracts and we are afraid of being accused of charging the government for the “$500 toilet seat” that was such a scandal a few years ago. Are we paranoid?

A. Not really, especially in this age of the internet and cable where people are looking for “juicy” news items all the time. Yes, there is always a risk of some journalist (or even auditor) cherry picking an item or several items you are describing and then publicizing how you are gouging the government. Most such assertions fail to understand the nature of direct and indirect cost allocations where the result of such legitimate cost allocation practices can result in an item costing more than the “intrinsic” value of the items. You probably need to make a judgment of risking such adverse publicity and if you decide the risk is too high you may agree, for example, to charge the government contract a “commercial” price and assuming the amount is immaterial, not worry about deducting the costs from your indirect cost base.

Q. Our company is a service disabled, veteran owned small business. My husband is the veteran and has recently died. How will his untimely death affect the status of our business. I am worried about the financial distress a change may entail.

A. Current law treats the surviving spouse as the owner for purposes of maintaining veteran owned status. The spouse has one year to transition the business out of the SDVOSB status if the veteran was rated less than 100 percent disabled or died of a non-service connected injury. In addition, a business immediately loses its SDVOSB status upon the death of its owner for purposes of contracts with any agencies other than the Veterans Administration. However, a recent legislative proposal, stating there are 500,000 SDVOSBs in the US, would allow all agencies to keep the SDVOSB status after the death of its owner where it would treat the surviving spouse as the owner for 10 years if the deceased had a 100 percent service-connected disability or died as a result of a service-connected disability. If the deceased had a less than 100 percent disability or did not die of the liability then the surviving wife will be the owner for three years.”

Q. As a government contractor, we follow the applicable travel regulations for airfare, per diem/ lodging limits, etc. Do consultants and professional service providers we hire also have to follow those limitations or do normal commercial “reasonable travel expenses” practices apply? Does it matter if they are charging directly to a contract or to overhead/G & A?

A. I have looked at the DCAA guidance and don’t see any explicit reference to consultants. The criteria is always “reasonableness” where many auditors will opt to apply the FTR rates while others will be more flexible. To be safe, try to have your consultants stay within FTR rates. That is what we do for our clients and if our expenses exceed the FTR rates, we simply don’t charge them.

Q. We have a “captive” insurance company where we pay insurance premiums. We are not CAS covered so what does the FAR allow.

A. This is one of the many areas that the FAR alludes to CAS as the proper treatment of costs. The situation you describe seems to meet the definition of self insurance where FAR 31.205-19 requires the costs conform to CAS 416. To be very brief, CAS 416 requires you to compute an average loss rate and to use that plus other administration costs rather than the actual premium you pay the captive insurance company.

Q. We have a firm fixed price production subcontract. We are using some ‘Commercial Items’ produced by us. What are the FAR rules about applying G&A and/or profits on the commercial items? For example, the commercial catalog item sells for $1,000, which includes our OH, G&A as well as profit. We charge the full amount to direct material, making it part of the total manufacturing cost. Then we add G&A as well as profit to that pool. Seems like double-dipping on both G&A
and profit. How are we supposed to handle a situation like this? Do we need to exclude one or both (G&A and profit) and at what level would we do so?

A. As you probably know, the FAR basically says you are eligible to apply G&A and overhead (profit depends on what you negotiate or if the FAR allows it) to all costs that are included in the respective bases. So, it depends on what costs associated with the commercial item are included in the base. Is it the raw material and raw labor of producing the item - then you would apply OH and G&A only if you were proposing the raw labor and material costs associated with the commercial item. If the material costs of your base included the entire commercial price of the item, then yes you would be entitled to G&A just as if it was an item you purchased at a commercial price from either a vendor or an affiliated segment of your company. However, if only the raw material and labor costs of the commercial item are included in the base, then I would say you are not entitled to OH, G&A (and presumably profit) on the entire commercial price because some elements of that price are not really “costs” that are included in the G&A base.

Q. We are a contractor holding current government CPFF and FFP contracts. We receive approval for our provisional rates each year for that particular year. How do we go about obtaining a FPRA (Forward Pricing Rate Agreement) and what are the requirements/benefits/drawbacks of doing so?

A. These days it’s difficult to receive a FPRA. You can either ask the ACO to approve one and then submit it to have DCAA audit it but its unusual except for the majors. The requirements are usually a request by the ACO/CO to establish FPRAs or if it is common practice for a contractor to obtain one then you can simply submit a FPRA proposal.

The purpose is primarily one of convenience to establish one set of rates to use for an entire year rather than prepare new ones or audit new ones. The benefit is the one set of rates that can be used on all proposals rather than propose new ones for each major proposal. The drawback is it means less flexibility to propose different rates during the year.

Q. We have a CPFF contract where we have overrun our indirect costs by $257k relative to funding but not the contract ceiling. We have taken $25k of fee on the job which is less than the funded fee. Are we allowed to bill our indirect overrun amount and keep the fee at the contractual percentage or should the cost overrun come out of fee?

A. You should be able to bill the indirect overrun and keep the fee at the contractual percentage. After all, a CPFF contract should entitle you to actual costs, both direct and indirect, not what you originally estimated. As I’m sure you know, the government may not be crazy about reimbursing for an overrun of indirect costs despite the fact you are entitled to it. Make sure you provide the 75% notification so they don’t have that as an excuse not to pay.

Q. I have always pro-rated my hotel taxes and after reading your GCA Report Vol 19, No. 3 I started discussing this with my customer. In order to justify submitting my taxes I did a little on-line research and found that the taxes paid needed to be prorated to the allowable and unallowable portion of my travel costs so I could not be reimbursed the full amount of taxes paid.

A. Thanks for your observation.