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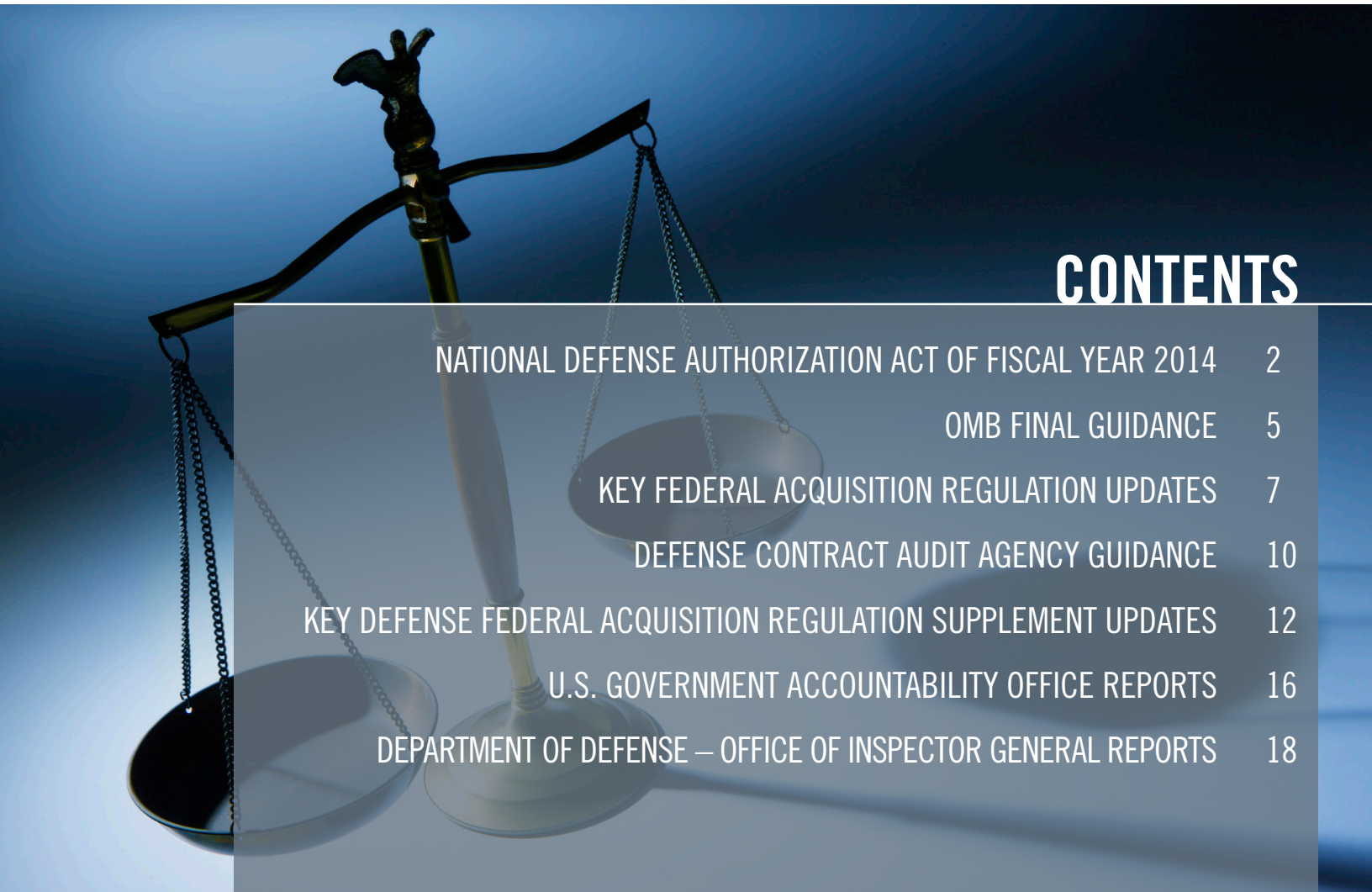


CONTENTS

Berkeley Research Group's Government Contracts Advisory Services (GCAS) practice keeps its clients up to date on the latest regulatory developments affecting the government contracts industry. This edition of the GovCon Research Report summarizes the critical regulatory and compliance issues contractors faced in the fourth calendar quarter of 2013. The issues are summarized by the following key subject-matter areas:

- National Defense Authorization Act of Fiscal Year 2014
- OMB Final Guidance
- Key Federal Acquisition Regulation Updates
- Defense Contract Audit Agency Guidance
- Key Defense Federal Acquisition Regulation Supplement Updates
- U.S. Government Accountability Office Reports
- Department of Defense – Office of Inspector General Reports

NATIONAL DEFENSE AUTHORIZATION ACT OF FISCAL YEAR 2014

Special Alert: President Signs FY 2014 National Defense Authorization Act into Law

BY: ZACHARY SCHOENHOLTZ

President Obama signed the FY2014 National Defense Authorization Act (NDAA) into law on December 26, 2013. This act serves to authorize and prioritize funding for the Department of Defense (DoD) and establishes the policies under which money will be spent in the coming fiscal year. This year, the bill authorized a $526.8 billion topline for national defense programs. More pertinent to contractors, the 2014 NDAA includes several policy changes that will likely give rise to changes within the FAR and DFARS in the near future.

Title VIII of the NDAA is of particular interest to the Government contract industry, as it includes provisions for acquisition policy and management. The FY2014 NDAA includes the following key updates:

Section 802 – Extension of Limitation on Aggregate Annual Amount Available for Contract Services

Section 802 eliminates some of the requirements from Section 808 of the 2012 NDAA. As previously reported here, section 808 of the 2012 NDAA restricted DoD procurement of services spending to FY2010 levels and required written approval of spending of continuing services in excess of $10M. In addition Section 808 of the 2012 NDAA established DoD negotiation objectives for direct labor and indirect rates to remain at FY2010 levels. Per Section 802 of the 2014 NDAA, the DoD buying commands are no longer required to target negotiation objectives of contractor direct labor and indirect rates at FY2010 levels. In addition, DoD officials are no longer required to approve in writing any award for continuing contract services in excess of $10 million. Section 802 of the FY2014 NDAA also amends Section 808 to extend the overall limitation on DoD services contract spending at FY2010 levels through FY2014.

Section 811 – Government-wide Limitations on Allowable Costs for Contractor Compensation

Section 811 includes a provision that establishes the contractor compensation cap at $625,000, with annual increases based on the Bureau of Labor Statistics Employment Cost Index (ECI). It also provides for the heads of executive agencies to establish exemptions for specialist areas that require unique areas of expertise. However, the NDAA compensation caps were effectively superseded when the President signed the Bipartisan Budget Act of 2013 (BBA) on the same day, which established its own compensation cap of $487,000 (*see related article in this issue of the BRG GovCon Research Report*).

Section 813 – Compelling Reasons for Waiving Suspension and Debarment

Section 813 updates DoD's existing responsibility to justify contracting with entities that have been suspended or debarred. Currently, the justification is required to be "available for public inspection"; under the provisions of the 2014 NDAA, DoD would be required to publish its reasons for waiving suspension or debarment "on a publicly accessible website."

Section 814 – Extension of Pilot Program on Acquisition of Military Purpose Non-Development Items

The expiration date for DoD's pilot program on acquiring military-purpose non-developmental items (originally established in Section 866 of the FY 2011 NDAA) is now extended through December 31, 2019. The program was initially set to expire in 2016, five years after the enactment of the FY2011 NDAA.

Section 821 – Synchronization of Cryptographic Systems for Major Defense Acquisition Programs

Section 821 amends Section 2366b(a)(3) of Title 10 of the United States Code to include an additional certification requirement that defense acquisition programs must meet before receiving Milestone B approval on cryptographic systems. Milestone B is one of three milestones used to oversee and manage defense acquisition programs. It represents the initiation of engineering and manufacturing development phase. In order to receive Milestone B approval, programs must now develop a plan to mitigate and account for the costs of any anticipated decertification of cryptographic systems and components during the production and procurement of the program.

Section 824 – Comptroller General of the United States Review of DoD Processes for the Acquisition of Weapon Systems

Section 824 requires that the Comptroller General perform a review of DoD's processes and procedures for procuring weapon systems. The objective of the review is to identify existing processes or procedures for which costs outweigh benefits or are otherwise not adding value. The report is due by January 31, 2015.

Section 831 – Prohibition on Contracting with the Enemy

Section 831 expands the authority granted to the U.S. Central Command (CENTCOM) under Section 841 of the FY2012 NDAA (and at DFARS 252.225-7993) to include additional combatant commands identified by the Secretary of Defense. The expanded authority now permits these combatant commands to prohibit, limit, or restrict the award of any DoD contract, grant, or cooperative award to a person or entity that has failed to exercise due diligence to ensure that none of the Government's funds are provided to any person or entity that opposes the United States or coalition forces. Contracting activities are further authorized to void or terminate for default any existing award under the same circumstances. This authority now applies to any award greater than $50,000 (down from the $100,000 threshold established in the FY2012 NDAA).

Readers should note that the provisions within the NDAA are not immediately incorporated into the FAR or FAR supplements. However, proposed and/or interim FAR/DFAR changes to incorporate these provisions of the 2014 NDAA into the regulations can be expected. BRG will keep its clients and contacts abreast of these changes as they are published within the Federal Register.

Significant Changes to Compensation Limit on the Horizon as President Signs Budget Deal and FY2014 NDAA

BY: SAJEEV MALAVEETIL AND ZACHARY SCHOENHOLTZ

December proved to be an eventful month in the procurement world as it relates to contractor compensation. On December 26, 2013, President Obama signed the Bipartisan Budget Act of 2013 and the FY

2014 NDAA. Both acts include provisions for reducing the Government-wide cap on the allowable costs of contractor compensation and expanding the applicability of the cap to all contractor employees. Though both acts have been signed into law, changes to the FAR have yet to be made.

The acts were signed into law just three weeks after the Office of Federal Procurement Policy (OFFP) increased the benchmark allowable compensation amount from $763,029 to $952,308 for FY 2012.

Section 811 of the 2014 NDAA includes a provision that establishes the contractor compensation cap at $625,000, with annual increases based on the Bureau of Labor Statistics Employment Cost Index (ECI).

The NDAA compensations caps were effectively superseded when the President signed the BBA, which established its own compensation cap of $487,000. Like the NDAA cap, the BBA cap is to be adjusted annually to reflect ECI changes.

To ensure continued access to needed skills and capabilities, both the NDAA and BBA provide provisions for the head of an executive agency to establish exemptions to the cap for scientists, engineers, and other specialist positions. The NDAA expands this group to include individuals in the mathematics, medical, and cyber security fields, as well as other fields requiring unique areas of expertise. Language in the BBA caveats that these exceptions should be narrowly targeted.

Both the NDAA and BBA compensation caps apply to all civilian and defense (i.e., Department of Defense, NASA, and Coast Guard) contractor employees, with the BBA including applicability to subcontractor employees as well. Both acts are applicable on costs incurred under any cost-type contract awarded on or up to 180 days after the December 26 enactment, which would be June 24, 2014. However, the FAR would need to be modified to reflect any change.

We expect to see a proposed or interim rule updating the compensation cost principle at FAR 31.205-6(p) to reflect a reduction of the compensation cap and to remove the OFFP's authority as it relates to establishing the compensation cap. Any such FAR change will have to be carefully coordinated, as the FAR Council still has before it two other FAR cases dealing with contractor compensation.

The first, FAR Case 2012-017, is a June 26, 2013, interim rule that extended the limitation on allowability of compensation for Defense contractor personnel from the top five senior executives to all employees. The second case, FAR Case 2012-025, is a proposed rule that—if finalized—would retroactively implement the expansion of the cap to contracts awarded before December 31, 2011, as it relates to Defense contractor employee compensation costs incurred on or after January 1, 2012.

Even though the new compensation cap will not be in effect until the FAR is modified, it is recommended that contractors proactively begin to analyze the potential impact of the anticipated change. At a minimum, contractors should begin:

1. *Evaluating work forces to determine the employees and positions that would likely be impacted by a reduced compensation cap, resulting in unallowable costs*
2. *Analyzing the associated potential impact of the reduced cap and expanded applicability on future forward pricing rates, direct labor rates, and provisional indirect billing rates*
3. *Identifying individual key personnel and standard service offerings that might qualify for the aforementioned "specialist" exemptions within the BBA and NDAA; and developing documentation on the importance of the individual skills and capabilities to customer requirements*
4. *Assessing the potential impact on departmental and company-wide profit margins resulting from a reduced cap and its expanded applicability to all contractor employees*

In addition, for contractors currently proposing on contracts subject to FAR Part 31 that are anticipated to be awarded on after June 24, 2014, it is recommended that consideration be given to the likely possibility of a reduced compensation cap when proposing and negotiating contract awards.

OMB FINAL GUIDANCE

Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards

BY: JOHN CRAIG

On December 26, 2013, the Office of Management and Budget (OMB) released its final "Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards."

This guidance is applicable to grants and cooperative agreements and represents a comprehensive consolidation and revision of OMB Circulars currently governing Federal awards to non-Federal entities. The guidance combines A-110 and A-102 into a single set of administrative rules; combines A-21, A-87, and A-122 into a single set of consolidated cost principles with entity-specific appendices describing indirect rate guidance for government, higher education, and nonprofits; revises the language of A-133; and presents all in a single document serving as a "one-stop shop" for financial assistance regulatory requirements.

Key changes in the consolidated regulations, now codified at Title 2 of the Code of Federal Regulations, include:

Revisions to Pre-award Policies
2 CFR 200.200 et seq.

Before making awards, awarding agencies must evaluate the risks to the program posed by each applicant, and each applicant's merits and eligibility. These requirements are designed to ensure applicants for Federal assistance receive a fair and consistent review prior to an award decision. This review will assess items such as the applicant's financial stability, quality of management systems, history of performance, and single audit findings.

Revisions Related to Post-Award Administration
2 CFR 200.300 et seq.

The final guidance consolidates financial, administrative, procurement, and program management standards that had been encompassed in OMB Circulars A-102 and A-110.

The new guidance takes the majority of the procurement standards language from OMB Circular A-102 (with many differences for organizations familiar with A-110) and provides more clarity regarding the expectations on Federal awardees with respect to subrecipient and subaward oversight and management.

Key changes include a new section that explicitly outlines the Government's expectation of recipients in terms of their internal controls; and more stringent requirements in Section 200.318(b) that non-Federal entities maintain a contract administration oversight system (originally a "contract administration system" in the proposed rule) to ensure contractors perform in accordance with the terms, conditions, and specifications of their contracts and delivery orders.

Significantly, in response to industry comments, the final rule includes a provision at Section 200.113 that was not included in the proposed guidance. Noting that "requirements in procurement regulations for non-Federal entities to disclose in writing any violations… have been effective measures to help prevent or prosecute instances of waste, fraud, and abuse," OMB included this new provision requiring non-Federal entities, both prime and sub-recipients, to "disclose, in a timely manner, in writing to the Federal awarding agency or pass-through entity all violations of Federal criminal law involving fraud, bribery, or gratuity violations potentially affecting the Federal award."

Revisions Related To the Cost Principles and Recovery of Indirect Costs
2 CFR 200.400 et seq.

The final guidance incorporates a number of changes to existing cost principles that warrant review. These changes may significantly impact

award recipients. Revisions in the new rule include new documentation requirements for travel and conferences expenses, elimination of "morale" costs from allowable employee health and welfare expenditures, a cap on certain relocation costs, allowability of certain computing devices to be expensed as supplies, and alternative methods for time and effort reporting.

One noteworthy change in the final guidance is that non-Federal entities may treat administrative costs as direct costs when such costs meet conditions showing they are directly allocable to a federal award. (2 CFR 200.413(c))

With regard to indirect rate recovery, entities new to Federal awards may use a "flat" indirect cost rate of 10 percent of modified total direct costs if the non-Federal entity has never had a negotiated indirect cost rate.

The new guidance also requires Federal agencies to accept negotiated indirect cost rates unless an exception is required by statute or regulation, or otherwise approved by a Federal awarding agency head or delegate based on publicly documented justification.

Finally, organizations with a Negotiated Indirect Cost Rate Agreement (NICRA) have been historically required to submit a new indirect cost proposal to the cognizant agency within six months after the close of each fiscal year. The new policy allows organizations to apply for a one-time extension of current NICRA without further negotiation of Federally approved negotiated indirect cost rates for a period of up to four years (2 CFR 200.414(g)).

Revisions Related to Audit requirements 2 CFR 200.500 et seq.

The final guidance sets forth new consolidated audit standards for entities receiving Federal financial assistance awards and replaces OMB Circular A-133. The changes within the final guidance primarily combine the guidance in OMB A-133 and A-50 on audit follow-up. The guidance reflects a movement to focus these audits and oversight efforts on higher-dollar, higher-risk awards and focus oversight on improper payments, waste, fraud, and abuse.

Most significantly, the threshold triggering a single audit or program-specific audit requirements is increased to $750,000 or more in annual Federal awards. These requirements apply equally to recipients and subrecipients under Federal programs. The final guidelines incorporate an exception to these audit requirements for non-U.S.–based entities expending Federal awards.

Further, the final guidance increases the minimum threshold for reporting questioned costs from $10,000 to $25,000 to focus on the audit findings presenting the greatest risk. OMB believes this will eliminate smaller-dollar audit

findings, which require utilization of resources for follow-up audits that are unlikely to indicate significant weaknesses in internal controls.

These changes necessitate a careful review and analysis of an organization's current business practices. Although OMB has raised certain thresholds for audit and materiality, it has also beefed up mechanisms of oversight related to mandatory disclosures, pre-award review of risks, standards for financial and program management, sub-recipient monitoring, and remedies for noncompliance.

Agencies have six months to submit to OMB necessary drafts implementing regulations, with the expectation that they will be finalized and effective no later than December 26, 2014. New audit requirements will apply to audits of fiscal years beginning on or after December 26, 2014. In the meantime, entities receiving Federal financial assistance awards are encouraged to become familiar with and comply with the new standards.

KEY FEDERAL ACQUISITION REGULATION (FAR) UPDATES

Proposed Rule: Higher-Level Contract Quality Requirements (FAR Case 2012-032)

BY: LUKE MANCINI

Today's Federal procurement contracts involve a wide variety of electronic items, which increases the risk of counterfeit components and items making their way into Federal service. Section 818 of the 2012 NDAA required DoD to issue regulations addressing contractor responsibilities for detecting and avoiding the use or inclusion of counterfeit parts or suspect counterfeit parts.

On December 3, 2013, the FAR council issued a proposed rule to modify the FAR to ensure agencies assess the risk of counterfeit items when determining whether higher-level quality standards should be used by the Government and relied on by contractors.

In proposing the rule, the FAR council states that the risk of counterfeit parts extends beyond just DoD and electronic parts and, instead, poses a supply-chain challenge to both Government and industry. The proposed rule is one of three FAR proposed rules addressing various aspects of detection and avoidance of counterfeit parts as required by Section 818 of the 2012 NDAA. The two others are DFAR Case 2012-D055 ("Detection and Avoidance of Counterfeit Electronic Parts"), which was published on May 16, 2013; and FAR Case 2013-002 ("Expanded Reporting of Nonconforming Supplies").

To hedge the risk of counterfeit parts on all Government contracts, the FAR council proposes to amend the FAR to: a) clarify when the use of high-quality standards in solicitations and contracts are necessary; b) update obsolete quality standards; and c) add two new industry standards that pertain to the avoidance of counterfeit items. Additionally, the proposed rule adds quality standards to the list of issues considered as part of the standard Contractor Purchasing System Review (CPSR).

The FAR changes proposed include:

FAR	Summary of Change
FAR 44.303: Extent of (Purchasing System) Review	CPSR steps would be revised to add implementation of higher-level quality standards to the areas for evaluation when conducting a contractor's purchasing system review.
FAR 46.202–4(a): Quality Assurance – Higher-level Contract Quality Requirements	Require agencies to establish procedures for determining when higher-level quality standards are appropriate, determining the risk (both the likelihood and the impact) of receiving nonconforming items, and advising the contracting officer which higher-level quality standards should be applied on the contract.
FAR 46.202–4(a)(1): Quality Assurance – Higher-level Contract Quality Requirements	Add "design" and "testing" to the list of examples of technical requirements.

FAR	Summary of Change
FAR 46.202–4(b): Quality Assurance – Higher-level Contract Quality Requirements	Remove outdated or obsolete standards, and add new examples of higher-level quality standards, including those related to counterfeit electronic parts and materials. This list of standards was reviewed and revised based on subject-matter experts in quality assurance from across the Government.
FAR 46.311: Quality Assurance – Higher-level Contract Quality Requirement	Clarify that, if the clause is used, the contracting officer shall specify one or more higher-level quality standards.
FAR Clause 52.246–11: Higher-Level Contract Quality Requirements	Revised to remove the opportunity for the offeror to select a standard. (The contracting officer (CO) would tailor the clause, and the contractor would be subject to the CO-determined requirements)

Comments to the proposed rule are due on February 3, 2013. If this proposed rule becomes final without changes, it will have a significant impact on Federal IT contractors, with implications for supply-chain sourcing, associated quality assurance programs, and contractor purchasing system reviews.

With the potential expansion of the detection and avoidance of counterfeit parts requirements beyond all electronic parts included on DoD contracts, manufacturing contractors will need to ensure that all components included in manufactured products sold to the Government are not counterfeit and meet quality assurance requirements specified in the contracts. This burden may be felt more acutely by smaller manufacturing contractors, for whom the additional cost of compliance will loom larger.

Final Rule: Prioritizing Sources of Supplies and Services for Use by the Government (FAR Case 2009-024)

BY: SAJEEV MALAVEETIL

On December 31, 2013, the FAR Council updated the FAR to clarify and refine the priorities of required Government supply and services sources.

The most significant change from the final rule is the removal of Federal Supply Schedule (FSS) contracts from FAR 8.002. Prior to the rule change, FSS contracts were commonly believed to be among the list of priorities of mandatory sources for supplies and services. The change clarifies that FSS contracts are not to be considered as a mandatory source of procurements for either supplies or services.

In response to public comments to the proposed rule for FAR Case 2009-024, the FAR council explicitly stated FSS contracts are not a mandatory source. Instead agencies are encouraged to consider using FSS contracts and other existing vehicles before considering sources in the open market.

The final rule revises FAR 8.003 "Use of other mandatory sources," and FAR 8.004, "Use of other sources." Under the revisions to the FAR, if an agency is unable to satisfy its requirements from the mandatory sources specified at FAR 8.002 or FAR 8.003, they are encouraged to satisfy their requirements from other sources, such as FSS contracts (for supplies and services); Federal Prison Industries, Inc. (for services); and commercial sources (including education and non-profit institutions). Agencies are reminded to provide consideration to small business concerns and 8(a) contractors.

Contractors with significant FSS contract sales are concerned that the clarification within the FAR resulting from this rule change will adversely impact FSS program sales as a result of fewer opportunities being placed through the schedule program.

Final Rule: Accelerated Payments to Small Business Subcontractors (FAR Case 2012-031)

BY: MARY KAREN WILLS

This FAR rule adds provisions to FAR Part 32 that require prime contractors to pay small business subcontractors on an accelerated timetable to the maximum extent practicable, and upon receipt of accelerated payments from the Government, after receipt of a proper invoice and required documentation from the small business subcontractor. The rule implements OMB Memorandum M-12-16 and M-13-15, which included temporary policy regarding accelerated payment to small business subcontractors. The rule also requires this accelerated

payment under subcontracts with small business subcontractors for the acquisition of commercial items.

A new clause, FAR 52.232-40, "Providing Accelerated Payments to Small Business Subcontractors," will be inserted in solicitations and contracts after the effective date of December 26, 2013. FAR 52.244-6, "Subcontracts for Commercial Items," will be revised to incorporate FAR 52.232-40.

The comments to the interim rule included remarks about the lack of definition around when accelerated payments are made, and what they are made for. The final rule response provided that this is to ensure flexibility in the application of the rule and accommodate varying contractor capabilities to make accelerated payments.

Small business subcontractors should ensure they flex this rule as necessary to receive accelerated payments from prime contractors.

Proposed Rule: Ending Trafficking in Persons (FAR Case 2013-001)

BY: JOAN BERGHANE

On September 26, 2013, the FAR Council issued a proposed rule to amend the FAR to strengthen protections against trafficking in persons in Federal contracts. The proposed rule is intended to implement the September 25, 2012, executive order on "Strengthening Protections Against Trafficking in Persons in Federal Contracts," and Title XVII, "Ending Trafficking in Government Contracting," of the 2013 NDAA. Intended to create a stronger framework for agency compliance by providing additional requirements for awareness, compliance, and enforcement, these policies would prohibit:

- Destroying, concealing, confiscating, or otherwise denying access by an employee to his or her identity or immigration documents (e.g., passports or drivers' licenses)
- Using misleading or fraudulent practices during the recruitment of employees (e.g., failing to disclose basic information or making material misrepresentations regarding the key terms and conditions of employment)
- Charging employees recruitment fees, providing or arranging housing that fails to meet the host country housing and safety standards
- Failing to provide in writing an employment contract, recruitment agreement, or similar work paper in the employee's native language prior to the employee departing from his or her country of origin

In addition, the proposed rule would require contractors to provide return transportation or otherwise pay for the cost of return transportation upon the end of employment for an employee who is not a national of the country in which the contracted work takes place.

The proposed rule would require contracting officers to include within the Federal Awardee Performance and Integrity Information System (FAPIIS) any allegations substantiated by an agency inspector general that the contractor violated the in trafficking provisions.

The second component of the proposed rule would apply to contracts where the portion of work performed outside the United States exceeds $500,000. These expanded protections consist of a contractor certification and a compliance plan. The requirement for a compliance plan applies only to the portion of the contract that is performed outside the United States. The thresholds and applicability do not apply to a contract or subcontract that is solely for commercially available off-the-shelf items.

The contents of the compliance plan would be required to be posted at the workplace or the contractor's website. The compliance plan would consist of an awareness program; a reporting process; a recruitment and wage plan; a housing plan; and procedures to prevent subcontractors or their agents from engaging in trafficking in persons and to monitor, terminate, or detect any agents, subcontractors, or subcontractor employees that have engaged in such activities. Implementation of the compliance plan would require certification. The certification would be required

prior to receiving an award and annually thereafter for the term of the contract or subcontract.

If finalized in its current state, the rule changes would require contractors to modify existing functions to ensure anti-trafficking requirements are met. Processes that will need to be impacted include ethics, contracts, human resources, procurement, subcontract management, and program operations.

DEFENSE CONTRACT AUDIT AGENCY (DCAA) GUIDANCE

Revised Policies and Procedures for Low-Risk Incurred Cost Proposals Less Than $250 Million in ADV (MRD 13-PPD-021(R))

BY: ZACHARY SCHOENHOLTZ

On October 29, 2013, DCAA issued revised guidance and policies and procedures for sampling low-risk incurred cost submissions. DCAA will follow the new guidance for all submissions going forward, in addition to all submissions currently on file for which audit work has not been started. The policy changes were in response to feedback received from DCAA regional offices and field auditors and the result of ongoing monitoring of low-risk incurred cost proposals.

Consistent with previous guidance, the DCAA will continue to audit adequate incurred cost submissions exceeding $250 million in auditable dollar volume (ADV). In general, a contractor's ADV is the total direct and indirect costs on flexibly priced DoD contracts, adjusted for any costs that DCAA decides not to audit. The DCAA will continue to classify all submissions with an ADV less than $250 million as either high or low risk. Based upon the risk assessments, all high-risk submissions will be audited, and all low-risk submissions will be subject to audit only if selected by a statistical sample.

Under the new guidance, DCAA will perform a two-step procedure for determining the risk associated with an incurred cost submission: the first step will be a review of the questioned costs from the prior year (or most recently completed) incurred cost audit, and the second step will be a consideration of other risk factors relevant to the submission under review.

Based on the dollar value of the submission being reviewed, a classification of high risk will be given whenever the prior year questioned costs exceed the following amounts:

Current ICS Dollar Value	Questioned Cost Threshold in Relation to Dollar Value for Most Recently Audited ICS
<$1M	≥10%
$1M to $5M	Greater of ≥5% or $100K
$5M to $250M	>$250K

If the most recent audit questioned costs exceed these thresholds, the current submission will be classified as high risk and scheduled for an audit. For this step, questioned costs include costs questioned for a segment and a segment's allocation of questioned costs from any home office and/or corporate service center. Questioned costs take into consideration Government participation.

The second step of the risk assessment process applies only to submissions that were not classified as high risk in the first step. This step considers other risk factors relevant to the submission being evaluated. For submissions with dollar values less than $5 million, this includes fraud referral forms, disapproved accounting system determinations, or other specific risks that have a material impact on the submission being assessed. For larger submissions with dollar values in the $5 million to $250 million range, additional considerations include business system deficiencies relevant to the year under audit and the extent to which DCAA has previous experience with the contractor. DCAA uses a risk determination tool to help auditors document the specific significant risks that support the determination that an audit is warranted.

All submissions classified as low risk have the potential to be selected for audit by DCAA using statistical sampling. DCAA uses the following sampling guidance when selecting low-risk submissions to audit:

Low-Risk ICS Dollar Value	HQ Sampling Percentage
<$1 Million	0%
$1M to $50M	5%
$50M to $100M	10%
$100M to $250M*	20%
>$250M	100%

*For low-risk submissions between $100 million and $250 million, a mandatory incurred cost audit will be performed once every three years.

All low-risk submissions not selected for audit will be closed out through a Memorandum for Contracting Officer by DCAA.

Contractors should perform self-assessments of their submissions to determine if they qualify as high or low risk. If a low-risk determination is likely, consider communicating with DCAA and the Administrative Contracting Officer (ACO) to manage timely approval of indirect rates and issuance of a signed memorandum for the contracting officer.

Audit Program Revision: Major and Non-Major Contractors Labor Floor Checks or Interviews (Activity Code 13500 and Activity Code 10310)

BY: ZACHARY SCHOENHOLTZ

In October 2013, the DCAA published revised audit programs for labor floor checks at both major and non-major contractors. The revised audit programs reflect an additional audit step that was added to section F-1, "Conducting (Detailed) Employee Interviews," of each audit program.

The new audit step expands on the existing requirement that, during employee interviews, auditors must obtain documentation to substantiate the employee's labor efforts on each project being worked. Now, the auditor must also verify the documentation to actual contract requirements. Alternatively, auditors may obtain a description from the contractor on how the interviewed employee's work corresponds to contract requirements.

For floor check audits started in October 2013 or later, auditors will request not only documentation to substantiate labor efforts, but also contract documents that support the effort and documentation provided. This new requirement will likely increase the effort required to support floor check audits at major contractor locations.

As part of labor floor checks, contractors should be prepared to demonstrate that an individual's labor efforts are required per the contract.

Reducing the Number of Required Audit Reviews (MRD 13-PPS 024(R))

BY: ZACHARY SCHOENHOLTZ

On November 22, 2013, DCAA issued a Memorandum for Regional Directors (MRD) updating the guidance in DCAA Instruction 7642.2, an internal policy document outlining the required levels of review for each type of audit and the specific purpose of each review. This MRD is the latest development in DCAA's ongoing effort to balance audit timeliness and audit quality.

DCAA Instruction 7642.2 was first introduced through an April 9, 2013, MRD (MRD 13-PPS-005(R)). According to the April MRD, the new instructions were created because DCAA had received feedback from the field that the audit review process was taking too long, and that there were too many required levels of review, some of which were duplicative. The memorandum also noted that the review process was not consistent across teams, offices, and regions within the agency.

The November 2013 MRD revises DCAAI 7642.2 in consideration of input received from the field since its creation. Per this new MRD, DCAA has concluded that it can reduce the number of final reviews of audit packages without adversely affecting audit quality. As a result, DCAAI 7642.2 is modified to reduce the number of required reviews and allow management teams at each individual Field Audit Office (FAO), in coordination with the Regional Audit Manager (RAM), to determine the need for additional reviews.

Decreasing the number of required reviews should result in timelier audits, presuming that there will be

no adverse impact on the quality of audits performed.

KEY DEFENSE FEDERAL ACQUISITION REGULATION SUPPLEMENT UPDATES

Final Rule: Unallowable Fringe Benefit Costs (DFARS Case 2012-D038)

BY: ZACHARY SCHOENHOLTZ

Effective December 6, 2013, fringe benefits provided to ineligible dependents are expressly unallowable on DoD contracts and, as a result, subject to penalties. On February 17, 2012, the Director of Defense Pricing issued a policy memorandum, "Unallowable Costs for Ineligible Dependent Health Care Benefits." The memorandum reported that some contractors had been claiming healthcare benefit costs of employee dependents that were otherwise ineligible to receive those benefits. The memorandum emphasized that these costs should be disallowed per FAR 31.205-6(m), which requires that employee healthcare benefit costs must be reasonable and required by law, an employer–employee agreement, or an established policy of the contractor. It also stated that while DoD would not be pursuing penalties for these ineligible dependent healthcare benefit costs at the time, it did intend to amend the DFARS in the future to make these costs expressly unallowable. As previously reported on our blog, on March 28, 2013, the DCAA issued guidance to its auditors—consistent with DoD's memorandum—stating that penalties should not be pursued for unallowable costs for ineligible dependent healthcare benefits.

As of December 6, 2013, the DFARS is officially amended at 231.205-6 to explicitly state that any fringe benefit costs that "are contrary to law, employer–employee agreement, or an established policy of the contractor are unallowable." These costs, which would include fringe benefits provided to ineligible dependents, are now expressly unallowable and subject to penalty under FAR 42.709. The penalty provisions would be restricted to direct and indirect costs claimed on defense contracts issued on or after the effective date of the rule change.

Contractors should ensure that the HR/benefits enrollment process vets for ineligible dependents and segregates associated costs as unallowable.

Final Rule: Safeguarding Unclassified Controlled Technical Information (DFARS Case 2011-D039)

BY: SAJEEV MALAVEETIL

On November 18, 2013, DoD issued a final rule updating the DFARS to add a new subpart and an associated contract clause to address the requirements for safeguarding unclassified controlled technical information within contractor information systems. Controlled technical information is defined as technical data, computer software, and any other technical information covered by DoD Directive 52030.24, "Distribution Statements on Technical Documents" and DoD Directive 5230.25, "Withholding of Unclassified Technical Data from Public Disclosure."

The new DFARS Subpart 204.73 and associated clause DFARS 252.204-7012 require contractors to implement information technology (IT) security standards if the contractor has access to or transmits controlled technical information on or through its systems. The minimum security controls for safeguarding unclassified controlled technical information are based on National Institute of Standards and Technology (NIST) Special Publication (SP) 800-53, "Recommended Security Controls for Federal Information Systems and Organizations." The minimum controls include:

- Access controls
- Awareness and training
- Audit and accountability
- Configuration management
- Contingency planning
- Identification and authentication
- Incident response
- Maintenance
- Media protection
- Physical and environment protection
- Program management

- Risk assessment
- System and communications protection
- System and information integrity

Alternatives or exceptions to these standards require contracting officer approval.

In addition, the rule requires contractors to monitor their systems and report to the Government any cyber incidents within 72 hours of an incident occurring. For any cyber incidents that do occur, contractors are required to preserve and protect images of known affected systems and data for 90 days to allow for potential DoD review. Finally contractors are required to flow down to their subcontractors the DFARS clause 252.204-7012, which is to be included in all solicitations and contracts, including those using FAR Part 12 procedures for commercial items.

Defense contractors should evaluate their information systems to ensure that they meet the new requirements of DFARS 252.204-7012. In addition, IT security processes should be updated to ensure that incident monitoring, reporting and documentation requirements are fulfilled. Finally, defense contractors should update their purchasing and subcontract procedures to ensure appropriate flow down of DFARS 252.204-7012 requirements.

Interim Rule: Private Sector Notification Requirements of In-Sourcing Actions (DFARS Case 2012-D036)

BY: ZACHARY SCHOENHOLTZ

On October 31, 2013, DoD issued an interim rule amending DFARS 237.102-79 to implement Section 938 of the FY2012 NDAA. Per the requirements of Section 938, the Secretary of Defense must establish procedures to provide "timely" notification to contractors if the services being performed under a contract will be insourced to the Federal employee workforce.

Per the interim rule, once a contracting officer (CO) has received a decision from the cognizant component in-sourcing program official that contracted efforts will be insourced, the CO has 20 business days to provide notification to the incumbent contractor. This notification, which must be coordinated with the program official, must include a summary of the requiring official's final determination as to why the services are being in-sourced. The Government is precluded from initiating any hiring actions until the notification is provided. Similarly, the CO is prohibited from taking any formal contract actions associated with the insourcing until the notification is provided to the contractor.

Final Rule: Trade Agreements Thresholds (DFARS Case 2013-D032)

BY: KAYLA SEE

On December 31, 2013, DoD issued a final rule amending the DFARS to incorporate increased Trade Agreement thresholds to be in effect as of January 1, 2014. Every two years, the trade agreements thresholds are escalated according to a predetermined formula set forth in the World Trade Organization Government Procurement Agreement and the Free Trade Agreements.

The new thresholds can be found at DFARS 225.1101, 225.7017-3, and 225.7503, and DFARS clauses 252.225-7017 and 252.225-7018.

Final Rule: DFAR Supplement: Item Unique Identifier Update (DFARS Case 2011-D055)

BY: BRYANT LE

On December 16, 2013, DFARS Clause 252.211-7003, "Item Unique Identification and Valuation," was amended to update and clarify requirements for unique identification and valuation of items delivered under DoD contracts. The changes revise the prescription of the clause and the language within the clause to update and clarify instructions for identification and valuation processes. The clause is applicable on solicitations and contracts that require item identification or valuation, or both, in accordance with DFARS 211.274–2 and 211.274–3.

Specifically, the clause requires DoD item unique identification or a DoD-recognized unique identification equivalent for all delivered items, including items of

contractor-acquired property delivered on contract line items, for which:

1. The Government's unit acquisition cost is greater than $5,000;
2. The Government's unit acquisition cost is less than $5,000 and the requiring activity believes the identification to be necessary for mission essential or controlled inventory items; or
3. Regardless of value, for any:
    a. DoD serially managed item,
    b. Parent item,
    c. Warranted serialized item,
    d. Item of special tooling or testing designated for preservation, or
    e. High-risk item identified as vulnerable to supply chain threat, a target of cyber threats, or counterfeiting.

An exception to the identification requirements exists for contingency operations, or if the agency determines that it is more cost effective for the identification to take place after delivery. The latter exception applies to only acquisition of FAR Part 12 commercial items from small business contractors.

Furthermore, when applicable, the clause requires contractors to identify the Government's unit acquisition cost for all deliverable end items to which item unique identification applies.

As expected, industry comments to the rule expressed concerns regarding the additional cost burdens associated with compliance with the updated clause.

DoD responded referencing the Director, Defense Procurement and Acquisition Policy Memorandum, dated July 9, 2004, "Subject: Contract Pricing and Cost Accounting—Compliance with DFARS 252.211-7003," which clarifies that increased cost burdens associated with compliance with the clause are generally allowable given the costs comply with CAS and the FAR cost principles.

Final Rule: Preparation of Letter of Offer and Acceptance (DFARS Case 2012-D048)

BY: LUKE MANCINI

This December 6, 2013, final rule amends 48 CFR Part 225 to require additional communication between contracting officers and prospective Foreign Military Sales (FMS) contractors. This modification is intended to assist DoD implementing agency in preparing the Letter of Offer and Acceptance (LOA). It also allows COs to request relevant information on price, delivery, and other relevant factors from the contractor; as well as provide the contractor with additional information with regard to the FMS customer. The rule calls for increased communication between the CO and the contractor in advance of entering into an FMS contract.

Interim Rule: Requirements Relating to Supply Chain Risk (DFARS Case 2012-D050)

BY: LUKE MANCINI

Effective November 18, 2013, the Government is piloting a program to reduce supply chain risk to National Security Systems. This pilot will be conducted by DoD and will apply to the most sensitive Government intelligence, cryptologic, command and control, and weapons systems. The 2013 NDAA defines supply chain risk as:

> [T]he risk that an adversary may sabotage, maliciously introduce unwanted function, or otherwise subvert the design, integrity, manufacturing, production, distribution, installation, operation, or maintenance of a covered system so as to surveil, deny, disrupt, or otherwise degrade the function, use, or operation of such systems.

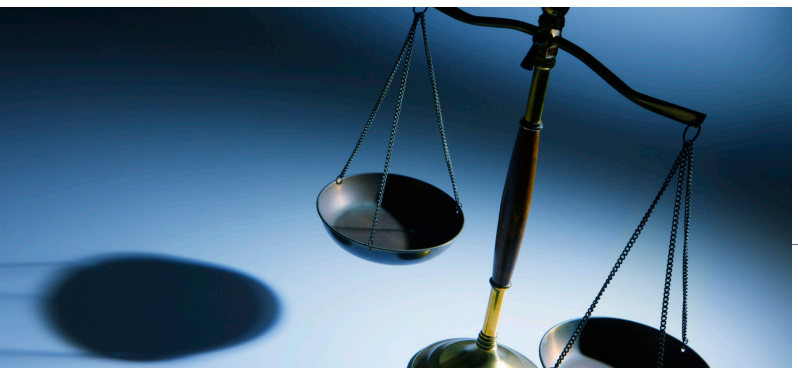
This pilot program will end on September 30, 2018, when DoD presents its results to Congress.

This rule provides the Executive Branch of the Government with broad powers to unilaterally "exclude sources" based on their assessed supply chain risk. Supply chain risk may be managed by one of the three approaches:

1. Exclude a source that fails to meet qualification standards established in accordance with 10 U.S.C. 2319
2. Exclude a source that fails to achieve an acceptable rating with an evaluation factor providing for the consideration of supply chain risk in the evaluation of proposals for award
3. Withhold consent for a contractor to subcontract with a particular source or to direct a contractor for a covered system to exclude a particular source

Criticism of the new rule includes the lack of due process and recourse mechanisms for excluding suppliers. Once the supply chain risk-management authority of Section 806 is authorized, it cannot be challenged via the usual Government Accountability Office (GAO) or judiciary channels. Such exercises of authority are deemed to be matters of national security, which means that the Government is not required to disclose the details of such an action.

The process for exercising this authority is somewhat convoluted. A single action against a prime contractor, subcontractor, or source requires: 1) approval from the head of a covered DoD agency; 2) approval from the Under Secretary of Defense for Acquisition, Technology, and Logistics; 3) approval from the chief information officer of DoD; 4) a risk assessment from the Under Secretary of Defense for Intelligence identifying the contractor/supplier in question as a "significant supply risk"; 5) written determination by the initiating "head of a covered DoD agency" stating that no less-intrusive measures are possible, and that this action is the only option; and 6) notice of the previous five steps, provided in advance to the appropriate Congressional committees.



Contractors should pay close attention to the evolution of this new supply chain risk-mitigation program, as it presents a new challenge for mandatory compliance efforts. The additional compliance burdens for contractors (evaluating and securing their supply chain without clear parameters) combined with the possibility of unilateral exclusion result in a significant risk. The pilot program will likely lay groundwork for more formalized regulations in the 2019 NDAA, which will be based on DoD presentation of its related findings.

Contractors providing information technology supplies or services should consider the following:

- *Contractors are required under the interim rule to "maintain controls in the provision of supplies and services to the Government to minimize supply chain risk"*
- *Agencies may consider all sources of information in determining supply chain risk; contractors should therefore perform diligence to ascertain if they might trigger a supply chain risk*

In addition, contractors should perform due diligence on supply chain subcontractors, which may be individually excluded from national security system information technology procurements

Comments to the interim rule were due by January 17, 2014.

Final Rule: Approval of Rental Waiver Requests (DFARS Case 2013-D006)

BY: LUKE MANCINI

Over the past year, DoD has experienced a "significant increase" in the number of requests for either waiver or reduction of rental charges for use of Government property on work for foreign governments or international organizations. Until now, the Defense Security Cooperation Agency (DSCA) has been tasked with approving these waivers/reductions, even though the DSCA has no involvement in such activities. To streamline this process, contracting officers are now vested with the authority to approve such waivers and reductions without additional review and approval from the DSCA. The final rule was effective as of October 31, 2013.

Final Rule: New Designated Country—Croatia (DFARS Case 2013-D031)

BY: JOAN BERGHANE

On October 31, 2013, the DFARS was amended to identify Croatia as a new designated country under the World Trade Organization Government Procurement Agreement (WTO GPA). Croatia joined the European Union, which is a party to the WTO GPA, on July 1, 2013. The amendment includes Croatia among the list of permitted designated countries as it relates to the procurements involving the Trade Agreement Act and photovoltaic devices.

Final Rule: New Free Trade Agreement—Panama (DFARS Case 2013-D044)

BY: JOAN BERGHANE

On October 31, 2013, the DFARS was amended to adopt, as final with changes, a previously published interim rule to implement the United States–Panama Trade Promotion Agreement. The free trade agreement provides for the procurement and mutually non-discriminatory treatment of eligible products and services from Panama.

Proposed Rule: Domestically Nonavailable Articles—Elimination of DoD-Unique List (DFARS Case 2013-D020)

BY: HOMER WINTER

On December 6, 2013, DoD proposed a rule that, if finalized, would eliminate DoD-unique list of nonavailable articles included in DFARS Section 225.104. The section of the DFARS would be removed in its entirety, as the articles listed are either available domestically pursuant to the Buy American statute (41 U.S.C. 8302(a)) or are no longer procured by DoD. Comments to the proposed rule are due by February 4, 2014.

Proposed Rule: Application of Certain Clauses to Acquisitions of Commercial Items (DFARS Case 2013–D035)

BY: JOAN BERGHANE

DoD is proposing to revise DFARS Part 212, "Acquisition of Commercial Items," to clarify the applicability of DFARS clauses 252.211–7008, "Use of Government-Assigned Serial Numbers," and 252.232–7006, "Wide Area WorkFlow Payment Instructions," to acquisitions of commercial items by adding them to the list at 212.301(f) and revising the clause prescriptions to require their inclusion in solicitations and contracts for acquisitions of commercial items using FAR Part 12 procedures. Comments on the December 6, 2013, proposed rule must be submitted by February 4, 2014.

U.S. GOVERNMENT ACCOUNTABILITY OFFICE REPORTS

Reverse Auctions: Guidance Is Needed to Maximize Competition and Achieve Cost Savings (GAO Report GAO-14-108)

BY: HOMER WINTER

Reverse auctions vary from traditional auctions in that the roles of buyers and sellers are reversed. Since sellers compete to provide the lowest price and/or highest-value offer to a buyer, reverse auctions are often viewed as an effective means to increase competition and potentially reduce cost. Published by the GAO on December 9, 2013, the report Reverse Auctions: Guidance Is Needed to Maximize Competition and Achieve Cost Savings examines how Federal agencies currently use reverse auctions and discusses how to maximize their benefits going forward.

Congress asked GAO to explore the current use and conduct of reverse auctions, trends in the use of reverse auctions, and the extent to which potential benefits are being maximized. Prior to conducting its study, GAO identified five agencies that conduct roughly 70 percent of all reverse auctions: the Departments of the Army, Homeland Security, the Interior, and Veterans Affairs, and the Defense Logistics Agency (DLA). GAO used data collected from these agencies and from interviews to gather information and insight into the use of reverse auctions. Since DLA only collected summary-level data, GAO focused its efforts on the other four Federal agencies.

Based on the data and interviews, GAO discovered the use

of reverse auctions grew steadily between FY2008 and FY2012. During this time period, reverse auctions were largely used for the acquisition of FAR Part 12 commercial items and services, with the typical contract resulting in awards less than $150,000 to small businesses.

Although reverse auctions are used more frequently and may result in increased competition, GAO learned that only one bidder participated in over one-third of FY2012 reverse auctions. Additionally, GAO identified some instances in which Federal agencies were paying two fees to the reverse auction contractor as a result of obtaining items from preexisting contracts. GAO suggests there is still some unfamiliarity with reverse auction fees and how reverse auctions are to be conducted, since the FAR does not provide uniform policies or procedures for their use. GAO recommends that OMB consider amending the FAR to provide uniform guidance and clarify agencies' use of reverse auctions.

GAO Bid Protest Annual Report to Congress for Fiscal Year 2013 (GAO-14-276SP)

BY: BRYANT LE

The GAO annually reports to Congress a summary of its bid protest activity. Per the requirements of the Competition in Contracting Act (CICA), the GAO must report each instance where a Government agency did not fully implement a recommendation made by the GAO in connection with a bid protest decision.

In its report for FY 2013, the GAO discloses data regarding bid protest filings and, for the first time, the most prevalent grounds for the GAO to sustain protests. Below is a chart of bid protest statistics for the previous two fiscal years and a summary of the FY 2013 report.

	FY 2013	FY 2012
Cases Filed	2,429 (down 2%)	2,475 (up 5%)
Cases Closed	2,538	2,495
Merit (Sustain + Deny) Decisions	509	570
Number of Sustains	87	106
Sustain Rate	17%	19%
Effectiveness Rate	43%	42%
ADR (cases used)	145	106
ADR Success Rate	86%	80%
Hearings	3.36% (31 cases)	6.17% (56 cases)

Most Prevalent Grounds for Sustaining Protests

For FY 2013, Congress implemented the requirement for the GAO to report the most prevalent grounds for sustaining protests during the preceding year. Accordingly, for the first time, the GAO disclosed this information in its annual report. In FY 2013, the GAO sustained 87 of 509 (17 percent) protests that went to decision. The most prevalent basis for the sustained protest decisions were:

1. Failure to follow the solicitation evaluation criteria
2. Inadequate documentation of the record
3. Unequal treatment of offerors
4. Unreasonable price or cost evaluation

Not surprisingly, the aforementioned bases are procedural in nature and relatively less subjective (as compared to sustaining a protest on a technical evaluation basis). However, the GAO notes that agencies took voluntary corrective action for "a significant number of protests" filed with the GAO in response to protests. This is a positive sign for both contractors and the U.S. Government, as it reflects the effectiveness of the protest system in providing resolution without having the parties endure a protest process all the way through to a GAO decision.

Agency Did Not Fully Implement GAO Decision

In its report, the GAO summarized two instances

where an agency did not fully implement the office's recommendation. One case involved the Department of Housing and Urban Development (HUD). Specifically, the GAO recommended HUD cancel its notice of funding availability (NOFA) instrument, which would result in the issuance of a cooperative agreement to solicit contract administration services and issue an instrument that would instead result in a contract award. Referring to the Federal Grant and Cooperative Agreements Act (FGCAA), the GAO contended that the solicited contract administration services solely and directly benefit HUD (i.e., the U.S. Government) and accordingly, HUD should use a procurement contract.

Another instance involved the Department of Veterans Affairs (VA). The VA's use of the General Service Administration (GSA) FSS procedures without considering whether "two or more service-disabled veteran-owned small businesses or veteran-owned small business concerns were capable of meeting the agency's requirements at a reasonable price" conflicted with the Veterans Benefits, Health Care, and Information Technology Act of 2006.

Decline in Number of Protests Filed

The significant number of voluntary corrective actions is a notable statistic to ponder when analyzing the decline in the number of protests filed with the GAO during FY 2013, albeit a small percentage decline (2 percent). As a point of contrast, the previous four fiscal years had year-over-year increases in bid protests filed.

In a recent interview with Federal News Radio, Dan Gordon, the associate dean for Government Procurement Law at George Washington University Law School, stated that "the effectiveness rate (considers voluntary corrective actions), which increased by 1% relative to the previous three fiscal years, may help explain the decline in the number of protests filed." Though anecdotal, Gordon poses a possibility that the decline in cases filed may be a result of voluntary corrective actions where the case does not go through the full protest process to a GAO sustain/deny decision. Therefore, the GAO dismissed the protest; yet the protestor does not ultimately receive the award. Gordon is researching "what happens to contractors when the agency agrees to take corrective action instead of going through the bid protest process." He expects to finalize his research at some point this year. It will be interesting to see his results and whether the trend for FY 2014 year will be consistent.

DEPARTMENT OF DEFENSE – OFFICE OF INSPECTOR GENERAL (DOD OIG) REPORTS

Missile Defense Agency and Defense Microelectronics Activity Use of Cost-Reimbursement Contracts (DODIG-2014-011)

BY: BRYANT LE

In its November 22, 2013, report, the DoD OIG summarized its latest findings and recommendations for the use of cost reimbursement contracts. Specifically in the report, which is the third in an ongoing series of reviews, the DoD OIG reviewed the use of cost-reimbursement contracts by the Missile Defense Agency (MDA) and Defense Microelectronics Activity (DMEA).

The DoD OIG assessed whether MDA and DMEA adhered to the FAR requirements including:

- Approval by a person at least one level above the contracting officer (CO)
- Justification of the selection of a cost-reimbursable contract
- How requirements under the contract could be transitioned to a firm-fixed-price (FFP) contract in the future
- Government resources available to monitor the contract
- Adequacy of a contractor's accounting system at the time of contract award

The DoD OIG determined that these agencies did not consistently adhere to the FAR requirements for approximately 82 percent of the contracts reviewed. However, no intentional misclassifications of cost-reimbursement contracts as FFP were identified during the review.

Based on its findings, the DoD OIG recommended guidance and training courses on the FAR requirements related to cost-reimbursement contracts, improved procedures for CO approval of cost-reimbursement contracts, and development of guidance for contracting personnel around documentation of contracts precluded from issuance as an FFP contract.

Contractors are likely to continue to be impacted by Government's ongoing scrutiny of contract type determinations. Several agencies have continued to shift away from the use of cost-reimbursement contracts. As a result, contractors are left facing the challenges of managing the impact of the transition to business unit and program margins. In addition, contractors without approved accounting systems are facing increased audit and scrutiny of their systems.

U.S. Army Corps of Engineers Transatlantic District-North Needs to Improve Oversight of Construction Contractors in Afghanistan (DODOIG-2014-010)

BY: RYAN BYRD

On November 22, 2013, the DoD OIG issued an audit report on the oversight of U.S. Army Corps of Engineers (USACE) construction contractors in Afghanistan. The objective of the audit was to assess whether the USACE was properly monitoring contractor performance and adequately performing quality assurance (QA) oversight responsibilities in Afghanistan in accordance with the FAR.

FAR Subpart 46.4, "Government Contract Quality Assurance," states that Government contract QA shall be performed as necessary to determine that the supplies or services conform to contract requirements. The audit determined that oversight was not conducted in accordance with the FAR and USACE guidance. The DoD OIG specifically included the following findings in its report:

1. When projects were initiated, area and resident engineers did not provide project engineers and construction representatives with a Statement of Understanding and Compliance
2. Project engineers did not always follow contract oversight responsibilities
3. Project engineers worked with incomplete contractors' quality controls plans
4. Project engineers did not prepare QA plans
5. Project engineers could not substantiate that contractors fully executed the three-phase inspection process
6. USACE Transatlantic District-North technical inspections of contractors' construction efforts were limited

These findings result from the QA process being a secondary priority to project completion. As a result, there is an increased risk that completed projects may not meet contract requirements.

USACE responded to the audit findings by stating that they "will emphasize the requirements" and that "follow up would occur during USACE in-country visits."

Contractors performing construction contracts in Afghanistan for the USACE should be aware that additional monitoring and inspections are likely as result of these audit findings, and should ensure QA processes and plans are in place and well documented.

Hotline Allegation Regarding the Follow-up Audit of a Contractor's Material Management and Accounting System (DODIG-2014-002)

BY: KAYLA SEE

The DoD OIG reviewed a DoD Hotline complaint regarding a follow-up audit of a contractor's Material Management and Accounting System (MMAS) audit. The complainant alleged that a DCAA auditor who performed a follow-up audit of a major DoD contractor's correction of MMAS deficiencies had established several outstanding deficiencies as being corrected without obtaining sufficient evidence to support these decisions. The complainant also alleged the DCAA auditor reported the entire MMAS system as adequate when two deficiencies were known not to have been corrected.

The DoD OIG found that, of the 28 deficiencies reported by DCAA as having been corrected, the auditor failed to obtain sufficient evidence for 10 of the corrective actions.

The DoD OIG recommended that the DCAA rescind the MMAS follow-up audit report as a result of the auditor's failure to obtain sufficient evidence to support the audit opinion. It was also recommended that DCAA instruct the CO to not rely on the report results and to initiate a full audit of the contractor's MMAS. The DCAA agreed with the recommendations.

However, a more pertinent outcome of the DoD OIG's report is the DCAA's willingness to rescind an MMAS adequacy determination pre-dating the business system revisions of 2011 and conducting a new, complete MMAS audit in its entirety. While in this case, the rescinding of the prior audit report was a result of the DoD OIG review and recommendations, nothing within the DCAA's existing policy would preclude similar action for other contractors who are found not to have adequately remediated prior business system deficiencies.

The DoD OIG report should serve as a reminder to contractors that business system issues can arise even when systems are previously determined to be approved. As such, contractors should proactively and periodically monitor their systems to business system requirements. As part of these reviews, contractors should review the efficacy of processes and controls within their systems.

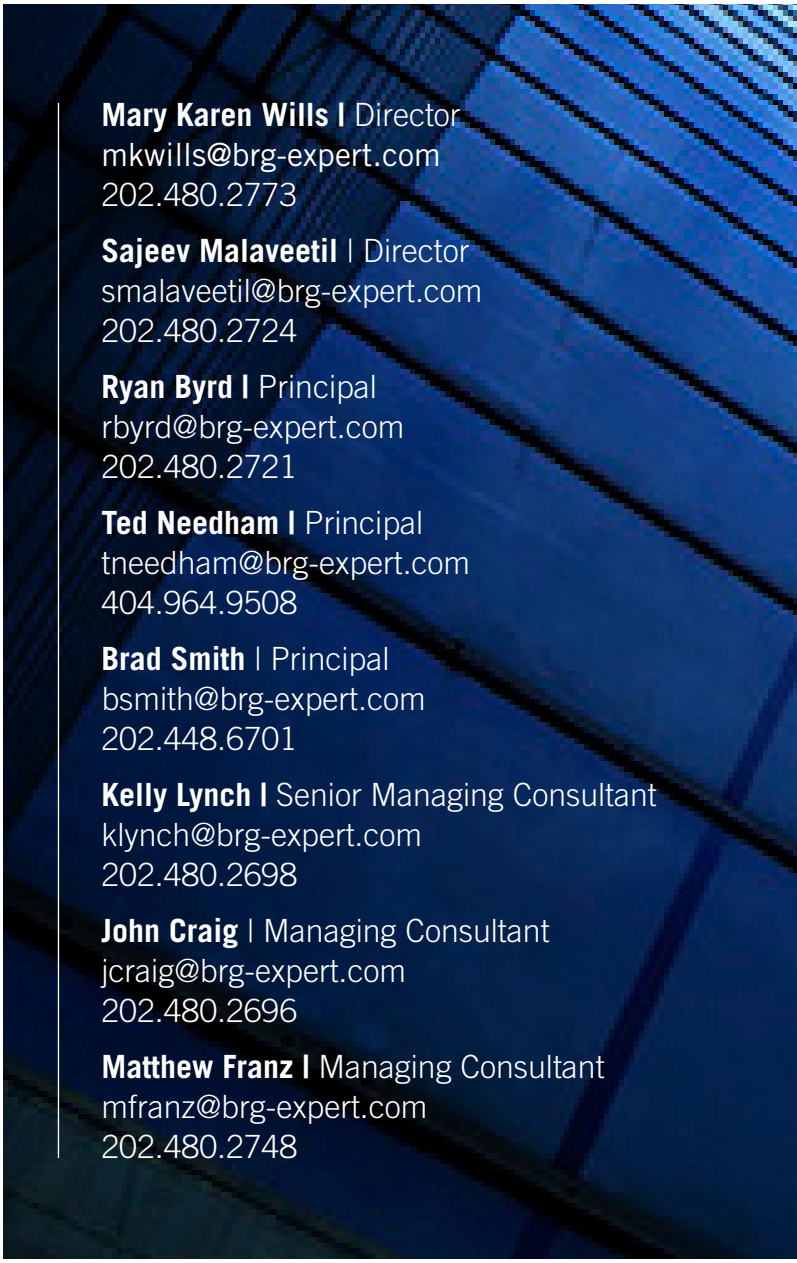
BRG'S GOVERNMENT CONTRACT BLOG:

We first reported many of the items in this edition of the GovCon Research Report on our Government Contract blog. Please follow us at www.brggovconinsight.com for up-to-date information on Government Contract matters.

IN SUMMARY

If you have questions about specific items in this publication and would like to know more about how they apply to you, please feel free to contact one of our experts.

For general questions, please contact Joan Berghane at jberghane@brg-expert.com or 202-480-2697.



Mary Karen Wills I Director
mkwills@brg-expert.com
202.480.2773

Sajeev Malaveetil I Director
smalaveetil@brg-expert.com
202.480.2724

Ryan Byrd I Principal
rbyrd@brg-expert.com
202.480.2721

Ted Needham I Principal
tneedham@brg-expert.com
404.964.9508

Brad Smith I Principal
bsmith@brg-expert.com
202.448.6701

Kelly Lynch I Senior Managing Consultant
klynch@brg-expert.com
202.480.2698

John Craig I Managing Consultant
jcraig@brg-expert.com
202.480.2696

Matthew Franz I Managing Consultant
mfranz@brg-expert.com
202.480.2748

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