GCA Report

(A publication of Government Contract Associates)

July - August 2018 Vol 24, No. 4

NEW DEVELOPMENTS

New Contract-Related Interest Rate Set for First Half of 2018

The Treasury Secretary has set a rate of 3.5% for the period July through December 2018. The new rate is an increase from 2.625% applicable to the first six months of 2018. 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).

Revenue Growing Fast for Federal Contractors

A recent Grant Thorton survey concludes that revenue is growing fast for one out of every two federal contractors. Between 2016 and 2017, the revenue of 25 percent of the companies surveyed increased by more than 10 percent while another 25 percent grew between 4 and 10 percent. The other 49 percent of the contractors reported either revenue was flat or increased by less than 3 percent. Reasons for the increase were attributed to (1) the white house increase in expenditures in such areas as defense and (2) respondents benefiting from merger and acquisition activities.

TINA Threshold Increases to $2 Million

Along with some recent changes to thresholds we have previously reported on – simplified acquisition procedures now apply to acquisitions under $250,000 and the micro-purchase threshold is now $10,000 – another significant change is the increase in the Truth in Negotiations Act threshold to $2 million from $750,000. This significant change will mean that numerous contracts and subcontracts will no longer be covered by TINA which will mean much less vulnerability to assertions of defective pricing (and claims of fraud which often accompanies defective pricing assertions).

IG Issues Reports On CO Failure to Sustain DCAA Questioned Costs

Following a recent case that challenged a contracting officer for failing to uphold questioned costs by DCAA, the DOD Inspector General issued a report addressing the case intended to make sure there is more attention by COs to address costs questioned by DCAA. *(Some commentators are saying this will put pressure on COs to sustain those costs).* The case reflected an audit of a termination settlement proposal that questioned $852,000 of the proposed amount of $1.86 million where the CO authorized payment of the entire amount. The IG report said the CO lacked experience negotiating questioned costs, was not properly supervised and failed to comply with the FAR and contract terms by not issuing a price negotiating memorandum as required by FAR 15.406-3, Documenting the negotiation *(DODIG-2018-128).*

Another IG report was issued addressing a CO for not upholding $1.1 million in indirect costs and an additional $9 million in direct costs in the contractor's proposal four years earlier. In this situation, the IG said the CO's negotiation memorandum stated DCAA did not provide an overall audit opinion on the proposals and partly because the contractor was not willing to negotiate the audit's results with the government. Also, the CO told the IG is was concerned that the 6 year statute of limitations on recouping the expenses had expired. The IG faulted the CO, first with violating FAR 42.705-1(b)(5)(iii) that requires the CO to address "significant matters reported by the auditor" regardless of whether there was an overall audit opinion. Second, if the contractor failed to negotiate the CO had the option of issuing a unilateral decision to uphold the audit findings. Third, the CO failed to seek legal advice on whether the statute of limitations applied *(DODIG-134).*

DOD Shortens "Sweep" Period to Five Days

Director of Defense Pricing/Defense Procurement Shay Assad issued a memorandum directing DOD contracting officers on actions subject to the Truth and Negotiations Act (TINA) to ask offerors to execute the certificate of current cost or pricing data as soon as practicable but no longer than five days after the date of price agreement. The memo is intended to reduce the lead-time between the time contractors submit "sweep data" after price negotiation but before contract award. Several years ago, companies that were required to submit certified cost and pricing data with their proposals started conducting "sweeps" which, after reaching a price agreement but before certifying the cost data as accurate, complete and current, they sent out a notification within the company and to their suppliers requesting a last minute check of records to find any cost and pricing data submitted that were not accurate. The motivation for the sweep procedures is to avoid assertions of defective pricing or even false claims. Though contractors and the government consider sweeps to be a reasonable precaution the Defense Dept. has long complained that the sweeps needlessly delay contract awards or modifications, sometimes taking 60 days or more. Commentary on the memo indicates that the five-day limit may be too short a time where proposals are often quite complex and fear any more time makes contractors vulnerable to having their estimating system deemed inadequate.

Commercial Item Issues

(Editor's Note. Commercial item determinations are a hot topic. Here are a few stories.)

The final version of a defense policy legislation that would have allowed agencies to purchase more low value commercial items with less regulatory requirements was scrapped. Numerous industry groups lobbied against the provision arguing it would allow expansion of foreign products purchased by the government.

The Defense Department has issued a proposed rule on the inapplicability of certain laws and regulations on contracts for commercial items, prohibits certain flow down clauses and would modify the definition of "subcontracts" under commercial item contracts. The proposed rule, implementing the 2017 National Defense Authorization Act, will exempt from commercial item contracts and subcontracts all contract clauses in FAR 12.503 to 12.505 and DFARS 212.503 to 212.505. To eliminate the "overloading of commercial contracts with any clause that may seem to be remotely needed", the proposed law would prohibit flow-down of FAR and DFARS clauses unless the clause is specified or listed in certain FAR sections. The proposed rule will also provide a revised definition of "subcontract" to (1) include as a subcontractor a transfer of commercial items between divisions, subsidiaries and affiliates and (2) exclude from the definition agreements by a contractor for the supply of commodities that are intended for use on multiple contracts and not identifiable with any one particular contract.

The GAO issued a report addressing issues that will affect the General Services Administration's new e-commerce program. The GSA has identified three potential approaches for the e-commerce program where the result will likely be a mix of the three: (1) the e-commerce model will have product vendors sell their products directly to the consumer through the portal where the e-commerce portals will be responsible for the fulfillment of orders, invoicing and delivery (2) the e-marketplace model will be an online marketplace run by one vendor, the portal vendor where the marketplace will offer products by both third party vendors and the portal provider and (3) the e-procurement model has a vendor provide software that enables price comparisons across multiple portals where suppliers are responsible for fulfilling orders *(GAO-18-578)*.

2019 GSA Travel Rates Released

The US General Services Administration August 18th released the 2019, effective Oct. 1, 2018, maximum reimbursable amounts allowed for federal employees. As usual, though lodging and meals are considered separately for federal employees, the two amounts are added together for purposes of government contractor employees. The Standard CONUS (Continental US rate) covers about 2,600 counties while rates for the other 325 counties (called non-standard areas or NSAs) are higher. For CONUS, the per diem rate increased 3.5% (from $144 to $149), the CONUS lodging rate increased 1% (from $93 to $94) and the MEI rate increased 4%.

DCAA Issues its 2017 Annual Report

DCAA's recent 2017 annual report continues to provide statistics and narratives that portrays itself in the best, some say deceptive, light. Some of the report's highlights include:

1. DCAA now has four corporate audit directorates which focus on the seven largest government contractors that provide expertise and innovative audit approaches. Though the existence of contractor based expertise at

large contractors is not new (over 30 years) the creation of a senior level executive over the directorate is being lauded as a big improvement over the prior experience of assigning GS-14s to each major contractor where now it is hoped there will be consistency in audits and audit interpretations.

2. Creation of coordinated joint audits of DCAA and large contractors on major business system audits. A joint audit with Textron's internal audit team and DCAA is cited favorably. Though there have been attempts at such joint work for many years, DCAA has rejected them citing independence as reason to reject such approaches which now seems to have given way to a more collaborative approach.

3. DCAA's backlog of incurred cost audits is now down to 14.3 months and is scheduled to be eliminated by Sept. 30, 2018. The "backlog" is not the same thing as contractor proposals waiting to be audited but rather those proposal submittals that are more than two year old.

4. DCAA statistics includes a total net savings of $3.503 billion of which $2.398 billion is attributable to forward pricing audits and forward pricing rates, $760 million to incurred cost audits and $347 million to special and other audits. DCAA's return on investment is $5.20 to $1 ($3.503 billion divided by its funding of $670 million).

5. DCAA's overall cost sustention rate is 50.4% which is the weighted rate for all types of audits. Forward pricing yielded a 66.2% sustention rate while its incurred cost audits yielded a 28.6% rate while its other two types of audits yielded a rate in the low 40s percent.

6. DCAA reports the amount of time it takes to complete an incurred cost audit not from the time it receives the submittal but rather from the time of the entrance conference which DCAA controls. Despite the progress the report cites on incurred cost audits, it still took longer to complete (143 days compared to 138 days) and it completed fewer (1,527 compared to 2,103).

House Committee Passes Small Business Bills

The House Small Business Committee approved by both parties eight bills designed to expand small business opportunities for federal procurements. The most significant include:

1. H,R. 6369, The Expanding Contracting Opportunities for Small Business Act of 2018 would increase the size of sole-source contracts awarded to women-owned, service-disabled veteran owned and Historically Underutilized Business Zone certified small businesses. The bill will also implement a new verification process that provides only eligible firms receive sole-source awards.

2. H.R.6368. The Encouraging Small Business Innovation Act will implement changes to make it easier for small businesses to use the SBIR and STTR programs.

3. H.R. 6367. The Incentivizing Fairness in Subcontracting Act would provide incentives to subcontract with small businesses requiring prime contractors to keep records of subcontracting credits claimed at lower tiers and implementing a dispute process for small subcontractors to bring nonpayment issues to the agency's small business advocate.

4. H.R. 6382. Responding to industry criticism of "category management" initiatives that are resulting in fewer opportunities for small businesses, the Clarity on Small Business Participation in Category Management Act will require the SBA to report federal spending on "best in class" procurements and to report on the dollars awarded to small business.

Trump's Buy America Not Working Out as Planned

President Trump's pledge to "Buy America" may be failing to live up to its billing, at least for the General Services Administration that buys $54 billion worth of products and services. People working with the GSA say there is little evidence of any new enforcement activity to prevent contractors from selling non-compliant products (e.g. Chinese) as distinct from other administrations. Under the Buy America Act federal agencies must purchase US made articles while the Trade Agreement Act provides exceptions (e.g. Canada, Mexico and Japan but not China or India). Contractors agree to comply with the TAA and when they are non-compliant they are vulnerable to False Claims Act liability when the rules are enforced which includes assertions of fraud, contract terminations and debarment from federal marketplace. Comments also indicate that whistleblower false claims cases are in trouble when the GSA is not aggressive because the courts have ruled non-compliance is not punishable because the government routinely pays millions for non-compliant products.

New Electronic System For Filing Protests

A new final rule, effective May 1, 2018, has revised the bid process procedures by introducing the Electronic Protest Docking System (EPDS) and a protest filing fee. EPDS is now the exclusive way to file a protest and protest-related documents at the GAO with two exceptions

– documents containing classified information or that cannot be filed through EPDS due to size or format. Any one who anticipates filing a protest or defending against one should set up an account on the new system at https/ epds.gao.gov. Protesters also still need to provide a copy of the initial protest to the contracting officers outside the electronic system. The new rule clarifies that documents will be considered "filed" on the EDPS on a particular day if the system receives the documents by 5:30 PM EST whereas documents received by means other than EDPS (except for the two exceptions) will not constitute a filing. The new rule also implements a $350 filing fee for the initial protest. The rule establishes that where a basis for challenging a solicitation becomes known after its closing date the protest must be filed within 10 days of when the protester knew or should have known of the basis.

Proposed Rule Addressing DOD Invoicing

The Pentagon has issued a proposed rule seeking to clarify its procedures for submitting contract payments and receiving related electronic documents. The change is said to be needed because many contractors are prevented from using the DOD's web-based system for submission of invoices and advance shipping data largely because there is a misinterpretation of existing rules. One of the clauses to be changed would make it clear that contractors may use methods other the DOD's web-based system – known as Wide Area Workflow, now called Invoice Receipt Acceptance and Property Transfer – to submit payment requests and complete other tasks when the CO has authorized non-electronic methods. The Pentagon rule accompanies other changes that would require certified cost or pricing data when only one offer is submitted in response to a competitive solicitation and another rule making it prime contractors' responsibility for determining whether a subcontract qualifies for an exemption from submission of certified cost or pricing data.

Pentagon Stands Firm on its Single Cloud Contract Approach

The Defense Dept. is holding firm to its decision to award one main award for its multi-billion cloud computing contract according to the final RFQ the agency issued in mid-July. The Pentagon released its third and final RFP for its 10-year joint enterprise Defense Infrastructure contract, known as JEDI – long anticipated by tech and defense contractors eager for a shot at the potential $10 billion windfall for the winning contractor. After more than a year of wrangling where potential competitors asserted the competition was rigged in favor of the JEDI front-runner Amazon's Amazon web services. The contract's ordering period will consist of a two-year base period, two three-year optional periods and a final two-year option where the contract's maximum value will be $10 billion.

DECISIONS & CASES

Preaward Costs are Allowable Under a Termination

(Editor's Note. The following case addresses numerous issues for recovering costs under termination for convenience contracts. The issues are too numerous to cover here so we intend to address them in the next issue of the DIGEST. However, we thought we would address one important issue here – allowability of pre-contract costs.)

Because it had never performed on the contract before AGHP decided the 10 month transition-in period allowed in the contract was insufficient so it proposed (and did) an additional 330 days before contract award which the government did not take issue with nor discuss. In its T of C settlement proposal, AGHP included the pre-award costs which the government questioned. The Board asserted the following. The Board first cited FAR 31.205-32, Pre-contract costs which states those costs incurred before the effective date of the contract are allowable to the extent they would have been allowable if incurred after the date. It cited *Radant Techs. Inc. (ASBCA NO 38324)* which established a four-part test for determining whether pre-contract costs are allowable: (1) the costs were incurred prior to the effective data of the contract (2) the costs must be incurred directly pursuant to the negotiations and in anticipation of the contract award (3) incurring the costs must be necessary to comply with the proposed delivery schedule and (4) the costs must have been allowable if they were incurred after contract award. Applying the four prong test, the Board sided with AGHP concluding (1) there is no question the costs were incurred prior to the effective data of award (2) the second test was met saying the term "pursuant to negotiations" does not mean the subject of the costs had to have been discussed during negotiations but only the costs were incurred as a result of the solicitation and award process (3) AGHP presented credible testimony the costs were necessary to meet its scheduled deliveries and the government's witnesses conceded the 10 month transition-in period applied to incumbent offerors only and (4) there was no dispute the costs would have been allowable *(Phoenix Data Sltns, ASBCA No. 60207).*

Boeing Prevents the Government's Rights Grab Attempt

You generally want to avoid giving the government unlimited rights to use your software where the rule is if the software was developed at private expense the government is barred from having unlimited rights to that software. The Government sought unlimited rights for the software under Boeing's helicopter contracts where Boeing protested asserting the government was not entitled to unlimited rights because the technology was developed by Boeing as a private expense. Boeing and the Army entered into technology investment agreements in 2001 to develop software for the Apache helicopter and another in 2003 for research and development into unmanned air vehicles. The technology agreements are cooperative agreements intended to provide R&D funding and are not procurement contracts where the agreements are considered to be developed by private expense. The Board sided with Boeing saying the defense rule barring unlimited software rights if software is developed at private expense applied here *(The Boeing Co., ASBCA No. 60373).*

Contractor Wins Buy America Dispute

Under the Buy American Act, federal agencies may buy only articles made in the U.S. where the Trade Agreement Act provides exceptions allowing the President to identify designated countries that can provide goods. Acetris lost the bid after the Veterans Admin. ruled its tablets had ingredients from India which is not an excepted country. The Court ruled in favor of Acetris stating the VA improperly excluded domestic end products from the Trade Agreement Act's definition of eligible US made products stating an item is a domestic end product if the cost of components produced or manufactured in the U.S. exceeds 50 percent of the costs of all components. It said to side with the VA would be to prevent the federal government from purchasing products it had always been able to purchase where commentators on the case assert it now expands the ability of products to be eligible for sale under the Trade Agreement Act *(Acetris Health LLC v United States, Fed. Cl., No. 18-433C).*

Court Rules Protester Lacked Eligibility as a Small Business

The government terminated a $49 million small business set-aside contract with Ideogenics when it determined that two of its subcontractors were affiliated with Ideogenics. The Court sided with the government saying the company lacked small business eligibility because it violated a regulation known as the "ostensible subcontractor rule" which provides that an offeror lacks small business eligibility if it is "unusually reliant" on a subcontractor who will perform primary and vital requirements of the contract *(Ideogenics LLC v United States, Fed. Cl., No.17-1938).*

Appearance of Potential OCI is Not Sufficient for an Ineligibility Decision

FAR 9.504 makes contracting officers responsible for determining whether an organizational conflict of interest (OCI) exists during the contract selection process and if so, to avoid or mitigate its affects or conclude the offeror is ineligible for award. Archimedes proposed two incumbent employees as key personnel who had access to information that could benefit it for award. Both employees signed affidavits stating though they had the ability to they nonetheless did not have access to useful information to gain a competitive advantage. The contracting officer said though the actions taken had the effect of instilling confidence that competitive information was not used they nonetheless could have gained access where though no OCI occurred the appearance of an OCI was present which made them ineligible for award. In their protest, the GAO sided with Archimedes ruling the government needed hard facts of an OCI to find a contractor ineligible for award where mere appearance is not sufficient *(Archimedes Global B-415886).*

A Proper Claim Must be in Writing Not By Phone

After the government rejected H2L1's request for an equitable adjustment of $227,000 it stated in a telephone call it wanted the CO to treat its request as a claim under the Contract Disputes Act. The CO treated the telephonic statement as a proper claim which it denied. The Board ruled it had no jurisdiction over the appeal of the CO's decision because the telephone statement was not a proper claim where such a proper claim must be a written demand seeking payment as a right *(H2Li-CSC JV ASBCA No. 61404).*

SMALL/NEW CONTRACTORS

Presenting a Claim

(Editor's Note. We have recently been involved in several consulting engagements helping clients prepare claims and providing expert testimony and litigation support on several

claims cases so it fresh in our minds. In both situations, we examined several articles we had written over the last 25 years on Requests for Equitable Adjustments and claims (though a claim is usually an REA that has ripened into a claim after negotiations have broken down we will refer to this process as "claims" to keep it simple). We compressed some of these insights into the article below to hopefully provide some practical advice on how to present a claim.)

Whether it is for either an express or constructive change, a contractor cannot obtain an equitable price adjustment to its contract until it submits a well-prepared claim. Under an express change, the change is normally ordered by the government and the government and contractor reach an understanding about the scope of the change and its effect by relating information to the change. When an express order is issued and the understanding is achieved, the contractor begins work.

When the change is constructive or the result of a delay the work has usually already been performed so the government may be less motivated to reach an acceptable understanding. The facts of the change, their justification and documentation of the added costs must be carefully presented to a party who may be less than receptive. The following is intended to provide some general yet useful advice in preparing the claim.

Before preparing the claim several steps should be taken such as analyzing the contract, investigating the facts of how the resulting contract differed from the original one and determining whether the government or contractor is responsible. *(We have written extensively on these areas so use our word search.)*

Preparing and Submitting the Claim

A soon as a decision has been made to submit a claim, a contractor should give the government notice of their intent to file one. Such notice is commonly a short one or two paragraph note identifying (1) government action resulting in a change (2) indication the contractor considers this action an increase in scope (3) reminder of what the original contract requirements were and (4) what the additional work will require (e.g. X days of delay or increased cost of performance) and notice that supporting data will be submitted after completion of the work. Most clauses that grant adjustments require that timely written notice be made (FAR 52.243-1 to 52.243-7). The time requirements vary by clauses but many set short time limits. For example, the standard changes clause in supply contracts under an express change order require a contractor to assert its right to an adjustment within 30 days of the receipt of a written order. Notice of a constructive change should certainly be made before final contract payment.

There is no prescribed form for a claim. If the matter is simple, a short letter may suffice while more complicated contractual and costs matters will require a more detailed submission. Whatever its length, the claim is logically divided into a five-section format.

Section 1: Summary of Claim. This is best left until the other documentation has been assembled. It should state the legal and contractual nature of the claim and the essential facts on which it is based.

Section 2: Contract Requirements. This section should specify the relevant contract requirements (e.g. RFP, proposal, actual contract document) in order to establish the limits of the contract beyond which the contractor was not required to perform without additional compensation. This section should cite the terms of the contract and if available, interpret their meaning in light of relevant case law.

Section 3: Specify the Additional Work (or for a delay, the work the contractor was unable to do). This section is intended to contrast the contract requirements identified in Section 2 with the wrongful government conduct that created the claim. It should refer to all supporting factual documentation such as correspondence, inspection reports, memos, etc.) and they should be appended to the claim.

Section 4: Detail the Extra Work. The fourth section should detail and quantify the extra or changed work the contractor was required to perform as a result of the government's action. It should provide the factual support for the dollar values computed in Section 5 and should attempt to convince the CO the dollar amounts contained in Section 5 reasonably reflect the actual costs incurred as a result of the government action.

Section 5. Summary of Pricing the Claim. This should be a brief summary of the pricing of the claim which should be broken down into elements of increased labor, material/subcontract and other direct costs, overhead/G&A and reasonable profit. The level of detail to append to this section is a judgment call – detail backing up the price summary can be persuasive yet too much may raise a red flag resulting in a request for a detailed audit that might not otherwise be sought.

Certifying the Claim

If over $100,000 make sure to certify the claim asserting: (1) the claim is made in good faith (2) the supporting data is complete and accurate to the best of the contractor's knowledge and belief (3) the amount claimed accurately reflects the contract adjustment for which the contractor believes the government is liable and (4) the certifier is duly authorized to certify the claim on behalf of the contractor.

The Government's Evaluation and Negotiation

The contracting officer may ask for additional supporting data and the contractor should provide it promptly and completely. The CO has 60 days to issue a final decision or provide a date when the decision will be made. The CO will rely on the advice of its technical, accounting and legal advisors. An audit is not always performed but one will often be performed if the CO is persuaded the claim has some merit. After the CO reviews the claim, formal negotiations with the contractor will begin. It is recommended that full effort to settle the claim be made at the CO level, even if you need to settle for less than hoped for. If negotiations do not produce an agreement, a final decision should be requested from the CO so an appeal may be filed.

A contractor should keep a complete claim negotiation file throughout the process of presenting and negotiating a claim because it will probably be invaluable for a trial if no settlement is reached. It should contain (1) all documents not attached to the claim (2) names and addresses of personnel who witnessed events in question (3) names and addresses of persons involved in preparing the claim (4) drafts of the claim (5) any memorandum generated during the course of negotiations and (6) estimating and pricing worksheets and revisions of material previously submitted.

QUESTION & ANSWERS

Q. Our contract called for "verification" of certain parts where there was no definition of what verification entailed. When the government accused us of not taking appropriate steps, we provided an industry manual which shows the proper steps for verification (which we took). Are we on solid ground?

A. We really don't have enough information to provide an authoritative answer. However, your question touches upon a recent article we read in the July edition of the Nash & Cibinic Report that addresses whether industry trade practices should be used to interpret the meaning of a contract. They cite numerous cases where they conclude the following rules:

1. If the judge finds the words of the contract are ambiguous from reading the words alone then evidence of trade practice is admitted to determine if it demonstrates there is a single meaning. However, to get this evidence in the contractor must demonstrate the ambiguity was not obvious. That is, they have to overcome the obligation to request clarification before they submit an offer.

2. If the judge finds that the words of the contract appear to have a plain meaning but they are words used in a trade, evidence of trade practice will be admitted either to determine their meaning or to confirm the plain meaning of the contract. However, clear contract language will be found to override trade practice.

3. If the judge finds the words of a contract appear to have a plain meaning, trade evidence of trade practice will not be admitted.

Q. Though we don't have a lot of independent research and development costs, we do have quite a lot of bid and proposal costs. Since the FAR and CAS require us to add overhead to these costs and put them in our G&A pool, we are worried that our efforts to get more government business is making our G&A rate too high. What do you recommend?

A. Though CAS 420 requires you to burden your firm's labor with overhead for IR&D and B&P projects you do not need to apply overhead to G&A personnel. So, for example, though you need to identify the direct people working on the B&P project (e.g. direct labor, project managers, engineers) you can separate out G&A personnel who work on multiple B&P projects (e.g. admin support staff, marketing personnel) and not have to add them to the overhead base which then must be burdened with overhead.

Q. We have had server room IT issues with the network going down and employees unable to work fully (span of 3-7 days). The following scenarios have occurred where we want to know if we can bill our employees directly and what regulations apply: (1) some of our employees are idle, unable to work (2) some employees are able to work but are working at a much slower pace (since

GCA REPORT
P.O. Box 1235
Alamo, CA 94507

FIRST CLASS
U.S. Postage
PAID
CONCORD, CA
PERMIT No 249

some servers are still down) and (3) some employees are fixing work they had already done because of the server problems.

A. In general, the treatment of these costs is more a question of judgment and negotiation on your part rather than clear regulatory requirements.

1. This is a bit gray. Sure, one regulation does address idle labor where usually such labor is treated as an indirect cost. However, idle labor is usually considered to be longer term where it is commonly caused by such factors as contract delays or work stoppages where employees cannot be laid off, not just a short time due to equipment breakdown. Whether you can justify charging those direct labor people to the contract is more a matter of what you can agree to with your customer.

2. My first take is if they are working on direct projects then their time is appropriately charged to those projects whether or not they are at 100% efficiency. Like the answer above, it may be a matter of negotiation with your customer.

3. Once again, it's a gray area which should be resolved between reasonable people rather than pointing to a clear regulation. My first impression is that, generally, if direct people are working on direct projects then their time should be appropriately chargeable to those direct projects. However, you could argue these activities come under the category of rework costs where either the contract or your policies may provide for a different treatment of those costs.

Q. During a recent invoice audit we were cited by DCAA for not using work authorizations to authorize work performed by employees. What is this about?

A. We are seeing more and more challenges to labor costs based on no work authorizations by DCAA. There are no regulations we are aware of that require work authorizations (WAs) but DCAA interpretations, along with their guidance, is considered by them justification for citing contractors for the absence of WAs. We came across a recent Redstone blog addressing this issue where they state DCAA will cite DFARS 252.242-7006(c)(1) which states "the contractor's system will provide for a sound internal control environment, accounting framework and organizational structure." Notably, neither this section nor any other regulations address WAs. The blog goes on to identify DCAA guidance. Though neither the DCAA Contract Audit Manual nor its audit programs are regulatory nor binding on contractors, several sections addressing controls over labor costs do address the need to have WAs. For example, DCAM Section 5.908 addresses procedures for recording labor costs to cost objectives where WAs are included as one of the procedures. DCAM Section 5.902(b)(3) states that for a labor system to be considered "low risk" procedures for issuing and approving WAs are required. Further, the DCAM Chapter 6 on auditing incurred cost proposal cites WAs as necessary to help auditors determine the reliability of a contractor's labor system.

This publication provides general information and is not a substitute for accounting, legal, or other professional advice.
Duplication of this publication, without writeen permission, is prohibited.
Subscription: $175 for one year, $325 for two years.