NEW DEVELOPMENTS

New Contract-Related Interest Rate Set for Second Half of 2015

The Treasury Secretary has set a rate of 2.375% for the period July through December 2015. The new rate is an increase from the 2.125% rate applicable to the first six months of 2015. The Secretary of the Treasury semiannually establishes an interest rate that is then applied for several government contract-related purposes. Among other things, the rates apply to (1) what a contractor must pay the government under the “Interest” clause at FAR 52.232-17 and (2) what the government must pay a contractor on either a claim decided in its favor under the Contract Disputes Act or payment delays under the Prompt Payment Act. The rate also applies to cost of money calculations under Cost Accounting Standards 414 and 417 as well as FAR 31.205-10 and when a discount factor is used to calculate the present value of future payments (e.g. deferred compensation).

Sick Leave Executive Order Passes

Under Executive Order 13706 a new contract clause applicable to new contracts issued after Jan 2017 and flowed down to subcontractors will require contractor employees earn at least one hour of paid sick leave for every 30 hours worked which is about 8 hours per year. Other features of the EO, intended to ensure government contractors benefits are in line with federal employees, are (1) contractors may not limit accrued paid sick leave to less than 56 hours per year (2) accrued sick leave can be carried over from year to year (3) sick leave will be reinstated for employees that leave and are rehired within 12 months and (4) sick leave may be used for a variety of circumstances including physical or mental illness or treatment, medical testing and preventative care, care of a child, spouse, domestic partner or other close relative and matters related to domestic violence, sexual assault or stalking.

Industry analysts are also beginning to criticize the new EO on sick leave asserting it will drive up the cost of federal contracts. Some critics assert the president is “exceeding his authority” by imposing another fringe benefit on top of existing vacation and other “prevailing” fringe benefits already required by the Service Contract and Davis Bacon acts. Though the new EO is expected to affect over 300,000 government contractor employees some critics have stated that for companies that already pay sick leave or are covered by union contracts the EO is “no big deal.”

Contracting Trends and Large Opportunities

Bloomberg Government analysts have identified five trends they believe will define government contracting in 2016.

1. Budget caps established in the 2011 Budget Control Act will limit discretionary spending to a growth rate of 1.7 percent through 2021. Without this cap, spending would have started out $150 billion higher in 2014 and risen faster at 2.1 percent.

2. Agencies will transform acquisition strategies which will mean 2016 will be a year of heartbreak for incumbents who will face major shifts in the way the government buys goods and services. Gone are the days of straight out recompletes where agencies just dusted off the last request for proposal and changed a few words. Agencies are expected to engage in some contradictory practices where they will break up single award contracts into task orders on multiple-award contracts (MACs) while recompeting other task orders as single award deals. They will slice and dice big system integration programs into small RFPs while consolidating other requirements into single contracts. Incumbent win rates are likely to remain lower.

3. Small business set-asides will boom. The unprecedented increase in set-asides started in 2014 will continue. Small business multiple award contracts, especially for technology services and knowledge-based services, worth billions of dollars in prime contract awards will shift to small businesses, probably squeezing out mid-sized companies.

4. Contractors will divest, merge and restructure. Mid-sized and large companies will have to economize to protect profit margins in the face of declining revenue and margin-squeezing initiatives such as strategic sourcing,
aggressive small business utilization and strategies to use lowest price, technically acceptable (LPTA) bidding. We are already starting to see diversified prime contractors separating lower margin technical services units from higher margin units working on weapons systems (e.g., L-3) and large and mid-sized companies are expected to merge and restructure their internal segments to reduce costs.

5. No major acquisition reforms will pass. Though there will likely be some tinkering with the rules to increase small business and women-owned firm contracts and likely some procurement regulations like rules on commercial item designation there will be no big changes which are years away.

Another trend is the share of Defense Department spending devoted to services as opposed to manufacturing has reached its highest point in a decade and is expected to increase. In fiscal 2014, DOD’s share of prime contract dollars devoted to services was 55.7 percent, 11 percentage points more than it spent on manufactured items such as ships, planes and vehicles. The services’ share exceeds the 53 percent in 2013 and the 52 percent in 2012. Budget pressures and changes in strategy appear to be shifting spending away from big ticket items toward maintenance of existing capital equipment, health care, cybersecurity, communication and surveillance. Spending on a handful of categories such as IT and Ships and Marine Equipment are the exceptions.

Despite budget cuts, the federal government is expected to award more than $180 billion in information technology services MACs over the next two years according to a recent Bloomberg Government August 13 webinar. Over 60% of federal IT services MACs and small business set-asides are expected to grow. Examples of such opportunities are:

Encore ll. Encore ll, which is a recomplete of Encore ll, is shaping up as a cutthroat competition for $1.2 billion a year in cybersecurity, cloud and other defense IT orders. A RFP is scheduled for November with contracts expected to be awarded in October 2016. The Defense Information Systems Agency (DISA) is planning to select 40 lowest bidders deemed technically acceptable for the 10 year MACs where 20 will be reserved for small businesses and 20 will be through full and open competition. The lowest price technically accepted (LPTA) approach is intended to give low price competitors who do not currently work for DISA a chance to oust more expensive incumbents. For those interested in obtaining market intelligence, DISA does not publish labor rates used on Encore ll but the GSA has published the rates used on Alliant which is similar to Encore.

OASIS On-Ramps are coming. If you did not bid on an OASIS (One Acquisition Solution for Integrated Services) contract the first time around in 2014 you may have an opportunity to do so soon. A growing number of agencies such as Homeland Security, the Army and Air Force have committed to acquiring professional services through OASIS and more are expected soon. OASIS allows on-ramps at any time.

Alliant 2. The General services Administration announced Sept. 14 plans to issue a second round of RFPs for Alliant 2 and Alliant 2 Small Businesses. The GSA will handle more than $3 billion a year in IT service orders where it is expected to pick 40 large companies and 80 small ones under Alliant 2. To help winnow the field the GSA is proposing to give extra points to bidders matching three criteria: (1) companies with IT project experience across multiple agencies (2) a project was performed under a task order issued through a MAC rather than a single contract and (3) bigger projects will get more points than smaller ones. Also, only joint ventures with prior experience will probably win a contract discouraging companies from forming a new joint venture using the experience of individual venture companies which is intended to open up bidding to more mid-tier and small companies lacking the breadth of experience required to win Alliant 2 contracts.

Industry Criticizing Proposed Commercial Item Rule

As we have been reporting, the government has been taking steps to lessen the amount of acquisitions classified as commercial items. One example we reported on in the last REPORT was the Defense Department is proposing to expand the authority to require submission of more non-certified cost data for commercial items. If the proposal is passed, it would eliminate the opportunity to demonstrate price reasonableness for commercial items sold only, or predominantly, to the government, such as the GSA schedule contracts or for “of a type” commercial items. The proposal sets standards for determining whether sales data for the same or similar items is sufficient for evaluating price reasonableness and how much uncertified cost data is required when price information is not adequate for evaluating price reasonableness. The proposal also states the CO will not limit the government’s ability to obtain any data that may be necessary to support a determination that the price is fair and reasonable opening up the possibility of basing price on cost build ups for most commercial items.

The Council of Defense and Space Industry Associations (CODSIA) has stated in a comment letter
that the proposed guidelines are “irrevocably flawed” and should be withdrawn. It stated the proposed rule offers no consistent or objective standards and offers instead “highly subjective principles” based on what a “prudent person” would consider sales data or amount of cost data. It also prohibits contracting officers from limiting the circumstances when cost or pricing data is sought, implying that such data is fair game in every circumstance. Even Sen. John McCain has publicly criticized the proposal saying it would “undermine the commercial item exemptions in existing law.”

White Paper on IR&D Costs Generating Concern

A recent White Paper issued by the Defense Department that we reported on in the last issue of the REPORT is generating considerable concern that the “I” in independent research and development (IR&D) is being undermined and that the government will be limiting reimbursement of such costs. The paper proposes that starting in FY 2017 every new IR&D project will be preceded by a meeting with DOD technical or operational staff to outline goals and plans and that DOD will share results with the DOD upon completion of the project. Many commentators are stating the new policy is part of a continuing trend since the 60s for Congress to place spending limits on IR&D where, for example, NIH disallows all IR&D costs reasoning if they want research they will put it under a contract. It is feared that DCAA will use the adequacy of the documentation of discussions with DOD to determine whether IR&D costs are allowable, resulting in the costs being questioned on the “flimsiest pretext.” (The White Paper is available at http://www.defenseinnovationmarketplace.mil/resources/USD%28ATL%29_RD_White_Paper.)

DCAA Issues Its 2016 Staffing and Program Plan

In August DCAA issued its annual audit program plan for 2016 (beginning Oct 1, 2015). Its 4,969 staff years does not differ much from 2015 and there are few changes in audit priorities. Stated audit priorities in descending order are:

- Demand work including audits of bid proposals and forward pricing rates, though DMCA is getting more involved in reviews of forward pricing rates
- Indirect cost rate proposal (ICP) audits where the goal is to complete all 2010 and a portion of 2011-2012 ICPs. DCAA is being funded to audit ICPs from NASA and DOE contractors so those may be high priority. For ICPs from 2008 and earlier, DCAA will assess audit plans against the six year statute of limitations.
  - Business systems. Of the six business systems the government audits, DCAA is responsible for three – Accounting, Estimating and MMAS (Material Management Accounting System). For 2016, DCAA is estimating 5,000 and 4,000 hours each for Estimating and MMAS audits but interestingly, is not budgeting for accounting system audits despite that being the one area DCAA usually focuses on.
  - Post award (Defective Pricing) audits. DCAA has identified 27 audits to 16 contractor business segments where its planned per audit hours has been increased to 1,250 hours from 250 hours.
  - Real time audits. These include floorchecks, physical observation and verification of direct material and post-payment testing of paid vouchers. For major contractors (over $100 million of flexibly priced contracts) quarterly audits will be conducted (15-OWD-25(R)).

DCAA Issues Guidance Auditing Incurred Cost Proposals

In addition to the 54 page guidance we summarized in the 2Q15 issue of the GCA DIGEST, DCAA has issued a 9 page guideline “Revised Checklist for Determining Adequacy of Contractor Incurred Cost Proposal.” The revision is intended to provide a clearer document to determine whether a contractor’s ICP is adequate to begin a review and to determine whether to accept or decline the audit engagement.

Industry is Asking Obama to Stop Targeting Contractors

Four industry groups and the American Bar Association’s Section of Public Law are asking the White House to stop issuing executive orders targeting contractors. Despite being “well intentioned” the EOs are requiring “substantial investments in time and systems though their actual impact is exceedingly minimal” where the 16 regulations are “raising a substantial barrier between commercial and government marketplaces.” One order that has raised particular concern is EO 13,673, Fair Pay and Safe Workplaces that requires businesses to disclose violations of 14 federal labor and employment laws (e.g. employment discrimination laws, Fair Labor Standards Act, The National Labor Relations Act, the Davis Bacon Act and the Family and Medical Leaves Act) for the
previous three years in order to be eligible to compete for a government contract worth more than $500,000.

**Agencies are Not Seeking Price Discounts on FSS and Not Assessing Prices**

A recent GAO report concludes that contracting officers are not seeking discounts or assessing pricing, as required, when ordering goods and services from the General Services Administration's Federal Supply Schedules. It reviewed 60 FSS orders from three agencies making the most FSS purchases and concluded that of the 75 percent of competitive purchases, 51 percent received only one or two quotes where the FAR requires three. Of the 25 percent of non-competitive quotes, almost half cited only one available source as the exception to using competitive procedures. For 16 out of 45 acquisitions above the simplified acquisition threshold, COs did not seek discounts as the FAR requires. When COs did seek discounts 21 of 26 instances resulted in vendors offering discounts from 2 percent up to 57 percent.

Another report stated that last year federal agencies awarded $54.5 billion through contracts for which multiple bids were sought but only one offeror submitted a bid, representing 12 percent of the $440.8 billion in prime contracts awarded. Contracting officers are now under pressure to cut such “competitive one-bid” contracts and ensure at least two bids for all competitive acquisitions are received.

**OFCCP Finalizes Pay Transparency Rule**

The Labor Department released a final rule prohibiting federal contractors and subcontractors from maintaining pay secrecy policies and discriminating against employees and job applicants who discuss, disclose or inquire about compensation. The rules implements the president's Executive Order 13665 issued in April 2014 where the changes will be incorporated into the mandatory equal opportunity clauses currently in government contracts. The rule also requires contractors to include similar provisions in employee manuals or handbooks that are disseminated to employees or applicants. The rationale of the change is intended to help combat pay discrimination in the workplace but several commentators have expressed doubt the new rule will actually have much of an impact (Fed. Reg. Sept 11, 2015).

**Inadequate Business Systems Penalties Are Being Implemented; DOD IG States COs Are Not Aggressive Enough**

The Pentagon is holding back millions of dollars over flaws in contractors' everyday business systems. United Technologies Corp. tops the most recent target list of 15 companies whose payment are being withheld for inadequate systems to manage subcontractor purchases, estimate costs or keep track of schedules. The Defense Contract Management Agency is holding back $180 million in billings or as much as 5 percent from two of the company’s two military units. Other companies such as units of Northrup Grumman, General Electric, General Atomics and Boeing are also seeing similar withholdings. The withholds are a result of Pentagon enforcement of a three year old regulation calling for contractor compliance of six internal systems (e.g. accounting, estimating, purchasing, earned value management and material management accounting) the government says are necessary to measure a company's progress in meeting its cost and schedule goals for weapons contracts.

Despite expansion of withholdings, the DOD Inspector General Office issued a report saying Defense Contract Management Agency’s (DCMA) contracting officers are not complying with one or more requirements involving reported business system deficiencies. The IG selected a random sample of DCAA’s business system deficiency reports where auditors issued a “deficiency report” intended to alert the DCMA CO such as failure to ensure material and labor costs were charged to appropriate contracts, notify the government of cost accounting changes within 60 days, perform adequate or periodic review of its accounting system and indirect cost rate structure or comply with labor categories specified in the contract. The IG report said DCMA's COs did not comply with one or more of the DFARS requirements where COs failed to take appropriate or timely corrective action to address the reported business system deficiency, did not issue initial determinations to determine if significant deficiencies existed and did not follow up on overdue or incomplete responses to evaluate contractor responses. The IG recommended that DCMA review the sampled cases and ensure COs take appropriate action on the reported deficiencies, require a board of review when a CO determines a deficiency is not significant and consider remedial actions for COs not complying with the DFARS.

**Panel Describes Ways for Subcontractors to Obtain More Business with Primes**

A National Defense Industrial Association’s National Small Business Conference Sept 24 outlined some simple steps small businesses should take to optimize their opportunities to obtain work from prime contractors on federal contracts. Some steps subcontractors should take include:
1. Synchronizing their computer systems with primes to make sure they are not blocked by prime contractors’ cybersecurity measures. For example, emails from small firms are often deleted or marked as cyber attacks when many prime contractors automatically delete e-mail addresses with Yahoo or Gmail domain names. The panelists recommend small firms should use their own domain name instead.

2. Update company information. Some companies like SAIC have an internal system where companies can register their profile information while others companies like General Dynamics check the dates that companies updated their information stating “I want to look for those who took the time to update.”

3. Update their System for Award Management (SAM) and Dun & Bradstreet profiles at least once a year. Companies like Northrup Grumman like to use the profiles to check on the accuracy of information such as North American Industry Classification System codes and company sizes.

4. Strictly ensure codes of ethics are maintained. BAE stated unethical conduct is “bad for business” where L-3 stated “if one of our teammates does something that’s not ethical, it can affect the entire team.”

SBA Proposes to Change Its Criteria for Meeting Subcontract Goals

The Small Business Administration is proposing to revise its small business regulations to allow non-small prime contractors to receive credit for meeting its subcontracting goals with subcontract awards at any tier. Currently, non-small prime contractors must establish small business subcontract goals at their first tier level and receive credit toward meeting their goals at only the first tier. Under the proposed rule, the prime contractor incorporates lower tier subcontractor performance into its subcontractor plan goals. The proposed rule would require related subcontract plans of all subcontractors that must maintain subcontracting plans. Also, the rule would clarify that the size standards for a particular subcontract must appear in the solicitation for the subcontract.

Proposed Counterfeit Rule Will Cover All DOD Contracts

A Sept. 21 proposed rule will make DOD contractors responsible for detecting counterfeit electronic parts. The rule excludes “embedded software” from the definition of counterfeit electronic parts but expands the existing rule to include acquisitions below the simplified acquisition threshold and those for commercial off-the-shelf items. Some commentators express the new rule is “incredibly broad” where companies without a past history of addressing counterfeit electronic parts will find compliance to be “very cumbersome.” Loser companies will be those who have acquired the cheapest parts without regard to a clear chain of custody while winners will be those companies that have already taken steps to discipline their procurement system to provide components that meet these requirements (Fed. Reg. Sept. 21, 2015).

CASES/DECISIONS

Probable Costs Was Not Determinable

The Army issued a RFP for support services where Viatech’s proposal included “undeterminable probable costs” because its proposal reserved the right to vary its labor mix and affiliates employed to perform on the contract. The GAO sustained the award to its competitor saying there were differences between Viatech and its affiliates regarding overhead and general and administrative rates and therefore Viatech’s approach of using affiliates’ labor raised the possibility its incurred costs would be much higher than proposed (Viatech Inc., GAO, B-411368).

Agency’s Evaluation Was Unreasonable

(Editors Note. The following case suggests several bases to lodge successful award protests.)

The Defense Department issued an RFP for proposal set asides for small businesses offering support staff. DOD received many proposals where the agency made an award to IGH and several of the offerors filed protests asserting the technical and past performance evaluations were flawed. Examples of technical flaws that the GAO found included (1) a significant weakness for not submitting a quality control plan was rejected where protester referenced a sample quality assurance plan it said was typical of its own plan, the RFP did not require submission of a plan but only asked for a description of its approach which was adequately provided (2) while Metis was assigned a weakness for failing to include a definitive list of reports and deliverables IGH also omitted the list but was not assigned a weakness (3) there were unexplained discrepancies between the technical evaluation board (TEB) and the source evaluation board (SSEB) describing evaluation results in materially different terms without explanations (e.g. TEB assigned IGH 8 strengths and one weakness for an acceptable rating while the SSEB
showed 7 strengths and no weakness) and (3) the SSEB rated IGH's proposal outstanding with no explanation for the differences. As for past performance evaluation the protesters challenged IGH's “satisfactory” rating which was assigned to all others but IGH's past performance was not relevant while the protestors provided examples of their past performance being more relevant to the tasks for the new contract (e.g. closer dollar value) (Metis Sltns, B 411173).

When 90 Day Appeal Clock Begins is Confusing

The Civilian Appeals Board ruled that when two or more copies of a contracting officer’s final decision is sent to a contractor it has 90 days to appeal that decision from the first time it received the decision (DekaTron Corp., V Dept of Labor, CBCA 4444). However, another Appeals Board applies a completely different rule stating that when multiple copies of a CO’s final decision is received where there is no indication which copy begins the 90 clock, the contractor is entitled to compute the date from the receipt of the last copy (TTF, ASBCA No. 59511).

Cost and Pricing Data Was Meaningfully Disclosed

Symetrics submitted a proposal based on rates contained in its forward pricing rate proposal (FPRP) and later submitted a revised proposal for a fixed price letter contract which used higher overhead and G&A rates that were reflected in a revised FPRP. The contract specialist who negotiated the contract price believed the revised proposal was based on its original FPRP and relied on what they understood to be the FPRP proposed rates. DCAA also audited the proposal relying on the same knowledge and understanding. The government asserted the contract was defectively priced arguing it was paying for “excess costs.” The government said Symetrics failed to comply with FAR 31.407-3(a) that required it to “identify the latest cost pricing data already submitted in accordance with its FPR agreement” in its specific pricing proposal. The board noted the FAR section did not address FPRPs but rather FPRAs and hence did not govern Truth in Negotiation Act disclosures. The Board stated a proper disclosure is not confined to a formal written submission but is fulfilled if the government obtains the data in question in some other manner or had knowledge. Because the people who evaluated the price proposal were all aware of the FPRP and expressly stated they relied on it for rate information the Board ruled the FPRP rates at issue were meaningfully disclosed to the government (Symetrics Inds., ASBCA 59297).

QUESTIONS AND ANSWERS

(EDITOR’S NOTE. DUE TO THE HIGH VOLUME OF QUESTIONS WE HAVE RECEIVED LATELY WE WILL OMIT OUR NORMAL FEATURE ARTICLE TO CATCH UP ON OUR QUESTIONS.)

**Q.** We have spent considerable expenses arranging for various short term borrowing to finance our working capital. Are they unallowable financing costs?

**A.** Unallowable financing costs are generally associated with financing that affects the capital structure of the company such as stock transactions and long-term borrowing. In our opinion, these costs should be distinguished from costs of setting up or administering short term financing (e.g. lawyers, brokers, accountants, consultants, in-house time, bank charges). Despite the differences, it is not unusual for DCAA to question these short term debt costs, where they assert they are “financing” costs and hence unallowable according to FAR 31.205-20. When asked to respond to DCAA’s findings we have been successful by alluding to the DCAA Manual, “Bank Fees” in Section 7-2110 which states “administrative costs associated with short-term borrowings for working capital may be classified as ‘bank fees’. These administrative costs are allowable under FAR 31.205-27, Organization costs.”

**Q.** We mistakenly ordered too much material on a cost-type contract. We cannot return it nor can we use it on our other work. Will the cost of the excess material be considered unallowable?

**A.** As a general rule, mistakes or omissions by a contractor’s employees, even if negligent, are not disallowed unless the mistake is a result of “willful misconduct” or “bad faith”. The “nobody is perfect” observation recognizes that it is a fact of life that even careful employees sometimes are negligent and make mistakes. Professor Cibinic in a Nash and Cibinic Report observed the Armed Services Board of Contract Appeals has ruled that proof of negligence does not prove “willful misconduct” or “bad faith” but requires an employee to be “recreant” to their duty, deliberately refuse plain well understood obligations or “demonstrate a conscious failure to use necessary means to avoid peril” (Morton Thiokol Inc., ASBCA 32629).

**Q.** We are considering charging otherwise allowable legal expenses associated with our commercial work to our G&A pool which allocates costs to both commercial and
government work. If we do that and the government decides to question the legal costs are we subject to penalties. The answer will determine if we take a chance.

A. I would say no. Penalties are assessed on “expressly unallowable costs” which are those specified in FAR 31.205, other agency supplements, or violate terms of the contract or other regulations. The legal costs you describe are not one of the activities identified in the FAR as unallowable so if auditors choose to question your claimed legal costs they would be doing so because they believe the costs are not allocable to government contracts (we would disagree with this assertion but that’s another story). Though the government may question costs because they are not considered allocable to government contracts, the penalty provisions of the FAR do not provide for a penalty for non allocable costs. For example, the cost accounting standards address allocation, as opposed to allowability issues, where disallowed costs in accordance with CAS would not be subject to penalties since the CAS is not one of the regulations addressed in the FAR provisions.

Q. (Editor Note. Here is an oldie but goodie response because the inquiry below is recent.) We spent over $250,000 creating sales material about our products and services and were recently informed by government auditors that these are unallowable contract costs. Are they right?

A. Maybe yes, maybe no. Presumably, the auditors have concluded the material is unallowable publications such as “brochures” and hence are unallowable in accordance with FAR 31.205-1(f)(5), Public Relations and Advertising costs and explicitly unallowable (subject to penalties) when “designed to call favorable attention to the contractor and its activities.” DCAA does provide guidance to its auditors that publications are unallowable when they are for (a) selling, marketing and advertising with little or no technical content that is distributed to current or potential customers (b) capability promotional items that stress superior capabilities or advertise achievements with little to no technical content and (c) material that does not contribute to contract performance but merely serves to enhance a contractor’s reputation.

However, both the FAR and some court cases provide numerous examples of brochure-like materials that are allowable. So, for example, material used for training and education (FAR 31.205-44), trade, business, technical and professional activity (31.205-43(e), labor relations (31.205-21) or employee morale, health and welfare (31.205-13(a) are considered allowable. In Aerojet-General Corp (ASBCA No.13372), the Board ruled several types of advertising costs were allowable such as a company brochure prepared in response to business inquiries that replied to factual questions about the company and was distributed to interested parties and a monthly magazine circulated outside of the company containing semi-technical summaries of the company’s technology development, government programs and changes in personnel. So, though some material may fall under the category of unallowable public relations others may be less clear and fall under other allowable cost categories. We recommend companies properly distinguish, in writing, between unallowable costs for advertising and public relations and such allowable costs as information dissemination (technical and non-technical) and technical sales tools.

Q. We have a subcontractor who wants to charge us $50 per hour for his labor and add his overhead and G&A rate. The hitch is $25 of that amount represents an equipment amount that he has rolled into his direct labor charge. Do you see problems here?

A. Yes. The equipment amount does not represent “direct labor” and any reasonable definition of “labor” would not include such an amount. Accordingly, it would not appear to qualify as an element of your overhead base (e.g. direct labor) nor would an overhead charge be justified. I don’t see any problem in establishing an hourly rate for the equipment (you’ll need to negotiate that and document it in the contract) but you would need to consider it an other direct cost where only G&A would apply.

Q. We have been developing a software package over the last couple years which can be used by our military customers. This software has not been developed due to specific contract requirements nor funded by any customer. How can we charge a software licensing fee to the government for new contracts once we have a finished product? As you know, when the government evaluates proposals, they evaluate cost data and there is no specific cost data other than the media related to a software license. We will be selling this software to customers other than the US Government as well and it is easy to include the license fee in those contracts because they do not evaluate current cost.

A. One question that will arise is whether you have been charging the government for development of the software as IR&D costs, usually included in your G&A rate over the years. As for being able to charge the government a license fee, there is no prohibition for such a fee so you will need to negotiate it separately as part of your specific contract. You are right about often needing to show the price for the fee is based on a


cost build-up but there is no prohibition against using a
different method for arriving at a price for the software
license. You will go far if you can show a similar fee
charged to commercial clients. Otherwise, you will need
to help the government demonstrate the fee they are
paying is “fair and reasonable.”

Q. I have read your articles on recent DCAA guidance
indicating there will be less audits of incurred cost
proposals (ICPs). Should I be dancing in the street?

A. Not yet. We are seeing a significant increase in
DCAA audits of provisional billing rates in lieu of the
ICP audits.

Q. We are a small company and intend to have a
substantial amount of our business in the government
sector. What accounting software should we consider
using?

A. A recent Redstone blog we saw correctly identified
three software packages commonly used by government
contractors.

1. Quickbooks. You will want to make sure the package
you use has the job cost module along with the general
ledger one (Premier Desktop is quite common). You will
need to use another vendor’s timekeeping and expense
reporting products if you want electronic reporting
where there are several good ones such as SpringAhead,
eFAACT and Unanet.

2. Unanet has long had timekeeping and expense
reporting systems that are excellent and well received by
auditors we have worked with. Unanet has expanded
their offerings to government contractors by creating
Version 10 that now includes the functions of most
financial accounting software (e.g. G/L, AP, AR,
budgeting). We do not have much information about a
job cost capability.

3. Deltek Costpoint. Deltek has long been the gold
standard for government contractors, providing all the
functionality that contractors need (e.g. financial, job
costs, time/expense, indirect rate computations, etc.)
Though they have traditionally targeted mid-sized and
large contractors they have developed a new package
oriented to small contractors (less than 150 employees.)
(In full disclosure, we have consulted for one of Deltek’s
affiliates to ensure their software features would comply
with DCAA requirements.).

Be aware, that other traditional accounting software
companies’ allow for modifications of their software to
customize features for government accounting.

Q. Many hotels charge the federal travel regulation
maximum lodging rates and then add on various taxes.
If the taxes result in excess over the maximum FTR
allowable rates are they unallowable.

A. There are two ways to be able to recover the taxes.
Taxes are now considered to be “miscellaneous” costs,
not to be included in per diem amounts. Also, the
Federal travel Regulations in Section 301-11.30 allows
reimbursement of actual expenses up to 300 percent of
the maximum per diem rate allowance so unless your
agency has some prohibition against it you should be
able to recover the taxes one way or the other.