GCA REPORT

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NEW DEVELOPMENTS

Compensation Caps Quietly Increased

Effective June 24, 2014, the government significantly reduced the ceiling for executive compensation and other employees to $487,000. FAR 31.205-6(p) establishes the compensation cap. Unlike previous years where it posted changes to the cap in the Federal Register, the Office of Management and Budget quietly posted changes where they can be seen on the OMB website. The new statutory caps are:

Jan 1 2018 – Dec 31, 2018 - $525,000
Jan 1, 2017 – Dec 31, 2017 - $512,000
Jan 1, 2016 – Dec 31, 2017 - $500,000
June 24, 2014- Dec 31, 2015 - $487,000.

Trends in the Government Marketplace...

We continue to briefly recount a few procurement trends.

- **Drone Killing Lasers Being Tested**

The US Air Force will be pitting lasers against numerous drones in a battle to find the best systems to defend bases from enemy incursions. Contractors are being invited to submit prototype laser systems that can shoot down small and medium sized unmanned aerial systems where the four most promising will be tested this fall. The prototypes are being developed using other transaction authority (OTA) that allows for expedited acquisitions due to fewer rules than FAR based procurements.

- **Competition to Provide E-Commerce Portal Heats Up**

The General Services Administration's e-commerce portal plan to select two or more providers in 2019 is beginning a fight among contenders who stand to bring in billions in revenue. Amazon, through its new business unit Amazon Business, is striking fear into its competitors that it aims to dominate the federal government's purchasing process where it will monopolize federal online purchases from pens and papers to computers and office furniture. The head of the new business, Anne Rung who used to run the Office of Federal Procurement states Amazon will be able to solve the issue of commercial firms accessing federal government buyers where in the near future smaller sized businesses can sell their products and services through an e-commerce portal rather than navigating 3,200 separate procurement units across the federal government.

- **DOD and CIA Delays Awarding Multibillion Dollar Cloud Contract**

The Pentagon, following many critical comments, has delayed indefinitely its final RFP that will spell out requirements for a multibillion-dollar cloud contract. The decision to avoid a "rush to failure" follows objections from such high tech firms as Microsoft and Oracle for a winner take all award they assert favors Amazon, the leading provider of cloud computing services. Despite the objections the DOD states it has not changed its winner take all strategy for an initial two year contract with two options that may add another eight years.

There is currently a hot debate going on for awards of cloud computing. The Central Intelligence Agency is looking to team up with industry experts to run a series of open source intelligence projects using its Amazon cloud. The CIA project, known as Mesa Verde, will use its C25 cloud built by Amazon Web Services LLC (AWS) to pour through thousands of terabytes of data, including that publicly available on the web, and apply such tools as natural language processing, sentiment analysis and data visualization to draw conclusions others might have missed. A first RFP draft is scheduled for Q418, final RFP in Q119, proposal deadline for Q219 and award in Q319. Many commentators are saying the Mesa Verde project is an indication of AWS's increasing penetration into the government's national security market following Amazon's $600 million 2013 ten-year award for C25 which is accessible to all 17 agencies of the US intelligence community.

- **DOD May Lead Race to Develop Self Driving Vehicles**

Despite the race of Alphabet, Uber, Tesla and Waymo to produce self-driving cars the biggest race could be run in the Pentagon. The stakes are high for the Defense Department where 52 percent of fatalities in combat zones are attributable to transporting food, fuel, munitions

and other logistics where Defense authorities are saying these deaths can be eliminated with relatively simple Artificial Intelligence algorithms that do not have to take into account pedestrians and road signs the other firms are dealing with. The head of DOD's DARPA Michael Griffen states there will be self-driving vehicles in combat arenas before they will be on the streets. The $700 billion defense budget will allow DOD to aggressively apply technologies developed in the commercial world to develop not just vehicles for delivering fuel but also unmanned tanks, smart vehicles for bomb disarmament and unmanned submarines.

DOD Final Rule Promotes Voluntary Disclosure of Defective Pricing

The Defense Dept. issued a final rule to the Defense Federal Acquisition Regulation Supplement (DFARS) affirming that DOD contracting officers have the right to request audits of defective pricing cases. The rule is being put into place to "promote voluntary contractor disclosures of defective pricing identified by the contractor after contract award." The DFARS amendment codifies the ability of COs to request either a limited in scope or full scope audit when contractors voluntarily disclose instances of defective pricing. The change was a result of receiving comments about the proposed change that required a mandatory audit for all cases where there was a voluntary disclosure of defective pricing.

GAO Updates its Guidance to Bid Protests

The General Accounting Office has just issued its 10th edition of its descriptive guide to filing protests at the GAO. The booklist is an informal guide that provides an overview of the GAO protest process that includes applicable regulations, available remedies, practice tips, key considerations, what to expect from each step and possible outcomes. It also addresses filing a protest, exparte communications, hearings, deadlines, GAO decision timetable, alternative dispute resolution, informal conferences, judicial proceedings and requests for reconsideration. The booklet was first issued in 1975 but goes through frequent revisions to keep track of new developments and GAO rulings.

FAR Final Rule on Audits of Termination for Convenience Settlement Proposals

The FAR Council issued a final rule raising the threshold for audit of prime contract and subcontract settlement proposals from $100,000 to $750,000, aligning the threshold to that of obtaining certified cost or pricing data. The rule revised FAR 49.107, "Audits of prime contract settlement proposals and subcontract settlements", where it removed the specified dollar threshold at which a termination contracting officer must refer a prime contractor settlement proposal for audit and replaces the threshold with a cross reference to "the threshold for obtaining certified cost or pricing data as set forth in FAR 15.403." *(Note, the threshold for the certification of cost or pricing data has recently been increased from $750,000 to $2 Million so we assume the T of C threshold will also be raised to $2 Million).* FAR 49.001 defines a settlement proposal as "a proposal for effecting settlement of a contract terminated in whole or in part submitted by a contractor or subcontractor in the form and supported by the data required by FAR Part 49" *(Fed Reg. 19149).*

Final Rule Increasing Threshold to Hear Task and Delivery Order Protests

FAR 16.505 has been revised to raise the threshold for DOD, NASA and Coast Guard task and delivery order protests from $10 million to $25 million. The change implements the 2017 National Defense Authorization Act where the FAR currently bars protests arising from task or delivery orders in excess of $10 million "except for a protest on the grounds the order increases the scope, period or maximum value of the contract." The change is intended to create savings for the GAO and other executive agencies to no longer hear protests for task or delivery orders between $10 million and $25 million *(Fed. Reg. 19145).*

DFARS Final Rule on Electronic Parts Supplier Review Requirements

A final rule clarifies an earlier proposed rule to make DOD contractors and subcontractors subject to review, approval and audit by appropriate DOD officials. The final rule clarifies that a government review, audit and approval of a contractor approved supplier is not mandatory but rather the government's review will generally be made in conjunction with a contractor purchasing system review (CPSR) or other surveillance of purchasing practices unless the government has credible evidence the supplier has provided counterfeit parts. The rule affects electronic parts that are no longer purchased by the original manufacturer of authorized aftermarket manufacturer and that are not currently in stock from the original manufacturer or authorized dealer. Disapproval by the contracting officer does not constitute a contract change entitling a modification of contract price because the contract clause already states the contractor-approved supplier is subject to review and audit. As for whether

disapproval affects other contracts the answer is Yes because deficiencies found from a CPSR impact all government contracts *(Fed. Reg. 19641).*

Class Deviation on Micropurchase and Simplified Acquisition Threshold Generates Opposition

The Director of Pricing/Defense Procurement and Acquisition Policy Shay Assad issued a class deviation on DOD acquisitions of supplies and services funded by DOD. The class deviation instructs contracting officers to use the revised definitions and procedures associated with the micropurchase threshold, simplified acquisition procedures and special emergency procurement authority. The class deviation increased the micro-purchase threshold to $5,000 and the simplified acquisition threshold to $250,000.

Separately, recently both the draft 2019 DOD Authorization Act and Senate provisions are proposing to increase the micro-purchase threshold from the current $5,000 amount for DOD and $10,000 for civilian agencies. The proposals, which are springing from the GSA actions to have portal providers to build new online marketplaces, are "premature" according to several industry groups. They state the change would increase the micro-purchase market from $7.5 billion to $15.5 billion where there has been no analysis of the impact of the change. Micro-purchases traditionally do not require competitive quotations and are usually performed non-competitively where criticism include they would detract from the Trump Administration's efforts to expand "Buy America" goals.

FAR Proposed Rule Will Expand Exception to Cost Data Requirement

The FAR Council has issued a proposed rule to create a separate standard for the Depts. of Defense, NASA and Coast Guard for the "adequate price competition" exception to submitting certified cost or pricing data under the Truth in Negotiations Act. The proposed rule at FAR 15.403 would dictate that "a price is based on adequate price competition only if two or more responsible offerors, competing independently, submit responsive and viable offers." This would have the effect of narrowing the circumstances in which an offer must submit cost or pricing data before award. The current standard for adequate price competition would remain in place for other agencies. The current standard contains more expansive conditions for identifying "adequate price competition" where it exists if (a) two or more offerors submit bids, the award is based on best value and the price or offeror is not found to be unreasonable (b) there was a reasonable expectation, based on market research, that two or more offerors would bid even though one offer was received and the CO reasonably concluded the bid was submitted with the expectation of competition and the price approved at least one level above the CO and (c) price analysis clearly demonstrates the price is reasonable. The proposed rule implements the 2017 National Defense Authorization Act provision that amends TINA stating certified cost or pricing data will not be required if the contract price is based "on adequate competition that results in at least two or more competing and viable bids" *(Fed. Reg. 27303).*

Companies Facing Sanctions Should Not Rush to Fire Employees

An interesting commentary in the June 19th issue of the Federal Contracts Report by Dominque Casimir and Charles Blanchard of Arnold and Porter cautions contractors about firing employees when a company becomes suspended or debarred or is accused of wrongdoing. Though understandable why that would be the first instinct – it allows the company to admit it was responsible, it shows disciplinary actions are being taken and that employees are being held accountable for their actions – such firings may not be in the companies' interests. Firing employees can be disruptive to ongoing work, bad for morale, require significant investment to recruit new employees, the company not employees are to blame where they may have compliance issues, poor training, wrong incentives or lack an ethical culture. They recommend companies take a more cautious approach including avoiding a rush to judgment and conducting an internal investigation, placing employees on administrative leave and take action only after results of investigations are completed.

CAS Board Reactivated

The long period of inactivity of the Cost Accounting Standards Board has ended where it recently selected an accounting member and has met three times this year. The board is discussing the congressional mandate to conform CAS with generally accepted accounting standards where it will first consider CAS 408 and 409 for conformance.

Government Meets Small Business Goal Again

The federal government awarded 23.88 percent of contract dollars, or $105.7 billion to small businesses in FY 2017, exceeding the statutory 23 percent government-wide goal for the fifth consecutive year. The government fell short

of its small business subcontracting goal of 31.95 percent where it awarded 31.40 percent of FY 2017 contracting dollars to small business subcontractors. The government missed its five and three percent goals for women-owned small businesses and Historically Underutilized Business Zones firms where respectively, it awarded 4.75 and 1.65 percent to WOSBs and HUBZone firms. The government did meet its three and five percentage goals for service disabled veteran owned small businesses and small disadvantaged businesses where respectively, it awarded 4.05 and 9.10 percent to SDVOSBs and SDBs. The Small Business Administration said nine agencies received grades of A+ (SBA, Commerce, HDS, Interior and Labor), twelve agencies received an A (NASA, GSA, DOD, DOE, DOJ and State), the VA and HHS received a B while USAID a C. The SBA gives an A+ to agencies achieving 120 percent or more of their agency-specific small business prime and subcontract goals, an A for 100-119 percent, a B for 90-99 percent, a C for 80-89 percent, a D for 70-79 percent and an F for less than 70 percent.

DCAA Anticipates End of its Incurred Cost Audit Backlog

According to DCAA's FY 2017 annual report, it is "on track to eliminate the backlog" of incurred cost audits by the end of FY 2018 stating its workforce did an "outstanding job" of reducing the backlog to an average age of 14.3 months. By that date, DCAA will then be "current on incurred cost audits based on a two year inventory of auditors." DCAA has been under pressure by both Congress and the GAO to reduce the backlog and reduce the time it takes to begin an incurred cost audit.

DCAA Issues Guidance on Auditing Long Term Agreements

The Defense Contract Audit Agency issued an alert with a separate Q&A section to its auditors clarifying that they may audit long-term agreements (LTAs) prior to the release of a request for proposal when such an audit will benefit the government and is requested by the contracting officer. An LTA is an agreement entered into between a prime or higher tier contractor and a subcontractor to establish pricing for future purchases of specified items. It is quite common for contractors to enter into an LTA with a subcontractor in advance of a specific RFP where DCAA audit assistance may be necessary to ensure the reasonableness of the subcontract price. Before initiating the audit the following is required: (1) the subcontract proposal has been approved by the subcontractor management (2) the prime has submitted the subcontract proposal to the government with an assertion it intends to award an LTA (3) the subcontract proposal is adequate for examination in accordance with FAR 15.4, Subcontract pricing and (4) the CO has determined that subcontract support is required.

In the Q&A section, the benefit of auditing LTAs is said to be based on the assumption that providing better subcontract pricing due to a stabilized business volume and acquisition cycle time benefits the government. The guidance states that certified cost or pricing data must be obtained for the subcontractor if the threshold for such certification (FAR 15.404) is met. Whether the entire LTA or just the portion applicable to a specific prime contract is to be audited will be determined on a case-by-case basis in conjunction with discussion with the PCO *(18-PSP-002(R).*

DECISIONS/CASES

Lockheed Can't Overcome Unisys' Price Advantage

(Editor's Note. The following should alert offerors that posing an alternative way to perform a contract often justifies a lower bid.)

A protest decision asserted the advantages Lockheed offered did not justify the difference between its $180 million offered price and Unisys' $30 million bid for security services. Lockheed put forth several arguments saying the technical evaluation did not occur on an equal basis and that Unisys' winning bid did not include many necessary costs. The Court ruled against Lockheed on the latter point stating the agency invited alternative technical solutions where the offerors' prices could reflect the alternative approaches *(Gen. Dynamics Mission Sys V US, Fed. Cl No. 18049).*

Joint Venture Contract Must Use its Member Employees Not JV Employees for Set-Asides

The Court ruled that Senter, a joint venture, was ineligible to receive an 8(a) set-aside contract for support services. It stated for a joint venture to be eligible for the set-aside contract employees performing substantive work must be employed by the joint venture's members, not the joint venture entity *(Senter LLC v US, Fed. Lc. No 17-1752C).*

Probable Cost Adjustment is Unreasonable

In its probable cost analysis which is allowed under FAR 15.404-1, the government made a downward adjustment

of $4.3 million to the labor costs of MEI's proposal where as a result MEI won the contract and Ares protested. The government's rationale for making the adjustment was that MEI proposed to hire staff from the incumbent contractor where because the proposed rates were higher than the incumbent's staff labor rates, it adjusted the proposed direct labor rates to the actual rates currently paid under the incumbent contract and also adjusted the applied indirect cost rates. The Comp. Gen. ruled the adjustment was unreasonable, especially in the light of the fact that MEI's technical approach represented that as part of its business strategy it offered a total compensation package designed to attract talent *(ARES Tech Servs, Comp. Gen. Dec. B-415081).*

Boeing May Not Rewrite CAS Rules

In 2011, a Boeing business unit implemented two unilateral accounting changes that raised the costs on one of its cost type contracts while six other accounting changes lowered the costs. The government sought reimbursement of $1 million for the increased costs whereas Boeing claimed the government would receive an unfair windfall where the other six accounting changes offset the increase. The Court sided with the government stating the cost accounting standards statute does not permit a contractor to offset multiple unilateral accounting changes when some of those changes increase costs while other decrease them. Boeing must pay for the impact of the increased costs because the CAS's clear language required examining the cost impact of each single accounting change where if it ruled in favor of Boeing it would be rewriting existing law *(The Boeing Co., v US Fed. Cl. No. 17-1969C).*

Litigation and Claims Costs Do Not Provide an Exception to Tecon

Under a DOE contract to operate a nuclear waste treatment plant at Hanford two former Bechtel employees filed lawsuits against the company alleging sexual and racial harassment and discrimination, As required by the DEAR, Bechtel notified DOE of the lawsuits where DOE authorized it to proceed with defense of the case while stating such authorization was not a determination for allowability of the legal costs which would await review against relevant regulations and court cases. After Bechtel and the employees settled the lawsuits and DOE reimbursed Bechtel $500,000 for litigation expenses the contracting officer informed Bechtel the costs were unallowable under standards established in the Geron vs Tecon case because there was more than "very little likelihood" the plaintiffs would prevail. Bechtel states that if Tecon was the standard then the costs would be unallowable admitting there was more than little likelihood but stated instead the DOE regulations at DEAR 970.5204-31 should be the standard that states "costs incurred to defend third party lawsuits are allowable." The Court ruled against Bechtel stating section (g) of the clause does identify exceptions to reimbursement when law or provisions of a contract prohibit it citing Tecon that ruled the contract clause at FAR 52.222-26, Equal Opportunity, which was incorporated into the contract, provides that costs incurred for defending and settling discrimination accusations are unallowable *(Bechtel Nat'l Inc v US, Fed. Cl. 1603333).*

NEW/SMALL CONTRACTOR

Avoiding Challenges to Direct Versus Indirect Charging of Costs

Many of our readers and clients have been drawing our attention to many types of costs that are being questioned because they are charged direct to contracts. Examples of these costs include depreciation costs, many support functions such as contract and subcontract administration, HR, Quality, accounting, project management and administration as well as bonuses. Most of the reasons being cited by auditors are variations on the theme that these costs are indirect costs where both their experience as well as the contractors' practices are to charge them indirect. Often the FAR or CAS 402 are cited as proof the costs should not be charged direct. However, most comments we hear is that, yes, these types of support cost are usually charged to indirect cost pools such as overhead, fringe benefits and G&A but for certain contracts these costs are legitimately direct costs. For example, for depreciation costs, those expenses relate to equipment purchased and used by specific contracts while for training costs they are direct because unique training may be required for a given contract. For direct support costs, they are direct costs because specific individuals are 100% devoted to specific contracts. The inquiries usually end by a "what do you think."

General Rules

Both the FAR and CAS do provide definitions of direct versus indirect costs. Direct costs are those identifiable with specific final cost objectives while indirect costs are those not identifiable with specific cost objectives or, phrased another way, all other costs. Most often the indirect costs are distinguished between indirect costs

in support of projects (e.g. overhead) or in running the business as a whole (general and administrative). Fringe benefit costs are considered indirect costs. Though there are a few commonly prescribed treatments or rules in how to treat these costs (e.g. marketing is usually G&A while, IR&D and bid and proposal costs are required to be G&A) most of the time there are no requirements where the decision is left to the contractor to make. CAS explicitly states the only requirement is the practice be put in writing (usually in the form of a CAS Disclosure Statement) and it be consistently treated where similar costs incurred under similar circumstances be treated as either direct or indirect. The same thing applies to non-CAS covered contractors where the Disclosure Statement is replaced by written policies and procedures.

How to Achieve Desired Results

The key criteria for determining what are appropriate treatment of costs is to turn to what is the contractor's practice. The best way of making this determination is what are the written procedures for treating these costs. Almost always, when there is a suggestion of a dispute, DCAA is supposed to ask what do the contractor's written procedures state. When a dispute is to be decided by an administrative contracting officer the first question asked is almost always: What does the contractor's written practices say? That often resolves the matter.

- **Written Policies**

Whether a contractor prepares a more formal CAS Disclosure Statement or prepares written policies, it is essential that they identify what practices they are likely to follow in the future. If the contractor wants to be able to treat costs differently, they should identify those costs in writing and justify the different treatments.

So for those expenses that contractors may want to charge both direct and indirect, each one should be identified in a written policy. Usually, for smaller contractors, an appropriate written policy may be just one all-inclusive one addressing "Government Contract Accounting Practices." That policy may address a myriad of accounting practices such as definitions for direct versus indirect costs, indirect rate structure, how direct versus indirect costs are distinguished and how indirect cost rates are monitored. For larger companies there should be a folder of government contract accounting policies where separate policies will address such topics as "Direct Cost", "Indirect Costs", "Computing Indirect Cost Rates", "Screening Unallowable Costs", "Labor Charging and Timekeeping" as well as specific practices addressing "high risk" expenses likely to generate audit scrutiny such as bonuses, consulting/professional services, selling expenses, insurance costs, severance pay, etc.

The ability to charge specific costs both direct and indirect when desired should be separately identified in the policies. Common verbiage is "when the cost is identifiable with one final cost objective it is charged direct; otherwise it is considered to be an indirect cost and charged to the overhead (or G&A) pool. If a similar cost is chargeable to more than one indirect cost pool, that should also be identified here. For example, rental and facilities related costs identified with assembly facilities are charged to overhead while similar costs incurred at a headquarters are charged to G&A.

- **Are Different Treatments in Compliance with FAR and CAS**

The requirement to treat costs consistently is a bedrock for government contract accounting. This requirement may contrast with the flexibility the regulations allow for. The key for understanding this apparent conflict lies in the concept of similar costs incurred under similar circumstances. When a contractor wants to be able to charge similar costs as direct or indirect sometimes, it must be prepared to show that the different treatment is because either the cost is not similar or is incurred under dissimilar circumstances. Examples of apparently similar costs that are treated differently are capital versus operating leases, purchased versus self insurance, pension versus 401(k) payments, project managers versus project administrators, etc. More often, dissimilar circumstances are grounds to treat costs differently. Most functions that are incurred to support projects (e.g. project managers, HR, accounting, purchasing, subcontract administration) are considered indirect because they often support multiple projects. Likewise, other support costs might be split between Overhead and G&A where senior executives over these functions are charged to G&A (VPs of finance, HR, Purchasing, Contracts, Accounting) because they set overall policy of the company while their subordinates might be considered overhead since most of their time is spent in support of multiple projects.

CAS 402

The most common objection we hear about dissimilar treatment of similar costs is the CAS 402 specific requirement to treat similar costs consistently as direct versus indirect. The most famous example in CAS 402-501(b)(2) addresses different treatment of firemen. In the illustration there are 10 firemen who protect all the

facilities and are charged indirect. In addition, a special contract requires three firemen on 24-hour duty at one fixed location where that contract would be charged direct. This famous, often quoted illustration is often raised as a justification for disparate treatment of similar costs.

Conclusion

Though preparing written policies is often viewed as a burden when carefully crafted they frequently act as a basis to be able to treat costs in a way that helps contractors achieve their pricing objectives. When preparing your written policy (or evaluating existing policies that may need to be updated) carefully consider all categories of costs where some may be treated just one way (e.g. contract material and subcontracts, touch labor, other direct costs) and then consider all other costs that may sometimes be treated direct and indirect. Take this opportunity to identify those costs that are significant and spell out the conditions for when they are direct and indirect.

QUESTIONS & ANSWERS

Q. We are a Subchapter S corporation and want to wait until the end of the year to pay our principles to conserve expenditures. We are working on two cost type contracts where the principles are charged at quite a high billing rate. If we are not paying them can the invoices be rejected for not reflecting actual costs?

A. If the billed rates reflect their actual salaries then the fact you are waiting to actually pay them should not result in problems with the invoices. If at the end of the period when you submit your incurred cost proposal and it is audited, if the salaries were not paid or compensation to the principles look like a "distribution of profits" rather than salaries, you are likely in for a fight. If you are not paying the principles, make sure you establish a liability for their salaries during the year.

Q. We had an extensive fire at our facility where we have received numerous inquiries about how to treat certain costs such as Can labor costs be charged direct when normally direct labor employees were sent home? Should cancelled travel costs not returned be charged direct or indirect? Etc.

A. Though government contractors have experienced similar situations such as during 9/11 we expected to see guidelines issued by the government and were disappointed they never came. The unusual nature of the event puts the proper treatment of these costs in the "gray area." First, I would look for written policies or practices that exist for analogous circumstances (e.g. paid absences for unusual circumstances, cancelled trips, etc.) and follow those practices. Secondly, since there are, in most cases, plausible justification for both direct and indirect charging, I would trust your judgement by choosing one method and be prepared to defend it. For example, direct charging of individuals can be defended because of the extraordinary nature of the events, the government required work to cease and you want to book these normally direct charged employees in a manner consistent with the way they normally are charged; indirect charging is viable because most paid absences are allowable indirect costs. If challenged, there will be no penalties. Finally, if more confirmation is desired, I would consult with your cognizant CO and ask either their opinion or tell them why your choice is used.

Q. If an employee does not complete their timesheets (they are sometimes out of the office unable to complete their timesheets on time) before we submit payroll we are told we have to input time for them in order for them to be paid (it's a state law). However inputting time for employees would be a violation of government timekeeping policies. What should we do?

A. One solution that comes to mind is to create a "dummy" account where the hours are identified for payroll purposes and the costs are reflected as an overhead "job" account. When the employee can, he will credit the "dummy" hours from the timesheet and charge the appropriate hours. There, of course, must be an adequate audit trail to track these transactions.

Q. Are your publications an overhead or G&A expense?

A. Like many other costs, you have a wide latitude unless your established practices limit you (e.g. all publications are charged to only one indirect cost pool). Generally, firms' definitions of overhead and G&A are sufficiently broad to allow either interpretation. For example, like many other categories of expense, the publications could be considered overhead to the extent they help you manage contracts or G&A because they help manage the company as a whole.

Q. We incurred costs on an unsigned contract in 2015 and our financial auditor told us we had to remove the revenue and costs from 2015 (because it was not signed).

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Should we remove the costs from 2015 for government costing purposes?

A. Assuming the auditor is correct, your question is a good example of many where accounting practices for financial accounting purposes diverge from accounting for government contracts. If the costs were incurred, they should be assigned to the unsigned contract since it is a cost objective in the year incurred. Whether or not the costs can be recovered is not relevant to how they must be reported.

Q. Our prime contractor keeps asking us for "DCAA approved rates." What are they?

A. Its not clear what they mean. Large and even some smaller contractors used to submit yearly or multiple-year proposals to establish forward pricing rates to be used on proposals for that year. (Your prime still may do this.) These rates were based upon budgeted or projected data for the period and DCAA would usually conduct a detailed review of the budgeted data and underlying assumptions and once completed, issue a rate letter approving the rates for proposal purposes. This practice is now rare. Now, DCAA will usually audit the first proposal (these days usually limited to direct labor and indirect labor rates) ensuring there is reasonable budget data if new rates are proposed or if prior year actuals are used, there are no significant changes. The results of the audit of the first proposal become the "audited rates" cited when government agency requestors ask about proposed rates used on subsequent proposals. These "audited rates" are the closest thing to "DCAA approved rates" these days. If an audit of proposed rates has not been conducted recently or if proposed rates differ significantly from the result of the latest audit then the closest thing to "approved rates" would be the provisional rates provided to DCAA for billing cost type work. They will usually send a letter approving these rates for billing purposes so you may want to assert these are your "approved rates."

Q. A state auditor is questioning our operating lease expenses included in our forward pricing rates asserting they "probably" include interest costs and since we cannot prove otherwise, they should be questioned. DCAA never questioned these costs. Is the auditor correct?

A. Just when many contractors were getting used to federal government auditors, they are increasingly being inundated by state auditors who audit state programs financed with federal funds (e.g. DOT, HUD, etc.). These auditors usually follow FAR cost principles (not always, sometimes they have their own state regulations) and often demonstrate a "creative" interpretation of them.

As for interest costs in the operating leases. You are required to make a determination of allowability on the expense you paid in accordance with FAR and contract terms – e.g. is it reasonable, arms length transaction, not associated with prohibited costs found in the FAR or contract. Unless the costs you are paying on the operating lease come from a cost type subcontract (highly unlikely) you are not required to inquire into the component costs of the invoice you paid nor is the vendor required to provide the information. An invoiced expense is the price set by the vendor and does not represent a cost build up for you to analyze – whether they incurred "unallowable" costs is irrelevant.

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