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# Essential Accounting Updates for Federal Contractors

March 20, 2015

By: Barbara Morgan, Steve Swales, & Aaron Solar

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# Awards / Accolades / Affiliations



## *INSIDE Public Accounting Top 100*

Once again, Aronson has earned a spot in the top 100 of this prestigious list, released by *INSIDE Public Accounting*. This is the longest running, most comprehensive and accurate independent analysis focusing on management and operations of America's large local, regional and national firms.

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## *Accounting Today Top Firm*

In 2013, Aronson was once again named to *Accounting Today's* list of the top 100 firms in the country. *Accounting Today* is a leading provider of online business news for the tax and accounting community.

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## *Washington Business Journal Best Places to Work*

Aronson has been recognized five times as one of the Metro area's "Best Places to Work." The award recognizes a company's achievements in creating a positive work environment that attracts and retains employees through a combination of employee satisfaction, working conditions and company culture.

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## *Washington Business Journal Top 25*

Aronson is ranked #12 on the *Washington Business Journal's* Top 25 Accounting Firms in the DC Metropolitan area.

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## *Montgomery County Chamber Corporate Social Responsibility Award*

In 2010, Aronson was honored to receive the MCCC's Corporate Social Responsibility Award based on the depth and breadth of the company's energetic commitment to support young people, in the areas of education, housing and health.

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## *The Gazette of Politics & Business Exceptional 53 Business Award*

In 2012, Aronson received the PB53 award for the third year in a row. The program acknowledges the top businesses and organizations in Maryland based on criteria that includes the company's annual revenue, employee growth, noteworthy product or service innovations, community service efforts and more.





# Stephen T. Swales – *Partner*

Stephen T. Swales, serves as a partner in Aronson LLC's Government Contract Services Group and Audit and Accounting Group. He has spent over 20 years in the industry, serving clients that include government contracting and nonprofit associations. Steve specializes in systems implementations for government contractors (Deltek), government cost accounting standards, customized software interfaces, audit, accounting, tax, and general consulting. He is also a technical specialist, having extensive experience with various application software, programming languages, and operating systems. As an expert in the field, he has made various presentations to trade organizations on topics related to his industry expertise. Steve earned his bachelor's degree in accounting from the University of Maryland in 1987. Upon passing the Certified Public Accounting exam, Steve earned the Elijah Watts Sell Award presented to the CPA candidates who attain the highest combined grades when taking all four sections of the Uniform Certified Public Accountant Examination at one administration. Steve is an active member of AICPA and MACPA.





# Barbara W. Morgan - *Director*

Barbara Morgan serves as a director in the Outsourcing practice of Aronson's Government Contract Services Group. She is responsible for implementing and integrating new clients and managing the outsourcing staff. She has over 25 years of experience in both public and private accounting. Prior to joining Aronson LLC, she was controller and principal accounting officer for a publicly traded company in the technology services industry.



## Licenses & Certifications:

- CPA





# Aaron Solar – *Senior Technology Consultant*

Aaron Solar is a senior technical consultant in the government systems practice area of Aronson's Government Contract Services Group. He provides technical consulting services in support of Deltek GCS Premier software and Cognos Impromptu for clients that include small and medium-sized federal contractors.

Aaron received a bachelor's degree in economics from the University of New Hampshire and is an active member of the Central Maryland chapter of the AFCEA, where he serves as the VP of Technology. He also volunteers for a local animal rescue organization.





# AM Agenda

- Introduction to the FAR
- Acquisition Methods
- Types of Contracts
- Contract Clauses with special significance
- Special Designations
- Adequate Accounting Systems
- Policies and Procedures





# PM Agenda

- Direct Vs. Indirect Costs
- Unallowable Costs
- Computation of Indirect Rates
- Subcontractor vs. Prime Contractor
- Types of Government Audits
- Key Performance Indicators
- Best Practices



# Introduction to the FAR

Presented By: Steve Swales



# Defense Contract Management Agency (DCMA) – DCMA.MIL

- Vision – One team, one voice delivering global acquisition insight that matters.



# Defense Contract Management Agency (DCMA) – DCMA.MIL

- Vision – One team, one voice delivering global acquisition insight that matters.
- Mission – independent eyes and ears of DOD and its partners, delivering actionable acquisition insight from the factory floor to the front ...around the world.



# Defense Contract Management Agency (DCMA) – DCMA.MIL

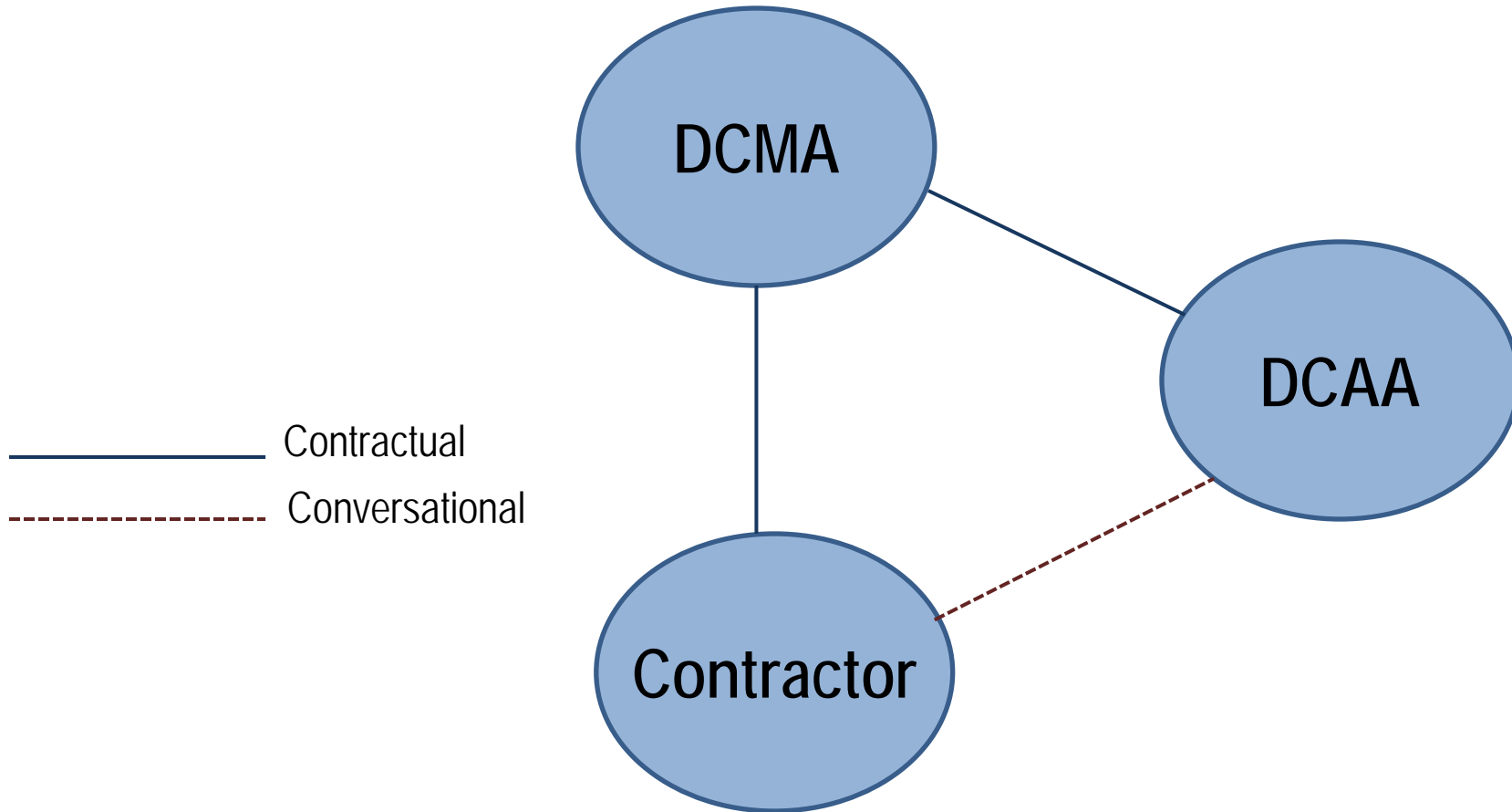
- Responsibilities
  - Before contract award –
    - Provide advice and information to construct effective solicitations
    - Identify potential risks
    - Select most capable contractors
    - Let contracts that meet the needs of DoD, Federal, and allied Govt agencies



# Defense Contract Management Agency (DCMA) – DCMA.MIL

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  - Before contract award –
    - Provide advice and information to construct effective solicitations
    - Identify potential risks
    - Select most capable contractors
    - Let contracts that meet the needs of DoD, Federal, and allied Govt agencies
  - After contract award
    - Monitor contractor performance and management systems
    - Ensure that cost, product performance, and delivery schedules are compliant

# Relationships of DCMA, Contractor, and DCAA





# Defense Contract Management Agency (DCMA) – DCMA.MIL



- **Vision** – Dedicated professionals working together to deliver top-quality audit services to support the Department and warfighter, and to protect the taxpayer's interest

# Defense Contract Management Agency (DCMA) – DCMA.MIL



- **Vision** – Dedicated professionals working together to deliver top-quality audit services to support the Department and warfighter, and to protect the taxpayer's interest
- **Mission** - Defense Contract Audit Agency (DCAA), while serving the public interest as its primary customer, shall perform all necessary contract audits for the Department of Defense (DoD) and provide accounting and financial advisory services regarding contracts and subcontracts to all DoD components responsible for procurement and contract administration. These services shall be provided in connection with negotiation, administration, and settlement of contracts and subcontracts to ensure taxpayer dollars are spent on fair and reasonable contract prices. DCAA shall provide contract audit services to other Federal agencies as appropriate.



# Defense Contract Audit Agency (DCAA) – DCAA.MIL

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## DCAA Major Areas of Emphasis

- Business systems



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## DCAA Major Areas of Emphasis

- Business systems
- Management policies and procedures
- Accuracy and reasonableness of contractors'
  - Forward pricing agreement
  - Incurred cost submission

# Defense Contract Audit Agency (DCAA) – DCAA.MIL



## DCAA Major Areas of Emphasis

- Business systems
- Management policies and procedures
- Accuracy and reasonableness of contractors'
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  - Incurred cost submission
- Adequacy and reliability of records and accounting systems

# Defense Contract Audit Agency (DCAA) – DCAA.MIL



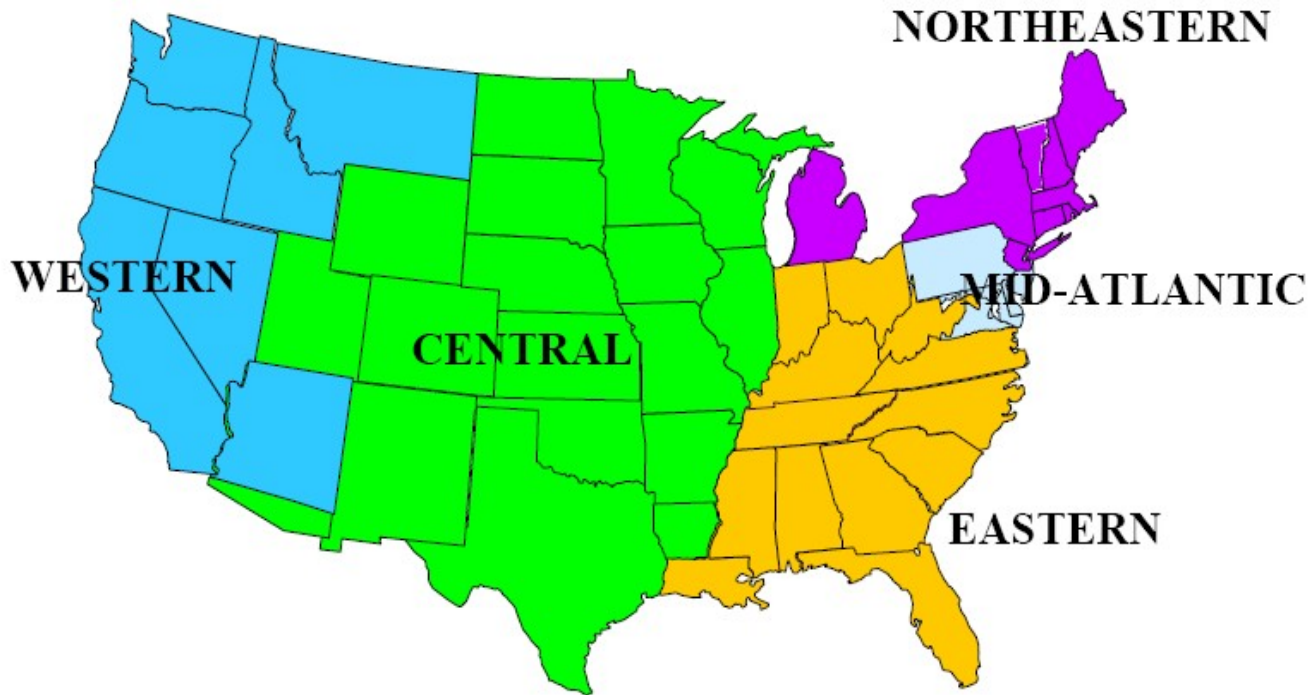
## DCAA Major Areas of Emphasis

- Business systems
- Management policies and procedures
- Accuracy and reasonableness of contractors'
  - Forward pricing agreement
  - Incurred cost submission
- Adequacy and reliability of records and accounting systems
- Contractor compliance with contractual provisions such as the Cost Principles



# Map

## DCAA Regional Boundaries



- Western Region includes Alaska, Hawaii, the Pacific and the Far East
- Eastern Region includes the Caribbean, Central and South America
- Northeast Region includes Africa, Europe, the Middle East, and Afghanistan



# Regional Telephone Numbers

Table 1. Regional Telephone Numbers.

Region	Telephone Number
Central Region (Irving, TX)	(972) 652-3600
Eastern Region (Smyrna, GA)	(770) 319-4400
Mid-Atlantic Region (Philadelphia, PA)	(215) 597-7453
Northeastern Region (Lowell, MA)	(978) 551-9710
Western Region (La Mirada, CA)	(714) 228-7003



# Federal Acquisition Regulations (FAR)

## FAR 1.101 – Purpose

### Federal Acquisition Regulations System

- **Purpose**
  - codify and publish uniform policies and procedures for acquisition
- **Components of System**
  - Federal Acquisition Regulations (FAR)
  - Agency Acquisition regulations



# Federal Acquisition Regulations (FAR)

## FAR 1.101 – Principles

- Vision
  - Deliver best products and services
  - On a timely basis
  - In the public's interest



# Federal Acquisition Regulations (FAR)

## FAR 1.101 – Principles

- **Vision**
  - Deliver best products and services
  - On a timely basis
  - In the public's interest
- **Objectives**
  - Maximize use of commercial and product services
  - Use contractors with a track record of success
    - Past Performance
    - Current superior ability
  - Promote competition
  - Minimize administrative costs
  - Operate with Integrity, fairness, and openness
  - Fulfill objectives of public policy



# Acquisition Methods

Presented By: Steve Swales



# Government Acquisition Methods

- Simplified Acquisition
- Sealed Bid
- By Negotiation
- Consolidated Purchasing Vehicles



# Simplified Acquisition Methods (FAR part 13)



- Purpose: promote efficiency and reduce admin costs
- Purchases under \$150,000
- Reserved for small businesses (provided 2 or more bidders)
- Must advertise purchases in excess \$30,000  
([www.fedbizopps.gov](http://www.fedbizopps.gov))
- Micro purchases – less than \$3,000 (70 % of Govt Purchases)
  - Not reserved for small businesses
  - Competition not required
  - Used with Credit Cards



# Sealed Bid (FAR part 14)

- Used for purchases that are specific, clear, and complete
- Invitation For Bid (IFB) includes
  - Product or service description
  - Bid instructions
  - Conditions (delivery, payment, etc.)
- [www.fbo.gov](http://www.fbo.gov)
- Sealed bids open in a public forum and awarded to lowest responsive offeror
- Contract will be awarded as a Firm Fixed Price



# By Negotiation (FAR part 15)

- Any award other than sealed bid
- Used for highly technical products and services
- Usually used for acquisitions in excess of \$150,000
- Used for sole source and competitive awards
- Trade off procedures for evaluation mean the award will not always go to the lowest offer
- Request for Proposals (RFP's) and Request For Quotations (RFQ's)
- [www.fbo.gov](http://www.fbo.gov)



# Consolidated Purchasing Vehicles

- Addresses common purchasing needs of multiple agencies
- Utilized to achieve economies of scale in administrative costs of purchasing
- Negotiated by government with multiple vendors
- GSA Schedules and Government Wide Acquisition Contracts (G-WAC's)



# Types of Contracts

Presented By: Steve Swales



# Contract Types

- Fixed Price
- Time & Materials
- Cost Reimbursement
- Indefinite Delivery/Indefinite Quantity (IDIQ)



# Fixed Price Contracts

- Used when performance risk is low
- Fixed Price Variations -
  - Firm (FAR 16.202) – no adjustment to price
  - Economic adjustment (FAR 16.203) – used to offset cost volatility
  - Incentive (FAR 16.204) – ultimate price determined by a formula based on
    - Final costs
    - Some performance metrics
- Contractor assumes risk of cost overruns
- DCAA work done pre-award



# Time & Material Contracts (FAR 16.600's)



- Not a fixed price contract (FAR 16.600)
- Used when Contracting Officer (CO) declares that no other contract type is acceptable
- Labor hours billed @ fixed hourly rates including fee plus direct and indirect costs
- Materials are at cost
- Labor hour contract – a T&M contract where the contractor delivers no materials



# Cost Plus Contracts (FAR 16.300's)

- Used when performance risks are high
- Variations –
  - Cost sharing – No fee and less than 100% of costs
  - Cost Plus Fixed Fee – Fee stated at contract award
  - Cost Plus Incentive Fee – Fee adjusted based on formula involving actual costs
  - Cost Plus Award Fee – Fee adjusted by judgmental evaluation of contractor performance
- Government assumes risk of cost overruns
- Requires contractor to have an approved accounting system
- DCAA work done post-award



# IDIQ Contracts

## Indefinite Delivery/Indefinite Quantity (IDIQ) Contracts (FAR 16.500's)

- Variations -
  - Definite quantity
  - Requirements
  - Indefinite quantity
- Used to maintain Govt stock at minimum levels



# Contract Clauses with Special Significance

Presented By: Steve Swales



# FAR 52.216-7 – Cost and Payments Clause

- Defines costs that can be billed and frequency
- Establishes the requirement to prepare an incurred cost submission
- Establishes DCAA's rights to audit costs
- Provides for the Quick Close Out Procedures (FAR 42.708(a))



# FAR 52.232-22 – Limitations of Funds

- Requires the contractor to make a written notification
  - 60 days in advance of reaching....
  - 75 % of funded contract amount
- This protects the contractor's right to stop work at the funded value



# FAR 52.242-3 – Penalties for Unallowable Costs

- Establishes Govt right to assess and collect interest and penalties on unallowable costs
- Interest runs from the time an unallowable cost was paid
- Penalty for claiming expressly unallowable costs is one (1) times costs
- Penalty for claiming any cost previously deemed unallowable is three (3) times costs



# Termination Clauses

- FAR 52.249-1 – Termination for Convenience (Fixed Price)
- FAR 52.249-6 – Termination (Cost Plus)
  - For Convenience
  - For Cause





# Special Designations

Presented By: Steve Swales



# Special Designations

- Part of small business programs (FAR 19) designed to promote economic growth
- Agencies set specific goals to award contracts to these categories
  - 8A – Economically Disadvantaged (FAR 19.800's)
  - Historically Underutilized Business Zone (HUBZone) (FAR 19.1300's)
  - Service Disabled Veteran Owned Businesses (FAR 19.1400's)
  - Women Owned Small Businesses (FAR 19.1500's)



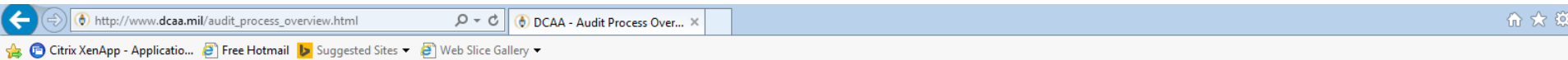
# Special Designations

Rules of the program dictate the business owner qualifying for the classification:

- Must own more than 50% of the company and have full decision making authority;
- Actively manage both the overall plan and day to day activities of the company;
- Be the highest ranking officer and the most highly paid employee;
- And have the experience, technical ability and managerial skills to effectively run the business.



# DCAA Website – Guide for Contractors



ABOUT DCAA

GUIDANCE

CHECKLISTS AND TOOLS

LOCATOR

CONTACT US

Request An Audit

**Audit Process Overview – Information For Contractors**

Directory Of Audit Programs

Useful information to assist contractors understand DCAA audit processes

**CAM – Contract Audit Manual**

Information for Contractors

**MRDs – Audit Guidance Memos**

A helpful guide that provides an overview of the types of audits DCAA conducts, links to checklists, and what you can expect in a DCAA audit.

**CAS – Cost Accounting Standards**

• Information for Contractors **FAR – Federal Acquisition Regulation**

**Help for Small Business FAR Cost Principles Guide**

DCAA Small Business Focal Point (703) 767-2271

**DFARS – Defense Federal Acquisition Regulation Supplement**

DCAA-OAL-Small Business Focal Point@dcaa.mil

**GAGAS/Yellow Book – Generally Accepted Government Auditing Standards**

In addition to the information for Contractors guide, DCAA offers targeted information to assist with audit issues that relate to small businesses. Access presentations below for help on specific topics important for smaller contractors:

**FAQs**

• Accounting System Requirements



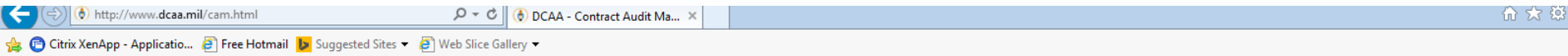


# DCAA Website - FAR

The screenshot shows a web browser window with the URL <http://www.dcaa.mil/far.html>. The browser's address bar and tabs are visible. The website's header includes the DCAA logo (Defense Contract Audit Agency) and navigation links: ABOUT DCAA, GUIDANCE, CHECKLISTS AND TOOLS, LOCATOR, and CONTACT US. A search bar is located in the top right corner. The main content area features a large image of a spiral-bound notebook on a blue surface. To the right of the image, a dropdown menu is open under the 'GUIDANCE' link, listing various resources: Request An Audit, Audit Process Overview – Information For Contractors, Directory Of Audit Programs, CAM – Contract Audit Manual, MRDs – Audit Guidance Memos, CAS – Cost Accounting Standards, FAR – Federal Acquisition Regulation (highlighted in orange), FAR Cost Principles Guide, DFARS – Defense Federal Acquisition Regulation Supplement, GAGAS/Yellow Book – Generally Accepted Government Auditing Standards, and FAQs.



# DCAA Website – Contract Audit Manual



- ABOUT DCAA
- GUIDANCE
- CHECKLISTS AND TOOLS
- LOCATOR
- CONTACT US

CAREERS





## CAM – CONTRACT AUDIT MANUAL

As of January 2013

We have provided

The most current version of CAM is provided, by chapter, in electronic format below. User comments/suggestions are welcome; refer to Section 0-007 of the CAM for details. Current audit guidance not yet incorporated into the CAM can be found on the MRDs - Audit Guidance Memos page.

- Request An Audit
- Audit Process Overview – Information For Contractors
- Directory Of Audit Programs
- CAM – Contract Audit Manual**
- MRDs – Audit Guidance Memos
- CAS – Cost Accounting Standards
- FAR – Federal Acquisition Regulation
- FAR Cost Principles Guide
- DFARS – Defense Federal Acquisition Regulation Supplement
- GAGAS/Yellow Book – Generally Accepted Government Auditing Standards
- FAQs

Contents	
Chapter	Table of Contents
Foreword	DCAA Contract Audit Manual - Foreword
TOC	Table of Contents (Mar 2015)



http://www.dcaa.mil/cam.html



# Adequate Accounting Systems

Presented By: Barbara Morgan

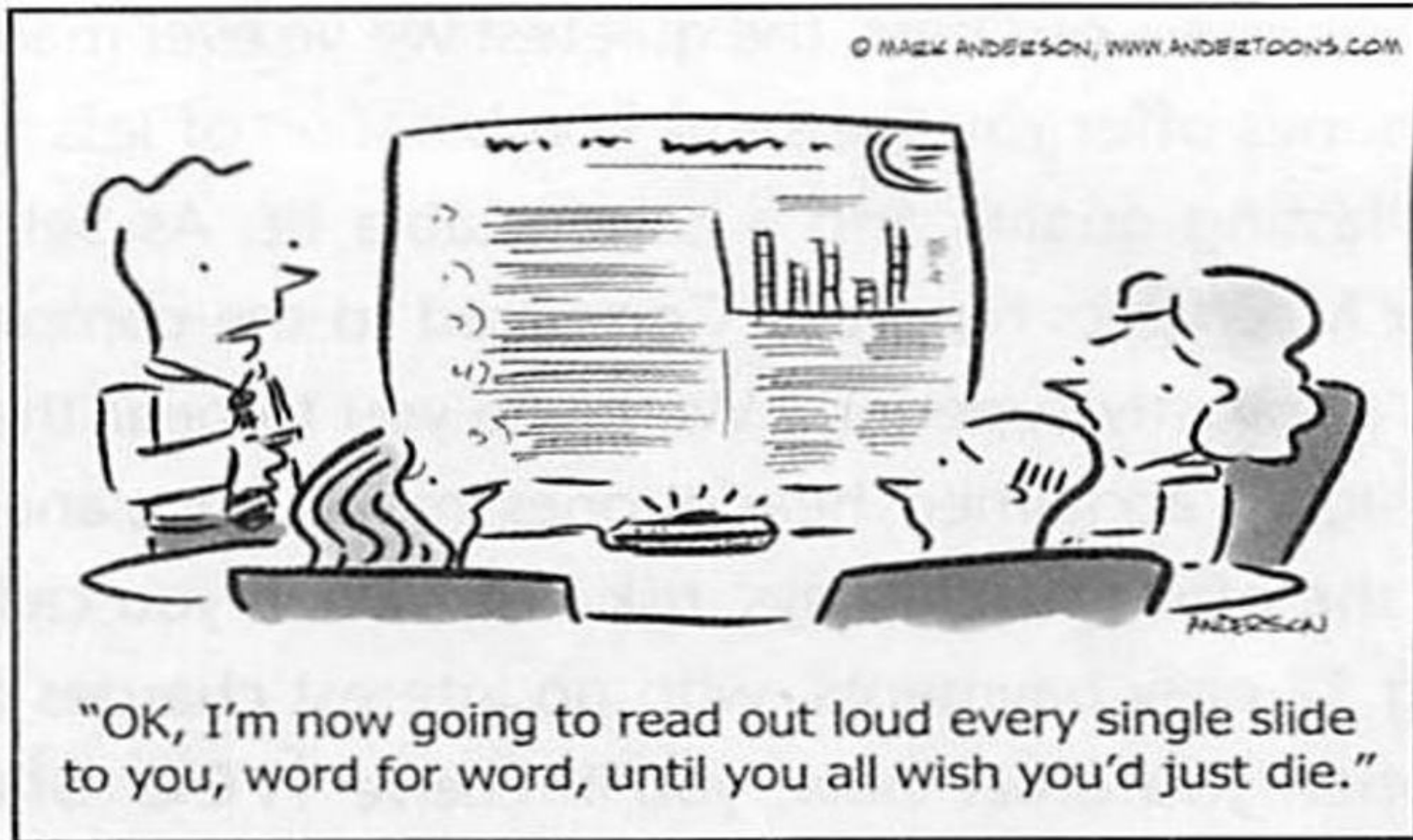
# Overview

- Government definition of “adequate accounting system”
- Specific attributes required
- Form SF 1408, assessment of a company’s systems.





# This is the Fun Part!





# DFARS Definition

“Accounting system” means the Contractor’s system or systems for accounting methods, procedures, and controls established to gather, record, classify, analyze, summarize, interpret, and present accurate and timely financial data for reporting in compliance with applicable laws, regulations, and management decisions, and may include subsystems for specific areas such as indirect and other direct costs, compensation, billing, labor, and general information technology.





# "Acceptable"

Acceptable accounting system means a system that complies with the criteria of this clause to provide reasonable assurance that ---

- Applicable laws and regulations are complied with;
- The accounting system and cost data are reliable;
- Risk of misallocations and mischarges are minimized; and
- Contract allocations and charges are consistent with billing procedures.



# What Does All of this Mean?

Your accounting “system” is much more than just your software.





# Required for All Contractors

- Accrual Basis and GAAP principles
- FAR Part 31, Contract Cost Principles
- CAS 401 Consistency – Estimating, Accumulating, Reporting
- CAS 402 Consistency – Allocating costs for the same purpose
- CAS 405 Unallowable Costs
- CAS 406 Cost Accounting Period

# CAS 401: Consistency in Estimating, Accumulating, and Reporting



## Consistent Application

Comparable transactions are treated alike to facilitate the preparation of reliable cost estimates (proposals) creating:

- an important basis for **financial control** over costs
- means for establishing **accountability for costs** in the manner agreed to by both parties at the time of contracting, and
- an improved basis for evaluating **estimating capabilities**.



# CAS 402 – Consistency in Allocating Costs

Ensure that each type of cost is allocated **only once** and **on only one basis** to any contract or other cost objective

## Fundamental requirement

- That all costs incurred for the same purpose, in like circumstances, are either direct costs only **or** indirect costs.





# CAS 405 – Accounting for Unallowable Costs

To facilitate the negotiation, audit, administration, and settlement of contracts.

- Identification of costs specifically described as unallowable
- Costs **expressly unallowable** or **mutually agreed to be unallowable**, including costs mutually agreed to be unallowable directly associated costs, shall be identified and excluded from any billing, claim, or proposal applicable to a Government contract





# CAS 406 - Cost Accounting Period

To provide criteria for selecting the **time periods** to be used as cost accounting periods for contract cost estimating, accumulating, and reporting.

- It will reduce the effects of variations in the flow of costs within each cost accounting period.
- It will also enhance objectivity, consistency, and verifiability and promote uniformity and comparability in contract cost measurements.



# When is an Accounting System Required?

- FAR 16.301(3) requires the contractor to maintain an adequate accounting system for determining costs applicable to the contract or order
  - Cost-reimbursement contracts
    - Cost
    - Cost-sharing
    - Cost-plus-incentive-fee
    - Cost-plus-award-fee
    - Cost-plus-fixed-fee
    - Cost-plus-incentive-fee
  - Fixed Price or Time & Materials contracts with cost reimbursable line items



# Accounting System Criteria

- Sound internal control environment, accounting framework, and organizational structure
- Proper segregation of direct from indirect costs
- Identification and accumulation of direct costs by contract
- Logical and consistent method for the accumulation and allocation of indirect costs to intermediate and final cost objectives
- Accumulation of costs under general ledger (GL) control
- Reconciliation of subsidiary cost ledgers and cost objectives to the general ledger
- Approval and documentation of adjusting entries



# Accounting System Criteria

- Mgmt. reviews and/or conducts internal audits to ensure compliance with P&P's
- Timekeeping system that identifies employees' labor by intermediate or final cost objective
- Labor distribution system that charges direct and indirect labor to the appropriate cost objective
- Interim determination of costs charged to a contract through posting of books of account
- Exclusion of unallowable costs based on FAR Part 31, and other contract provisions



# Accounting System Criteria

- Identification of costs by CLIN, ACRN, or other unit as defined by the contract
- Segregation of preproduction from production costs
- Cost accounting information related to:
  - Contract and funding values and limits
  - Indirect rate calculations
- Billings that can be reconciled for both current and cumulative amounts claimed
- Adequate data for use in pricing follow-on acquisitions
- Accounting practices in accordance with GAAP and CAS, if applicable



# "Sound Internal Control Environment"

- Expertise, awareness and understanding of the rules that apply to your company
- Are the right levels performing the right tasks?
- Segregation of duties
- Custody
- Authorization
- Record keeping and documentation
- Accountability
- Written codes of conduct to address ethical behavior
- Employee training



# “Under General Ledger Control”

- Accruals – Payroll, Subcontractors, Period Costs
- Approvals and documentation
- Reconciliations
  - Cash, Fixed Assets, Job Cost ledgers, Fixed Assets, Unbilled,
  - Billing – both current and cumulative
- System must be fully operational



# Direct vs. Indirect / Allowable vs. Unallowable

- Logical and consistent method
- Job Costing - accumulate costs by contract and by CLIN
- Cost Accounting – applying indirect costs to those contracts
- Calculation of indirect rates
- Excluding unallowable costs
- Separation of pre-production costs
- Consistency in billing, budgets and forward pricing





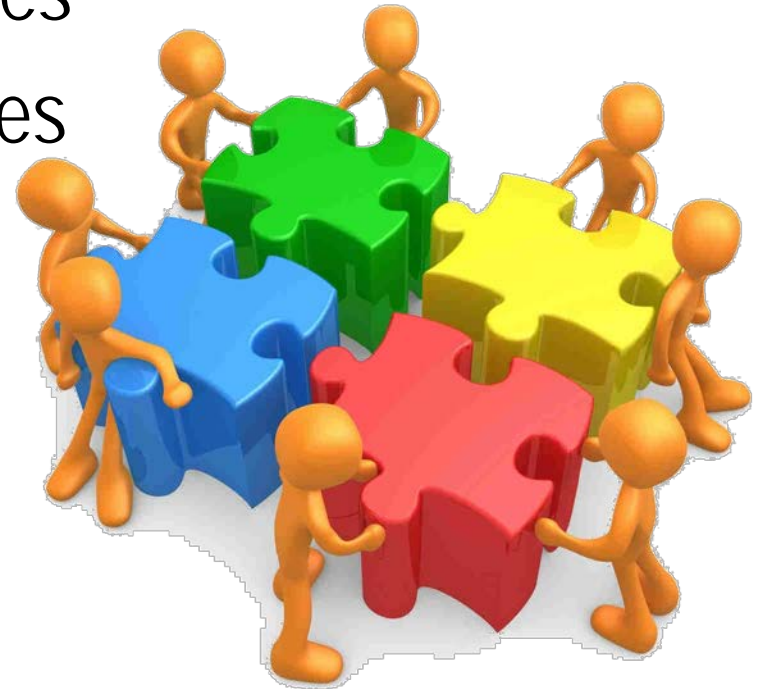
# Timekeeping and Labor Distribution

- Adequate timekeeping system that conforms to government standards
- Labor distribution to final cost objectives
- Reconciliation of Labor Costs



# Management Oversight

- Self-audit
- Adequate training of employees
- Written policies and procedures





# Form SF 1408

- Review of handout





# Policies and Procedures

Presented By: Barbara Morgan



# Why Have Policies and Procedures?

- Clearly communicate business rules and procedures
- Promote and facilitate efficient operations
- Help mitigate against fraud or misappropriation
- Required by an independent auditor
- Part of a due diligence package
- Required for government contracting



# Required & Recommended Policies

- Timekeeping
- Billing Procedures
- Direct vs. Indirect Costs
- Composition of Indirect Costs
- Travel
- Unallowable Costs
- Compensation and Bonus
- Fixed Assets
- Budgeting and Indirect Rate Management
- Employee Manual



# Required & Recommended Policies

- Contract Management/Contract Briefs
- Accounts Payable

If needed:

- Subcontractors
- Purchasing





# Policies and Procedures

- Each Policy and Procedure should explain:
  - Purpose
    - Control of costs
    - Compliance with regulations
  - Terminology
  - Responsibilities
  - Procedures to follow to ensure compliance
  - Employee Training
  - Self audit
- Must be compliant with company policies and procedures.







# Accounts Payable

- Who codes invoices? Are they properly trained?
- Who approves them?
- Who can add vendors?
- Who can issue or sign checks?
- Who reconciles the bank statement?
- Are vendors paid promptly?
- Do vendor invoices contain sufficient detail?
- What are your payment terms?





# Billing

- Does the output on your bills match your input? i.e. timesheets and payables
- Validate against contract totals, withholding, limitations, milestones or objectives
- Review for accuracy, exclusion of unallowable amounts, period of performance
- Who trains billing employees?
- Handling of subcontractor invoices?
- Copy kept by contracts manager?
- Calculation and review of unbilled direct or indirect costs.
- Government's overriding concern is that they are not overcharged.





# Compensation and Bonus

- Can be simple, but must be clear
- Bonus cannot be based on profit.
  - Based on company profit = unallowable
  - Based on employee performance = allowable
- How are owner's bonuses treated?





# Timekeeping

- Employees enter time daily
- Enter all time worked
- Review and approval by supervisors or management
- Process for changing timesheets
- Train your employees
- Treatment of overtime
- Handling of violations
- Self-auditing
- Make sure is consistent with your employee handbook

**Daily Time Sheet**  
Your Business Name

Name: Wavel Magic Corporation

\$100.00  
RATE/Hr

DET	NAME	PROFESSIONAL SERVICE	APPOINTMENT			TOTAL TIME	TOTAL FEE
			Start	Stop	Rate		
1	Fred Marvel	Consultation	5/11/2009 9:00	5/11/2009 9:15	0:15	\$25.00	
2	John Doe	Consultation	5/12/2009 8:30	5/12/2009 11:15	2:45	\$275.00	
3	Mattha Magic	Consultation	4 Hours	5/15/2009 9:00	5/15/2009 13:00	4:00	\$400.00
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# Travel and Per Diem

- Federal Travel Regulations (FTR)
- Joint Travel Regulations (JTR)
- Per Diem
- Lodging Per Diem
- MIE
- "Fly America"





# Direct vs. Indirect

**Purpose:** To ensures consistent charging of costs

- Explain and include chart of accounts
- Define "direct" and "indirect"
- Establishes and maintains procedures for charging costs
- Demonstrate your understanding of government contractor rules



# Unallowable Costs

**Purpose:** To ensure that unallowable costs are:

- Segregated
- Identified
- Excluded from costs

Costs can be expressly unallowable or specifically excluded per the contract.





# Description of Indirect Pools and Bases

- Define the indirect pools and the basis on which you allocate those costs
- Homogeneous cost groupings
- Defines procedures for:
  - Accurately budgeting indirect cost pools
  - Accurately estimating indirect bases
  - Controlling actual indirect expenses
  - Establishing and maintaining accurate indirect rates





# Most Important!

## Follow your own policies!





# Direct & Indirect Costs... and Pools!

Presented By: Aaron Solar



# Overview

- Direct vs. Indirect Costs
- Reasonable, Allocable, and Allowable concepts
- Unallowable Costs
- Indirect Rate Examples



# Direct vs Indirect Costs

- Per FAR 31.202/31.203...
- A direct cost is any cost that can be identified specifically with a particular final cost objective. No final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose in like circumstances have been included in any indirect cost pool to be allocated to that or any other final cost objective.
- An indirect cost is any cost not directly identified with a single, final cost objective, but identified with two or more final cost objectives or an intermediate cost objective. It is not subject to treatment as a direct cost.



# Direct Costs

- Labor directly related to a specific contract: software engineers, software developers, project managers, etc
- Non-Labor directly related to contract: materials, equipment, subs, consultants, travel, ODC's, Service Center Costs



# (Allowable) Indirect Costs

- Labor not directly related to a specific contract: executive management, IT, HR, accounting, contract managers, business development (non-bid/proposal), office admins, etc.
- Non-Labor not directly related to a specific contract: employee benefits, office rent, utilities, furniture/computer depreciation, etc.



# Indirect Cost Types

- **Fringe:** vacation cost accrual, holiday pay, jury duty/military/family leave, employer taxes (FICA/FUTA/SUTA), employer paid health insurance, workers comp insurance, bonus pool\*, employee morale\*\*
- **Overhead:** regional office rent & support, non-billable employee time\*, indirect PM time, non-billable travel, supports range of contracts but typically not all contracts
- **General & Administrative:** corporate office rent, utilities, executive staff, etc... costs of operating entire company not contract/division specific
- \*- Can fall under various pools, \*\* - Approaches DCAA 'gray area'



# Costs Under Various Pools/Gray Area

- Bonus Pools: Monthly accrual (consistently, for reasonableness) for on-contract employees can be deemed overhead, similar bonus pool could exist for office staff in G&A pool. Company wide bonus pool could exist in fringe as well!
- Rent & Related Costs (Utilities, Voice/Data, IT Equipment):
  - G&A only (only back office support staff)
  - Mix of G&A/OH (back office support AND direct billable employees at office)
  - Mix of G&A/OH/Direct (if allowed by contract, such as SCIF space)
  - Consider using Service Centers (more on that next!)
- Donuts: Costs labeled 'Employee Morale' are a bulls eye for DCAA. 6 years of donuts/bagels were later deemed unallowable & had to be reclassified





# Service Centers/Intermediate Pools

- Methodical means of allocating costs such as costs as percentage of headcount, square feet, etc.
  - We'll talk about Allocable Costs soon
- Rent allocation could be allocated based on square feet occupied by department or business unit
- Recruiting or HR costs could be allocated based on head count
- Provides a rational, reasonable means to allocate costs between direct & indirect, or across multiple indirect cost pools
- Some financial systems provide for somewhat automated calculation of service center costs
- Completely optional but provide a means to allocate costs based on rationale



# Material Handling/Subcontractor Pools

- Another way to manage indirect costs on material or subcontractor handling is via a Materials And Subcontractor Handling (MASH) Pool
- Pool Costs: subcontractor admin labor, purchasing labor
- Pool Base: costs of material or subcontractor costs purchased
- Indirect costs added as % on contract specific amounts allocated
- MASH pools allow for lower indirect rates across all contracts, allowing for contracts with heavy subs/materials to share more of indirect burden



# Reasonable, Allocable, and Allowable

- In order for costs to be included in indirect costs, they first must be reasonable, allowable, and allocable
- Reasonable is defined as "if, in its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business."
- Per FAR 15.404-1(b)(2)(i) "*...Normally, adequate price competition establishes a fair and reasonable price...*"
- While one may argue gold plated office furniture is reasonable, they would probably price themselves out of the market, i.e. their price to the customer would no longer be competitive.
- The type of cost generally recognized as ordinary and necessary for the conduct of the contractor's business or the contract performance



# Reasonable, Allocable, and Allowable

- A cost is allocable if it is assignable or chargeable to one or more cost objectives on the basis of relative benefits received or other equitable relationship.
  - Is incurred specifically for the contract;
  - Benefits both the contract and other work, and can be distributed to them in reasonable proportion to the benefits received; or
  - Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.
- From our service center example, allocate costs based on % of labor costs, % of total contract costs, head count, square feet, etc.



# Reasonable, Allocable, and Allowable

- A cost is allowable only when the cost complies with all of the following requirements:
  - Reasonableness.
  - Allocability.
  - Follows CAS/GAAP.
  - Terms of the contract.
- Unallowable costs can not be included in indirect costs therefore they are excluded from indirect rates, multipliers, and incurred cost submissions
- Sometimes referred to as non-reimbursable or unrecoverable costs



# Unallowable Cost Examples

- PR/Advertising (FAR 31.205-1): Includes conventions, exhibits, free goods, samples, magazines, newspapers, trade papers, direct mail, dealer cards, window displays, outdoor advertising, and radio and television programs. *Only costs related to recruiting, finding scarce materials, or material disposal are allowable.*
- Bad Debt (FAR 31.205-3): Includes collections & legal costs. In other words, "the government always pays its debts."
- Contributions/Donations (FAR 31.205-8): Unallowable!



# Unallowable Cost Examples

- Employee Morale (FAR 31.205-13): Gray area- vending machines, gifts, recreation (except sports teams) are unallowable
- Entertainment (FAR 31.205-14): Costs of amusement, diversion, social activities (holiday parties), and any directly associated costs such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities are unallowable
- Fines/Penalties (FAR 31.205-15): Costs of fines and penalties resulting from violations of, or failure of the contractor to comply with, Federal, State, or local laws and regulations are unallowable (unless contract mandates otherwise)



# Unallowable Cost Examples

- IR&D/B&P (FAR 31.205-18): Can be unallowable, but typically are not. Contact your favorite compliance expert if in doubt!
- Contract Losses (FAR 31.205-23): An excess of costs over income under any other contract (including the contractor's contributed portion under cost-sharing contracts) is unallowable.
- Organizational (FAR 31.205-27): When in conjunction with planning or executing reorganization, including M&A. Also, costs of raising capital. Includes attorneys, accountants, brokers, consultants, etc.
- Professional/Consultant (FAR 31.205-33): Typically allowable, however be prepared for justification on items like retainer fees (necessary & customary) and past service levels... or retainer fee is comparatively reasonable for cost of in house services.





# Unallowable Cost Examples

- Recruitment (FAR 31.205-34): Pirating personnel from other contractors? See this clause!
- Selling (FAR 31.205-38): can blend in w/ PR, commissions et al can be unallowable
- Taxes (FAR 31.205-41): Federal income tax unallowable, state taxes typically allowable
- Training (FAR 31.205-44): Typically allowable for bona-fide employees
- Travel (FAR 31.205-46): Ticket must be cheapest unless routing is inefficient.
- Alcohol (FAR 31.205-51): Unallowable ☹️



# Calculating Indirect Rates

- Primary pools typically comprised of fringe, overhead, and G&A
- Typically each pool is its own tier
  - Fringe based on total labor cost
  - Overhead includes Fringe on OH labor
  - G&A includes Fringe on G&A labor and OH allocation
- Intermediary pools or service centers feed pools and sometimes direct (such as facility/copier service centers)
- Most confusing for those new to 3 tier pool structure is differentiating cost type between pools, OH/G&A aren't always easy to differentiate particularly to small businesses
- This structure is an example, every company & pricing strategy is different



# Importance of Indirect Rates

- You really need an indirect rate structure for accurate labor rate pricing
- Market competition demands tight controls on corporate cost, in ability to meet actual costs with budgeted leads to cost overruns and therefore unrecoverable losses
- Your rates now effect your pipeline 3 years from now. Capture strategy in some intel markets starts years before the contract is awarded, and price to win needs to be actively managed for teaming and proposal opportunities
- Staffing & recruiting are the life blood of every small company looking to grow, knowing what room you have in your rates allows you to get competitive offers out faster (aka larger pool base)



# Computing Fringe Rates

- Typically calculated as total fringe cost as percentage of total labor cost
- Fringe costs are considered the cost pool, where as labor costs in this case are considered the pool base
- An increase in pool costs increase the fringe rate, whereas an increase in the pool base decrease the fringe rate
- Possible to have multiple fringe pools, such as FTE w/ benefits & PTE w/ limited or no benefits
- If fringe costs are \$30,000 and total labor costs company-wide are \$100,000, then fringe rate would be 30% (30k/100k)
- Use Account Numbers to keep pool accounts together



# Computing Overhead Rates

- Typically calculated as total overhead cost as percentage of total contract cost (labor and non-labor)
- Overhead costs are considered the cost pool, where as the contract costs in this case are considered the pool base
- An increase in pool costs increase the overhead rate, whereas an increase in the pool base decrease the overhead rate
- Possible to have multiple overhead pools and therefore multiple overhead rates, such as company site vs client site, client base (different customers may require different administrative effort), etc
- Fringe cost is added to overhead labor cost at fringe rate
- If fringe rate is 30% and OH labor costs are \$10k, then fringe applied would be \$3k



# Computing G&A Rates

- Typically calculated as total G&A cost as percentage of total contract cost (labor and non-labor)
- G&A costs are considered the cost pool, where as the contract costs in this case are considered the pool base
- An increase in pool costs increase the G&A rate, whereas an increase in the pool base decrease the G&A rate
- Companies typically have one G&A pool and therefore one G&A rate
- Fringe cost is added to G&A labor cost at fringe rate
- If fringe rate is 30% and G&A labor costs are \$25k, then fringe applied to G&A would be \$7.5k



# Fringe Rate Demo

YTD Amount	Account #	Account Description
20,000	0400-000	Paid Time Off
10,000	0405-000	Holiday
15,000	0410-000	Employer Payroll Tax
12,000	0415-000	Employer Paid Benefits
<b>57,000</b>		<b>Total Fringe Costs</b>
125,000	Multiple	Direct Labor
25,000	0500-000	Overhead Labor
5,000	0600-000	Service Center Labor (IT/HR/etc)
20,000	0700-000	G&A Labor
<b>175,000</b>		<b>Total Labor Costs</b>
<b>32.57%</b>		<b>Fringe Rate</b>



# Overhead Rate Demo

YTD Amount	Account #	Account Description
20,000	0500-000	Overhead Labor
6,514		Fringe on Overhead Labor @ 32.57%
500	0510-000	Overhead Meals
1,250	0515-000	Overhead Travel
<b>28,264</b>		<b>Total Overhead Costs</b>
575,000	Multiple	Total Contract Labor
20,000	Multiple	Total Contract ODC's (Material, etc)
<b>595,000</b>		<b>Total Contract Costs</b>
<b>4.75%</b>		<b>Overhead Rate</b>





# G&A Rate Demo

YTD Amount	Account #	Account Description
60,000	0700-000	G&A Labor (Exec, Accounting, Admin, etc)
19,542		Fringe on G&A Labor @ 32.57%
5,500	0705-000	Office Rent/Utilities
2,500	0710-000	G&A Meals
750	0715-000	G&A Travel
<b>88,292</b>		<b>Total G&amp;A Costs</b>
575,000	Multiple	Total Contract Labor
20,000	Multiple	Total Contract ODC's (Material, etc)
<b>595,000</b>		<b>Total Contract Costs</b>
<b>14.84%</b>		<b>G&amp;A Rate</b>



# Rate Application Demo

	Contract A	Contract B	Total Costs	
Direct Labor	500,000	75,000	575,000	
Travel	3,000	5,000	8,000	
Materials	5,000	5,000	10,000	
ODC's	1,500	500	2,000	
	<b>509,500</b>	<b>85,500</b>	<b>595,000</b>	<b>Total Direct Costs</b>
	162,850	24,428	187,278	Fringe @ 32.57%
Add Fringe:	31,937	5,222	37,159	Overhead @ 4.75%
Add Fringe & OH:	104,587	17,100	121,687	G&A @ 14.85%
	<b>808,874</b>	<b>132,250</b>	<b>941,124</b>	<b>Total Contract Costs</b>



# Fee (aka Profit) & Revenue

- Fee is often dictated by the contract on cost type contracts
- Either as % or fixed amount
- % typically applied total contract costs
- $\text{Contract Revenue} = \text{Total Costs} + \text{Fee}$
- Based on last example:

	Contract A	Contract B	Total Costs	
	808,874	132,250	941,124	Total Contract Costs
	56,621	9,257	65,879	Fee @ 7%
	865,495	141,507	1,007,003	Revenue



# Revenue

- Revenue can also be  $\text{hours} * \text{bill rate}$  on T&M contracts
- Fixed Price LOE also  $\text{hours} * \text{bill rate}$
- While revenue can equal billings, revenue following  $\text{costs} + \text{fee}$  is more GAAP appropriate



# Final Comments

- Contract Funding > Costs > Revenue > Billing > Cash
- Revenue and billing are independent concepts
  - Due to actual vs target rates
  - Delta between actual and target rates applied typically drives unbilled balances
  - Unbilled balances typically billed at end of FY when actual rates are final and/or approved by DCAA
  - Unbilled balances can also occur when costs exceed funding



# Subcontractor vs. Prime Contractor

Presented By: Steve Swales



# FAR 52.244-2 Subcontracts

- Governs the use of subcontractors and should be included in;
  - All Cost Plus contracts
  - Any Fixed Price or Time & Material contracts in excess of \$150,000
- Contractors without approved purchasing systems require consent to subcontract
- Consent must be in written form from the Contracting Officer (CO)
- Even with an approved purchasing system the CO may reserve the right to approve subcontracts



# Prime Contracting

- Benefits
  - Control contract funds (allocation and disbursement)
  - Control statement of work
- Challenges
  - Oversight and administration of subcontract





# Sub-Contracting

- Benefits
  - More potential clients
  - Narrow requirements open up possibilities
  - Less direct oversight from Govt
- Challenges
  - Lack of control



# Types of Government Audits

Presented By: Steve Swales

# Most Common DCAA Interactions for Emerging Contractors



- Accounting System Requirements
- Proposal Adequacy
- Real-Time Labor Evaluations
- Incurred Cost Submissions
- Provisional Billing Rates

*Note: Terminology used from DCAA.MIL - Information for Contractors*

# Accounting System Requirements/ Review (Preaward Audit)



- Required for award of a Cost Plus or Flexibly Priced contract
- May be updated as often as every three years
- May be triggered by accounting changes reported in Incurred Cost Submission
- Auditor complete Standard Form 1408 (FAR 53.209-1(f))
- Initiated by Contracting Officer (CO) at DCMA

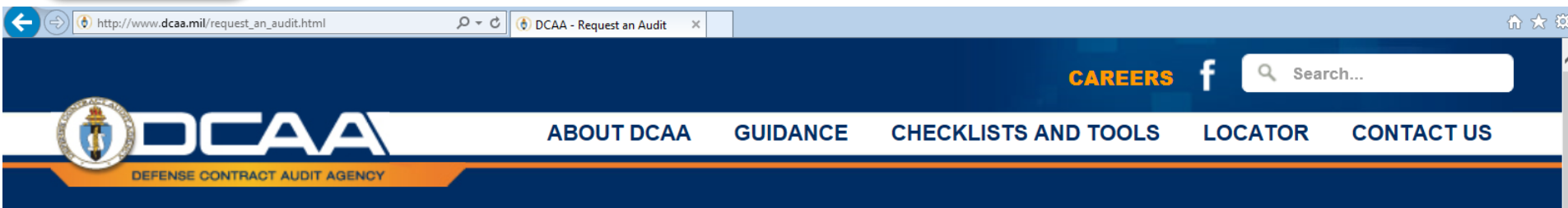


# Proposal Adequacy

- Initiated by Contracting Officer (CO) at DCMA
- Used to assist CO in contract negotiations
- DFARS 252.215-7009 – Proposal Adequacy Checklist
- Burden to support costs is on Contractor
- Adequate support for costs
  - Labor – Existing payrolls, offer letters, salary surveys
  - Materials – Vendor quotes or price lists, competitive bids
  - Indirect rates – Current year budget, last year's actual rates



# DCAA Website



## REQUEST AN AUDIT

Before requesting an audit, contractors' proposals, claims, or other submissions should be adequately prepared, and the contractor should be able to readily support the submission with adequate data, in order to fully protect the Government's interests and ensure receipt of timely and effective audit services. The how to request an audit guide has specific instructions to help [contracting officers prepare an audit request](#) and to submit the request to the appropriate DCAA office."

[Request an audit](#)

# Real-Time Labor Evaluation (Floor Check)



- Performed to validate that contractor is following documented and approved procedures
- DCAA unscheduled visit
- Employees are selected at random for;
  - Timesheet review
  - Interviews



# Incurred Cost Submission (Audit)

- Used to finalize indirect rates and close out contracts
- Must be initiated within 7 years of submission
- Contractor is required to maintain records to support submission
  - Timesheets
  - Vouchers
  - Subcontract agreements
- DCAA may propose changes to indirect rates
- Contractor will accept or refute changes





# Provisional Billing Rates (Forward Pricing)

- Supported by Forward Pricing submission
- Proposed rates at or below Forward Pricing submission should be accepted
- Proposed rates above Forward Pricing submission may



# Key Performance Indicators and Best Practices

Presented By: Barbara Morgan



# Key Performance Indicators

*Can I pay my bills?*

- Measuring Cash:
  - Cash Forecast –looks forward
  - Cash Flow – looks backward



# Key Performance Indicators

*Can I pay my bills?*

- Measuring Cash:
  - Cash Forecast –looks forward
  - Cash Flow – looks backward
- Accounts Receivable DSO
  - average collection time, in days



# Key Performance Indicators

*Can I pay my bills?*

- Measuring Cash:
  - Cash Forecast –looks forward
  - Cash Flow – looks backward
- Accounts Receivable DSO
  - average collection time, in days
- Working Capital
  - Difference between current assets and current liabilities
  - Measures capacity to meet obligations



# Key Performance Indicators

*How much is my business worth?*

- Debt to Equity
  - Total Liabilities/Total Equity – measures how you are funding your assets.
- Tangible net worth
  - The value of your business excluding intangible assets such as patents or trademarks



# Key Performance Indicators

*Am I making money?*

- EBITDA % of Sales
  - Net earnings excluding non-cash items (depreciation)
- Labor Utilization
  - What is the percent of billable vs non billable labor hours



# Key Performance Indicators

*What may happen in the future?*

- Wrap Rate/Pricing (yours vs. your competition)
- Pipeline – value & timing of potential contract wins







# KPI's for Gov't Contractors

- Backlog (funded and unfunded) - Expended contract funding remaining
- Unbilled Receivables – rate variance, working at risk, pending modifications
- Unbillable contract costs
- Rate Variance – billed rates vs. actual rates. +/-
- Burn Rate



# KPI's for Gov't Contractors

- Subcontracts vs Prime Contracts
- Disclosure milestones – compensation
- Compliance Triggers – CAS, EVM
- Status change milestones – small business threshold



# Best Practices

- Establish appropriate accounting systems and environment.
  - Holistic approach
  - Timely and correct billing
  - Create bills directly from your system
  - Keep high standards for timekeeping practices
  - Monitor receivables, funding and billing provisions & limitations



# Best Practices

- Budgeting
  - Continuous monitoring of expected vs actual results
  - Manage costs that you can control
- Training
- Setting a good example from the top down.
- Establish ownership and authority for critical tasks
- Evaluate where you stand in comparison to firms of a similar size and nature.



# Questions??

Thank you for your time today!

Please ask us a question.



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# Up Coming Classes

- [April 17, 2015](#)      [Courting the COR, Instructor Alan Boykin and Frank Anderson of Pace, LLC](#)
- [April 24, 2015](#)      [GSA Schedule – I got it. How do I flaunt it?](#)
- [May 07, 2015](#)      [Federal Construction Class – Best Practices Drive Profitability](#)
- [May 15, 2015](#)      [SBA Government Contracting Changes, Instructor Keir Bancroft](#)
- [May 22, 2015](#)      [Write a Powerful Capability Statement](#)



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# Up Coming Classes

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- Become a preferred customer. No cost. Many benefits.
- Come take another class!