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# GCA REPORT

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## NEW DEVELOPMENTS

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### **DOD Bill Curtails Outsourcing Efforts**

The \$416.2 billion fiscal 2005 defense appropriations measure overwhelmingly passed by the House and Senate and signed by the President includes a controversial provision that will curb competitive sourcing. The provision, which is supported by federal employee unions and strongly opposed by industry groups, would eliminate use of streamlined procedures recently incorporated in the revised Office of Management and Budget Circular A-76 that provides the ground rules for public-private competitions. Streamlined competition is a shortcut procedure for contracting out commercial type activities involving 11 though 65 full time equivalent (FTE) positions without a most efficient organization (MEO). The MEO is the in-house personnel's opportunity to revamp its staffing and operations to be more competitive and without an MEO the in-house personnel is forced to pit its status quo against the best offers of the private sector.

The appropriations bill will require that public-private competitions for functions performed by more than 10 federal employees include an MEO and the private sector offeror must beat the MEO cost by the lesser of 10 percent or \$10 million (currently, the so-called minimum cost differential applies only to competitions involving more than 65 FTEs). Further, contractors should "not receive an advantage for a proposal that would reduce costs" by either (1) not making an employer-sponsored health insurance plan available or (2) offering an employer-sponsored health benefits plan that requires employers to contribute less toward the premium or subscription share than the amount DOD provides its civilian employees.

### **Industry Weighs in on T&M Withhold Changes**

Numerous industry groups have issued favorable comments on the recent proposal to remove the requirement under FAR 52.232-7 that a contractor withhold five percent (up to a maximum of \$50,000) of payments due under a time-and-materials or labor-

hour contract. The proposed rule permits COs to use their judgment regarding whether to withhold payments so the withhold will be applied only when necessary to protect the government's interest. The DOD's Office of Inspector General requested the rule should clarify whether the \$50,000 withhold ceiling should apply per task order or for the entire contract, recommending it apply per task order.

In a separate action related to T&M and labor-hour contracts, the FAR Council September 20<sup>th</sup> has issued a proposed rule to expressly authorize the use of T&M and LH contracts for procurement of commercial services (Fed. Reg. 56315).

### **DCAA Eliminates Z-Score Data Requirement**

In the light of recent corporate scandals, DCAA is now required to conduct either a detailed or cursory financial risk assessment of government contractors and as we reported in the first quarter 2004 edition of the GCA DIGEST, DCAA is required to gather financial data to make their determinations. An August 26 memo to its auditors has eliminated the Z-Score and two cash flow ratios – Cash Flow Return on Assets and Cash Flow Adequacy from the required data accumulation. The Z-Score bankruptcy prediction model was eliminated because (1) it provided little additional assurance over the key ratio analyses performed (2) results were often misinterpreted or misunderstood by government contract personnel (3) the model was somewhat dated because it did not adequately address more current business practices such as just-in-time inventory and (4) use of the model required additional auditor documentation and working paper explanations that added little value to the financial condition assessment. The two cash flow ratios were eliminated because they essentially duplicated the results of other calculated ratios (94-PPD-048(R)).

### **SBA Finalizing Rule to Ensure Primes Take Their Subcontracting Plans Seriously**

The Small Business Administration is readying a new final rule intended to make sure prime contractors take their subcontracting plans seriously by authorizing – but not requiring – contracting officers to use goals in

primes' subcontracting plans or their past performance in meeting these goals as source selection factors in placing orders with the government. The current rules require that large businesses awarded a federal prime contract in excess of \$500,000 - \$1 million for construction contracts – submit a subcontracting plan to the contracting agency. The rules require that the subcontracting plan include both dollar and percentage goals that reflect the “maximum practicable” utilization of small businesses as subcontractors or suppliers and that a prime contractor who fails to make a good-faith effort to achieve their subcontracting goals are subject to assertion of material breach of contract and can be terminated for default or assessed liquidated damages. However, the small business community does not see the current scheme as effective as it could be because the goals are difficult to enforce so the incentive of having the subcontract plans be the basis for source selection should encourage primes to take their subcontracting plans seriously.

The proposed rule also contains procedures for conducting on-site compliance reviews and follow up reviews to see how well the prime contractors follow through on their plans. The rule would also increase, from \$10,000 to \$100,000, the dollar threshold above which primes must notify unsuccessful offerors – the higher amount is intended to conform to the simplified acquisition threshold.

### **OMB Puts Forth R&D Priorities for FY 2006**

The Office of Management and Budget August 12 updated its guidance on research and development priorities for the 2006 budget. A five page memo for heads of executive agencies identifies six interagency priorities to receive “special focus”: (1) homeland security R&D (2) networking and information technology R&D (3) The National Nanotechnology Initiative (4) discover-oriented physical science priorities (5) biology of complex systems and (6) climate, water and hydrogen R&D.

Under the homeland security categories the guidance says “winning the war on terror and securing the homeland” will be top priorities. Research areas include enhancing prevention, detection and treatment of nuclear, chemical and biological threats; ensure continued state-of-the-art capability to test and evaluate medical countermeasures; biosurveillance network integrating human, animal, plant and environmental surveillance and laboratory networks; shortfalls in development of new drugs and vaccines against foreign animal disease threats; and pursuing social and

behavioral studies to anticipate and counter threats to national security. In addition, agencies should continue to invest in technologies to enable decontamination following biological, chemical and radiological incidents, detection and protection against high explosives, development of secure infrastructures, advanced techniques for threat and vulnerability analyses.

In the networking and IT fields high priority will be given to high-end computing (supercomputing) and cyber-infrastructure R&D due to their potential for greatest progress to a broad range of scientific and technological applications. The guidance says agency plans in high-end computing should be consistent with the report of the High-End Computing Revitalization Task Force. Cyber-infrastructure R&D encompasses research on hardware and software tools aimed at strengthening the connections between new and existing computers, scientific instruments, researchers and facilities.

Agencies are told to produce (1) clear and concise definitions of program activities (2) an inventory of programs in the baseline budget (3) agency tradeoffs that will provide resources to help produce cross-agency programs greater than individual activities and (4) an interagency implementation plan. Agencies must “vigorously” evaluate existing programs and where possible consider them for modification, redirection, reduction or termination in keeping with national priorities. While agencies may propose high priority activities they must identify potential offsets by elimination or reductions in low priority programs. Go to [www.whitehouse.gov/omb/memoranda/index.html](http://www.whitehouse.gov/omb/memoranda/index.html) for a copy of the memo.

### **Nine Senators Express Concern Over Relocation and Education Expense Changes**

Nine democratic senators July 23 wrote the Office of Management and Budget to express concern the proposed changes to the FAR would “unfairly hold federal employees and government contractors to different standards and could result in greatly increased costs to taxpayers.” The proposed lump-sum relocation change, following commercial practices, would allow reimbursement of such expenses on a lump-sum basis rather than the current practice of reimbursing contractors for relocation costs up to actual expenses. The senators site DCAA as saying the lump sum payment represents an “unacceptable risk” on the government and creates an “excessive audit task.” The final rule on training and education expenses would make such costs generally allowable for both contractors and federal employees as opposed to the current

requirement that such costs cannot be reimbursed if their sole purpose is to obtain an academic degree or to qualify for a position that requires a degree. The senators said the result would be to “charge the government for education expenses” that Congress has prohibited for federal employees.

## **DCAA Issues Guidance on Agreed to Audit Procedures**

*(Editor’s Note. For various reasons, DCAA often does not conduct full audits requiring adherence to detailed audit steps but, instead, uses cursory steps following so-called agreed upon procedures (AUP) where not only the scope of effort is different but also the conclusion reflected in the report differs. It’s a good idea to know what requirements auditors are following to know what efforts to expect and what audit conclusions they may reach.)*

DCAA issued guidance on appropriate and inappropriate AUP scope of work and resulting reports. Based upon their internal reviews, DCAA concluded that certain AUP have been based upon inappropriate procedures and reports have included inappropriate conclusions and audit opinions. Examples of inappropriate AUP reviews include “unclear” and “vague” objectives such as evaluating reasonableness of direct or indirect rates, evaluating computer center savings or reviewing marketing costs for allowability, allocability and reasonableness. Examples of inappropriate opinion-like statements include proposed rates appear reasonable, proposal is in non-compliance with CAS 403, accepted contractor’s classification of certain production costs or concurred with their proposal methods.

The guidance stresses that AUP must be mutually agreed to in advance with requesters, be specific, subject to measurable criteria and most importantly, auditors must not express an audit opinion. Not only are audit opinions prohibited but there should also be no opinion on significance or materiality of costs where examples of inappropriate opinions would include we disclosed no significant errors, no material discrepancies between reported or actual costs or actual rates do not indicate significant increases compared to baseline rates.

When auditors are requested to perform an AUP they are told to reach an agreement on specific procedures to be used, reject an agreement that includes procedures that may be overly subjective that allow for varying interpretations or may include opinion-like conclusions. Examples of appropriate AUP might include comparing indirect expense rates in a specific proposal with a specific forward pricing rate agreement or verifying direct rates in a proposal to books and records. The audit report should express the specific procedures taken

and offer no audit opinion or negative assurance and must report all findings with no consideration of materiality unless the agreed-upon instruction provided limitations. Example of appropriate conclusions would be we compared proposed indirect rates to the forward pricing rate agreement and found no exceptions or we verified indirect labor rates to direct labor bid rates and found no exception (04-PSP-033(R)).

## **DOD Guidance Provides for Re-openers and Price Adjustments to Cover UID Compliance Costs**

The Defense Department July 19 issued guidance on the pricing and accounting for costs incurred by contractors to comply with DOD’s recent unique item identification (UID) initiative. The guidance recognizes that compliance with the interim DOD rule issued December 30, 2003 – requirement to provide unique identification for all items above \$5,000 to be delivered to DOD using machine readable data elements (i.e. bar codes) – may be costly for contractors and provides that costs of compliance should be allowable. If such costs cannot be estimated with reasonable accuracy, COs should consider including a reopener clause in new contracts to cover the difference between anticipated and actual costs; on existing contracts, COs should negotiate an equitable adjustment to the contract price for compliance.

The guidance states for the costs to be allowable they should follow cost assignment requirements of the Cost Accounting Standards and FAR 31: (1) tangible capital assets need to be depreciated in accordance with CAS 404/409 and FAR 31.205-11 (2) intangible assets expensed or amortized in accordance with generally accepted accounting principles (3) recurring costs that would have otherwise been incurred that are other than capital assets expensed in the period incurred (4) non-recurring costs that would have otherwise been incurred should be expensed in the period incurred but if not otherwise incurred then the expense should be separately accumulated as a deferred cost and amortized over a period not to exceed five years.

Under Secretary of Defense Michael Wynn September 3 issued a UID policy statement encouraging an “evolutionary approach” for implementing existing items in inventory and operational use. It set a 2007 date to have (1) all existing serialized assets entered into the UID registry and (2) UID marking capabilities established for all existing items and embedded assets so marking can begin. By 2010 all UID marking of items and embedded assets should be completed. The



DOD memo and highlights of the proposed policy are available at <http://www.acq.osd.mil/uid/>.

## **A Proposed FAR Revision Seeks Greater Use of Performance-Based Acquisitions**

The FAR Council is proposing to amend the Federal Acquisition Regulation to broaden the scope of performance-based acquisition (PBA) and give agencies more flexibility in using PBA while reducing the burden of force-fitting contracts into PBA when it is not appropriate. The substantial revisions to FAR Subpart 37.600, which would now be renamed “Performance-Based Service Acquisition (PBSA),” follows guidance made in a working group convened in April 2002 and seeks to implement numerous laws calling for use of PBA to the “maximum extent possible.” The FAR revision states the principle objective of PBSA is to optimize contract performance by expressing government needs in terms of performance objectives or desired outcomes rather than method of performance. The revisions provide that (1) solicitations for PBSA may use either performance work statement or a statement of objectives (2) PBSA contracts must include either a performance work statement (PWS) or measurable performance standards (3) PBSA contracts or orders may include performance incentives to promote contractor achievement which can be of any type such as positive, negative, monetary or non-monetary as long as they correspond to performance standards and (4) quality assurance would be expanded to address the means for assessing contractor accomplishment of outcomes. The Office of Federal Procurement September 7th set a PBSA goal of 40 percent, measured in dollars, of eligible service contracts over \$25,000 in FY 2005.

## **Industry Group Criticizes Proposed Billing Instructions**

An August 27<sup>th</sup> letter to the FAR Council by the Council of Defense and Space Industry Association (CODSIA) opposes certain sections of the June 25<sup>th</sup> proposal to amend the Defense Federal Acquisition Regulation Supplement to improve billing and payment instructions. The comments address the proposed requirement that billing amounts by Contract Line Item Number (CLIN) “best reflect” costs. CODSIA states that all cost type contracts funded by a single appropriation should be excluded from having to separately identify a payment amount for each CLIN since the billing and payment process for contracts containing only one appropriation can be highly automated and would meet statutory requirements. For separately funded CLINS, CODSIA

disputes the assertion that the rule is not expected to have a significant economic impact on substantial numbers of businesses. CODSIA states it will be necessary for contractors to establish new systems and processes for more detailed reporting. Further since “best reflect” has not been defined, the term will lead to “unattainable compliance requirements” arising from inconsistent interpretations by contracting and audit offices.

## **CASES/DECISIONS**

### **EPA Owes Contractor Fees on “Gross Overestimates” in LOE Contract**

The Environmental Protection Agency entered into a one year with five year option level-of-effort (LOE) cost reimbursement contract where the contract said the government “will order 119,000 direct labor hours (dlh)” for the base period. A modification of the contract after the base period changed the language to “the government’s best estimate of level of effort...will be as follows” where the base period and option period listed the 119,000 dlh. The contract also stated if the contractor provided less than 90 percent of the LOE specified an equitable downward adjustment of the fixed fee would be made. In fact, the largest number of dhs ordered in any period was 69,000 and the difference between the total fixed fees in the contract and total fees paid due to the lower dlh was \$1.5 million. Sanford claimed the EPA knew or should have known that its dlh estimates were “grossly inflated” and impossible to achieve and claimed a breach of contract due to the EPA’s failure to (1) order the specified number of hours and (2) renegotiate the fixed fee based on a realistic estimate of the level of effort.

Though the contract is neither a requirements nor indefinite delivery/indefinite quantity contract the Board asserted it is still covered by case law covering these types of contracts where the contract specifies quantities the parties agree to and a grossly overestimated estimate has the effect, intended or not, to entice a contractor to offer lower prices than it otherwise would since greater quantities mean lower unit prices. Whereas boards have held the government ought to be held liable for negligently prepared estimates under requirements and ID/IQ contracts, the same should apply to LOE contracts.

Though the Board ruled Sanford was entitled to damages it did not accept its proposal that it should be

compensated midway between the fee it would have earned if all the estimated hours had been ordered and the lesser fee based on hours actually worked because this would represent “anticipatory profit damages” that *Rumsfeld v. Allied Companies* had prohibited. Rather the proper methodology for computing the damages should be an equitable adjustments in the price of the units delivered (*Sanford Cohen & Associates Inc., IBCA, No. 42329/00*).

### **Court Vetoes Air Force Release of Option, Vendor Prices**

The Air Force wanted to divulge McDonnell Douglas’s (MD) option year prices and vendor pricing under several contract line items to a competitor under the Freedom of Information Act (FOIA) while the contractor asserted such information violated Exemption 4 of FOIA which protects “trade secrets and commercial or financial information obtained from a person and privileged or confidential”. The majority of court judges ruled against the Air Force stating the release of the option year prices in the one year with nine option years contract would likely cause MD substantial competitive harm because it would increase the probability that MD’s competitors would underbid it in the event the Air Force rebids the contract. Further since the release of the CLINs were composed largely of materials and subcontractor services, the judge ruled it was “reasonable to presume” that MD’s competitors could obtain similar pricing from the various vendors which would enable them to know the percentage markup MD receives from its vendors and subcontractors. The majority rejected the Air Force’s argument that disclosure would unlikely cause competitive harm because a rival can never understand precisely the business judgment that goes into another firm’s pricing, stating that disclosing constituent pricing information – as opposed to the bid price itself which is public information – can cause substantial competitive harm even though “pinpoint precision” cannot be derived (*McDonnell Douglas Corp. v Dept of the Air Force, D.C. Cir., No. 02-5342*).

### **Proven Management Skills Outweigh Limited Specific Experience**

IMC and TLD received essentially equally technical ratings on a grounds maintenance contract where solicitation requirements stated experience would be evaluated for “similar dollar value and complexity” and awarded the contract to the lowest priced bid. IMC, who protested the award, was rated “excellent” for past performance based on performance of a two-year

grounds maintenance contract worth \$2 million while TLD received a “very good” past performance rating where though it had only one mowing contract worth less than \$300,000 it had identified 10 other contracts that were mostly more complex than grounds maintenance ranging in value between \$140,000 and \$3.2 million where its customers gave it “excellent” and “very good” ratings. The Board rejected the protest saying TLD’s lesser experience in grounds maintenance was offset by its higher technical/management ratings and very good past performance on contracts of similar value and complexity. It stated the Army did not abandon its past performance evaluation criteria explaining “mowing grass is not a difficult task...but the ability to manage a team of individuals in an organized fashion that results in standards being met in a timely manner requires good management, organizations and quality controls skills” (*IMC, GAO B-291997*).

### **Profit on Stop-work Order is Allowed**

*(Editor’s Note. The basis for an equitable adjustment - e.g. delay versus suspension of work - can affect the allowability of profit.)*

The government agreed contractor was entitled to an equitable adjustment due to a stop-work order but asserted it was not entitled to profit because the contract itself was not profitable. The Board disagreed, stating that profit is part of an equitable adjustment unless the contract provides otherwise whether or not the contract was profitable. The Board made clear that while the appeals boards have ruled a contractor is not entitled to profit in an equitable adjustment when a compensable delay arises out of a contract clause, such as the Suspension of Work clause that expressly precludes profit, a Stop-Work Order clause is not such a clause. (*Rex Systems Inc., ASBCA No. 54444*).

### **No Meaningful Discussion Where Agency Failed to Advise of Proposal’s Weaknesses**

*(Editor’s Note. What is considered adequate discussions are continuing to evolve through board and court decisions. Here is an interesting case.)*

In a cost type contract for the National Institute of Health to provide support services, NIH conducted discussions with four offerors in the competitive range, visited their sites and considered revised proposals. Cygnus protested an award to THG asserting the NIH’s discussions with it failed to comply with FAR 15.306 that requires an agency undertake discussions with offerors where the CO, at a minimum, shall discuss with each firm “deficiencies, significant weaknesses and

adverse past performance information” the offeror had not had an opportunity to respond to and that discussions must be “meaningful, equitable and not misleading.” Discussions cannot be meaningful unless they identify those weaknesses, excesses or deficiencies in the proposal that must be addressed in order to have a reasonable chance of being selected (*TDS Inc. B-292674*). In explaining to the GAO why THG’s proposal was superior, the NIH cited weaknesses of Cygnus’ proposal, some of which were considered major weaknesses but the GAO found NIH had failed to advise Cygnus of these weaknesses. Further, though it raised some matters of concern during discussions the record showed NIH misled the protester as to the results of those discussions, advising Cygnus it had successfully addressed NIH’s concerns. Even at site visits, the NIH representatives indicated there were no further unresolved concerns with Cygnus’s proposal. In addition, the GAO found there were errors made in its technical evaluation, namely, the number of participants at meetings managed by Cygnus was significantly higher than the NIH assumed. The GAO sustained the protest ruling that Cygnus was prejudiced by the agency’s failure to conduct meaningful discussions (i.e. it had a reasonable possibility of winning the award) and provide an opportunity for correction of the errors. The Board recommended NIH reopen discussions with the offerors in the competitive range and then request revised proposals (*Cygnun Corp. Inc., Comp. Gen. Dec. B-292649*).

### **Need Adequate Documentation to Justify Source Selection**

*(Editor’s Note. The following illustrates the difference between a best value and lowest priced/ technically acceptable procurement.)*

The U.S. Marine Corps solicited a five month with three one-year options contract for lease and maintenance of washers and dryers where the solicitation contemplated award to be based on best value and where price was significantly more important than other factors – technical, management and past performance – combined. The Request for Proposal was subject to FAR Subpart 12.6 that stated selection must be consistent with factors contained in the RFP and that any trade-offs considered must be fully documented for rationale of source selection. USMC received quotes from five offerors and gave equal technical and management ratings to all; three vendors including Tiger received favorable ratings while B&E having no past performance ratings history received a neutral rating and since price was the most important factor, the Marines gave the contract to B&E. Tiger protested asserting USMC “failed to perform an adequate price/technical

tradeoff and did not follow the RFP’s evaluation plan and awarded the contract on a low priced, technically acceptable basis rather than on a best value basis.

The GAO ruled in the protester’s favor. The USMC’s source selection rationale consisted of a one page “evaluation determination” and a matrix setting forth past performance ratings where all three vendors were rated “favorable” for past performance despite the fact the matrix showed Tiger’s references were “excellent” while the second ratings were “good” and the third only “marginal.” As for USMC’s source selection decision, the record only provided that “all evaluation factors were met by the proposals” and since price is the most important factor, B&E appears to be the successful bidder. The GAO ruled (1) in the light of Tiger’s higher past performance ratings the record did not support the claim all three vendors were rated “favorable” and (2) the statements in the evaluation determination did not explain why B&E’s price advantage outweighed Tiger’s advantage under the past performance evaluation factor. The GAO concluded it appeared that the award to B&E was made on the basis of low-priced, technically acceptable which abandoned the solicitation’s “best value” approach (*Tiger Enterprises Inc., Comp. Gen. B-293951*).

### **Prime May Use Sub to Provide FSS Services But Must Inform Agency**

*(Editor’s Note. The following demonstrates how you can use a subcontractor if your Federal Supply Schedule items are not included in an acquisition).*

Protester claimed IntelliStaf did not qualify for a VA contract for nursing services because the awardee’s federal supply schedule did not include the required services and it could not provide the services it was not qualified for by using a subcontractor. The GAO confirmed the RFQ placed vendors on notice that all items were required to be within the scope of the vendor (or its subcontractor’s) FSS contracts. Next, contrary to the agency’s argument, an FSS contractor acting as a prime contractor may use a subcontractor to provide services not on the prime contractor’s FSS contract provided those services are included on the subcontractor’s FSS contract. Nevertheless, the GAO denied the protest because IntelliStaf’s quotation did not mention it would be subcontracting for performance of the items not listed on its FSS schedule ruling “it was incumbent upon it to identify the subcontractor” in order for the agency to confirm the missing items on the prime contractor’s FSS were included in the subcontractor’s (*Altos Federal Group Inc., GAO, B-294120*).



## NEW/SMALL CONTRACTORS

### Current Rules on Gifts and Gratuities to Government Representatives

*(Editor's Note. Its probably a good idea to make sure all company personnel having dealings with government representatives get a copy of this article. Our discussion is based on an article by Glenn Sweatt, general counsel for Environmental Chemical Corporation written in the August 2004 issue of Contract Management.)*

Contractor and government personnel have a great deal of interaction with each other – marketing personnel meeting with government representatives, technical personnel, government guest speakers and numerous conferences, seminars, etc. Though a gift, meal, etc. is quite common and accepted in the commercial world, failure to know which rules apply to government employee-contractor relationships can lead to civil and criminal liability that can certainly affect opportunities in the future. There can be steep penalties and actions under a variety of related regulations such as anti-kickback rules and anti-bribery statutes. Even small dollar violations can be referred to government investigation. For example, in 1998, a company paid \$150,000 in fines and other penalties for making \$374 of improper gratuities, not to mention legal fees and career implications for the individuals involved.

To maintain public trust and eliminate any conflict or appearance of conflict the Congress and the executive agencies have produced numerous rules and ethical guidance on limiting acceptance of gifts and gratuities from outside sources. The Code of Federal Regulations, 5 CFR 2635, addresses the basic rules and the Office of Government Ethics (OGE) establishes and maintains the standards that apply to executive agencies.

A gift is defined as anything of value (e.g. material good such as tickets, golfing fees, key chains) or a service (e.g. professional financial advice, painting, carwash). It can also be a discount on a good or service or a forbearance of debt or obligation such as forgiving a loan. It can be given directly or indirectly (giving a government employee's child a scholarship, donation to a charity at the direction or suggestion of the employee). Prohibited sources are those people seeking business or other favorable action from an agency. Favorable actions include contract awards and modifications as well as policy decisions, regulatory

actions, legal rulings, employment or hiring, tax or zoning rulings, etc. It includes any individual in the entire company, not just the project manager.

### Exceptions

There are nine stated categories of things that are explicitly “not a gift.” The significant exceptions are: (1) modest refreshments defined as food or drink (e.g. coffee, donuts, snacks) “incidental to a meal” (2) items of little intrinsic value (e.g. holiday cards, certificates of appreciation and even plaques or trophies but not gift certificates or monetary items that may accompany such awards) (3) loans from banks with generally available terms (4) travel, sustenance or related expenses accepted in connection with attendance at a meeting related to the employee's official duties while away from their normal duty station and (5) gifts for which market value is paid (e.g. pays the contractor the market value of say a meal or movie ticket). Market value is generally defined as retail price, readily available on the market. Some items have face value, other have a readily determined price (i.e. what the contractor paid for it) while for promotional items (key chains, pens with contractor logo) the price paid should be the equivalent item on the open market. Because the value of items can vary over time and location, the important aspect is to make a good faith determination of the value.

In addition to the nine cases of exchanges not considered gifts there are 21 other stated exceptions listed by the OGE in which it is acceptable to accept a gift. Some of the most commonly encountered items are below.

1. The “20/50” rule causes the most confusion. An executive branch employee may accept unsolicited gifts as long as the value of the gift is less than \$20 and is limited to \$50 per year. The rule is tightly interpreted and has many limitations: (1) it applies to an entire organization, not an individual (e.g. a government employee could not accept \$11 pens from five different employees or could not accept a \$15 shirt from employee A, \$19 lunch from employee B and an \$18 gift basket from “the company”) (2) even gifts less than \$20 cannot be given if they are recurring (e.g. \$10 lunch at each of a contractor's quarterly status meetings are unacceptable) (3) gifts cannot be solicited no matter what the amount and (4) employees may not “pay the balance” (e.g. accept a gift over \$20 and pay the amount over \$20).

2. Under the *widely attended gathering rule*, a government employee may accept free attendance at an event if five criteria are met: (1) it is expected that a large number

of persons will attend the event (e.g. usually over 20 persons where spouses and guests may be included) (2) it is expected that a diversity of views or interests will be present where the event is open to a given industry or profession and the attendees represent a “range of persons interested in a given matter” or there is otherwise a diversity of views represented (3) the employee’s attendance will further the agency programs or operations which can include community relations (4) the cost of the event for employees who attend (and their spouses or guests) will be paid for by the event sponsor or if not the event sponsor then the organization paying does not pick which employee can come or more than 100 people are expected to attend and the “gift” (attendance) has a market value of \$285 or less (5) if the government employee’s duties can substantially affect the interests of the paying source then the employee may not accept free attendance unless there is a written determination by the employee’s agency that the government’s interest outweighs the appearance the gift may improperly influence the employee.

3. Gifts based on *personal relationships* (e.g. a government employee who exits or retires from government service and leaves friends and colleagues with whom they used to exchange gifts) are usually still allowable but should be reviewed on the basis of the context and history. Important factors to be weighed are the nature of the friendship, value of the gift, who paid for it (employee or company), whether or not there is reciprocity, etc. For example two college friends who have exchanged modest gifts for 10 years and which are paid out of their own personal funds can continue. But two friends who start a gift-giving “tradition” after entering a contractor’s employment or a tradition that is unilateral or disproportionate would not likely meet the exception rule. Though there usually is no problem for family members, the factors of history, reciprocity, amount and nature of the relationship should be reviewed.

4. *Reduced fees* from professional organizations and discounts to government employees are applicable exceptions. Some professional organizations as well as hotel chains, travel agents, airlines, etc offer discounts to government employees and as long as these discounts are applied across the board evenly they are acceptable.

There are numerous other exceptions but these can be complex and highly fact driven (e.g. social invitations,

speaking engagements, awards or honorary degrees, gifts related to employment discussions, gifts from a political organization, outside business activities of employee or their spouse, etc.). The author suggests looking at the “Frequently Asked Questions” scenarios provided at [www.usoge.gov/pages/misc\\_files/faq.html](http://www.usoge.gov/pages/misc_files/faq.html) for a discussion of these and other exceptions.

## QUESTIONS & ANSWERS

**Q.** The owner of our company owns the building we occupy and charges us rent which we recognize as an overhead expense. DCAA now tells us we must charge ownership, not rental costs, which can include cost of money on the building. We also sublease part of the property and DCAA tells us we must deduct the rent received from our cost of ownership. Are they right?

**A.** Yes and no. Yes, normally you are required to charge the government for the cost of ownership (e.g. depreciation, allowable taxes, repairs and maintenance, leasehold improvements, etc) not the rent your company pays the owner as long as the owner exercises control over the property. You can also recoup cost of money on the capitalized value of the building and also the *land*. As for the accounting treatment of the sublease, you need to deduct the portion of the rent you receive that represents cost, not the entire amount of the rent.

**Q.** The government pays us with a credit card around \$62,000 per month on a GSA contract and we pay around \$22,000 per year on those credit card charges. Most of our charges on the contract are based on scheduled rates for different categories of employees and we also include separate charges for various direct expenses. Are the credit card charges considered a direct or indirect expense?

**A.** Even though credit card purchases may normally be charged indirect, the unusual amount for this contract would likely require a direct charge. You can probably recover it as an ODC charge to the GSA contract but even if not, government auditors would likely require the direct charge since it is such a material amount compared to your other credit card charges.