

BRG BERKELEY RESEARCH GROUP

GOVCON RESEARCH REPORT JANUARY—MARCH 2013

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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 first calendar quarter of 2013. The issues are summarized by the following key subject-matter areas:

- GSA and VA Schedule Matters
- Office of Inspector General Reports
- Pertinent Government Accountability Office (GAO) Audit Reports
- OMB Proposed Guidance
- Key Federal Acquisition Regulation (FAR) Updates
- Key Defense Acquisition Regulation (DFAR) Updates
- Latest on Sequestration and Government Spending
- Other News

GENERAL SERVICES ADMINISTRATION AND DEPARTMENT OF VETERANS AFFAIRS SCHEDULE MATTERS

General Services Administration Office of Inspector General Audit (GSA OIG) Reports

Major Issues from Multiple Award Schedule Preaward Audits (GSA OIG Report AM A120050-3)

BY: SAJEEV MALAVEETIL

On March 8, 2013, the GSA OIG issued a report that identifies what it describes as continuing issues identified during 2011 preaward audits of Multiple Award Schedule (MAS) contracts (i.e., GSA Schedule contracts). The report provides an update to a September 2011 memorandum that addressed preaward audits conducted in Fiscal Year 2010. In the September 2011 report, the GSA OIG identified the following issues:

- The majority of vendors provided information that was not current, accurate, and/or complete to support their proposed prices
- Nearly half of the vendors had minimal or no non-Federal commercial customers, making it impossible to use non-governmental commercial sales as a basis for determining price reasonableness
- Over a quarter of the contractors audited supplied labor that did not meet the minimum educational and/or experience qualifications required by their contracts

In the more recent report, the GSA OIG identified some rate of improvement in two of the three areas, but noted high rates of recurrence in all three areas as a major concern. In addition, the GSA OIG highlighted an additional area of concern regarding reporting of sales and payment of the Industrial Funding Fee (IFF).

The GSA OIG identified that in 2011, 29 of 42 audits (69 percent of audits performed) identified that contractor Commercial Sales Practices (CSPs) contained non-current, inaccurate, and/or incomplete information—a reduction from 83 percent in FY 2010 audits. Per the GSA OIG, the lack of accurate, current, and complete CSP data adversely impacts the contracting officer's determination of fair and reasonable pricing on MAS contracts.

In addition, the GSA OIG identified that over one-third of FY 2011 MAS preaward audits found that contractors had minimal to no commercial sales of the products offered on their MAS contracts. In the GSA OIG's view, the lack of commercial comparable sales compromises the effectiveness of the identified basis of award customer category in assuring customer agencies receive the benefits from pricing changes in the marketplace.

One-third of the preaward audits also identified that MAS contractors provided individuals on professional services contracts that failed to meet the educational and/or experience qualification requirements of their contracts. This issue was more prevalent in the FY 2011 audits (33 percent) than the FY 2010 audits (27 percent).

The new area of concern, as identified by the GSA OIG, relates to contractors and their systems and processes related to the calculation and payment of IFF. Per the GSA OIG, over one-third of vendors audited in FY 2011 had, what it describes as inadequate systems to accumulate and report schedule sales. In addition, in many instances contractors were not correctly computing IFF, resulting in underpayment of the fee to the Government. The GSA OIG has recommend that the GSA's management strengthen controls to ensure that schedule vendors have adequate systems to accumulate and report schedule sales and ensure proper IFF payments.

The issues identified by the GSA OIG reinforce the continued scrutiny faced by MAS contractors in preaward audits of GSA and VA Schedule contracts. If and how the GSA chooses to implement the GSA OIG's recommendations regarding IFF systems should be of particular interest to industry—particularly in light of statutory limitations precluding the requirement of Government-specific systems for commercial item acquisitions. •

OFFICE OF INSPECTOR GENERAL REPORTS

Department of Defense Inspector General (DOD OIG) Audit Reports

Monitoring of the Quality of the DCAA Agency Audits (DOD-OIG Report DODIG-2013-044)

BY: BRYANT LE

The DOD IG recently issued report no. DODIG-2013-044 detailing the agency's findings and recommendations pertaining to its peer review of the DCAA's FY 2010 audit reports and work. The DOD IG performed its last peer review for the DCAA in FY 2006 (for DCAA reports issued in FY 2006). For that period, the DOD IG's review provided that the "[DOD IG] determined the DCAA quality control system [was] adequately designed and functioning as prescribed" (see report no. [D-2007-6-006, DOD IG - Previous Peer Review Report](#)).

However, the DOD IG's current report states that any "GAGAS compliant" DCAA report issued subsequent to

August 26, 2009, "should have contained a modified GAGAS statement noting an exception to compliance with the Quality Control and Assurance standard" (see report no. [DODIG 2013-044](#)). In other words, the DOD IG instructed the DCAA to qualify its audits with a statement that it no longer complies with the peer review requirements of General Accepted Government Auditing Standards (GAGAS).

The DOD IG's rationale stems from the findings that DCAA did not remediate the deficiencies in audit quality that the IG previously identified in its FY 2006 report. This is evidenced by continued noncompliance per their FY 2010 peer review as well as the Government Accountability Office's (GAO) 2009 Audit Report, "DCAA Audits: Widespread Problems with Audit Quality Require Significant Reform" (see [GAO-09-468](#)). As a result of the continued deficiencies, the DOD IG is unable to support an adequate opinion regarding the DCAA's system of quality control.

It is important to note that the GAO's report was based on FY 2004 to 2006 audit reports. The DOD IG's report was based on FY 2010 reports, and the DOD IG communicated its findings to the DCAA in August 2009. Since this time, the DCAA has made several enhancements and changes to its internal audit policy and guidance—intended to address many of the issues identified in both the GAO Report and the 2006 DOD IG report, as well as the draft findings of the 2010 report. The audit reports that were the subject of the DOD IG's recent report date back to reports issued in FY 2010 and therefore may not truly reflect the DCAA's current state of remediation and corrective action.

Nevertheless, the preponderance of evidence indicates that audit quality issues have historically been present at the DCAA and may continue to exist. In its 2009 report, the GAO pointed to the production-oriented mission of DCAA's management environment and quality assurance structure as the underlying impetus to pervasive audit quality issues. The most recent DOD IG report lists a number of facets that gravitate to a "need for improvements in the area of competence" at the DCAA as the underlying impetus to noncompliance in audit quality. The

DOD IG report also acknowledges that “during the past 5 years, the GAO and DOD IG have issued 12 reports related to similar issues with DCAA that are addressed in [the] report.” In other words, the issues and concerns regarding the quality of the DCAA’s audit performance appear to be recurring. Some corrective action plans should begin to materialize by the next peer review/report.

The DCAA indeed “agreed in principle” with a majority of the DOD IG’s recommendations and has responded with initiatives and remediation plans to rectify the DOD IG’s report findings. However, the DOD IG believed that some responses by the DCAA were incomplete (i.e., the DCAA’s response “did not fully address the intent of the [DOD IG’s] recommendation”) and thus requested the DCAA to provide additional comments regarding the recommendation in the final report. The DOD IG anticipates receiving these comments in April of 2013. •

PERTINENT GOVERNMENT ACCOUNTABILITY OFFICE (GAO) AUDIT REPORTS

GAO Review of Contractor Employee Compensation

BY: MARY KAREN WILLS

The GAO is performing a review of Government contractor employee compensation. The report is due to Congress by May 2013. Congress has requested that the GAO assess the impact of proposed regulations included in the 2013 National Defense Authorization Act that would further cap allowable executive compensation for contractors. GAO must assess the potential impact of a new cap on the contractor industry base. In addition, GAO will assess the inconsistencies of current caps on executive compensation across Federal agencies.

GAO is currently soliciting input. To provide comments, go to <http://www.gao.gov/> •

Pension Costs on DoD Contracts - Additional Guidance Needed to Ensure Costs Are Consistent and Reasonable ([GAO Audit Report GAO-13-158](#))

BY: MATT FRANZ

On January 22, 2013, the GAO issued a report on its review of DoD contractor pension costs. The review was performed in response to an increase in pension costs since the 2008 market downturn and due to the prospect of recent changes to Cost Accounting Standards (CAS) and Employee Retirement Income Security Act (ERISA) rules regarding the calculation of pension costs.

Given this possibility of increased pension costs, the GAO assessed how:

1. Contractor pension costs are determined
2. DoD ensures the contractor pension costs it pays are appropriate
3. DoD contractors’ defined benefit pension plans compare with plans sponsored by similar companies
4. Pension costs have affected DoD contract costs, and the factors that contributed to these pension costs
5. Harmonization of CAS with ERISA will affect the amounts DoD will pay in pension costs in coming years

Some of GAO’s key findings included:

- CAS pension costs reported by the 10 largest DoD contractors grew considerably over the last decade, from less than \$500 million in 2002 to almost \$5 billion in 2011
- Contractor CAS pension costs grew as the market downturn increased unfunded liabilities
- Contractors and DoD officials expect CAS pension costs to increase starting in 2014 due to harmonization
- CAS discount rates used to value liabilities will be tied to the more volatile ERISA-based rates, making it harder to forecast future CAS pension



costs and reducing the consistency of cost projections used in contract pricing

- DoD issued limited guidance on projecting ERISA-based discount rates for CAS calculations, but lack of specificity in the guidance can lead to great variation among the rates contractors use
- The discount rates used for settlements were not updated as part of harmonization, meaning liabilities will be calculated differently under CAS and ERISA rules

In response to these findings, GAO issued the following recommendations:

- The Secretary of Defense needs to clarify responsibility for and guidance on assessing pension reasonableness and determining discount rates for pension cost projections
- The CAS board should set a schedule for revising the parts of CAS that address the settlement of plan curtailments

DoD agreed with the recommendations to the Secretary of Defense, and the Office of Management and Budget (OMB) responded that when the CAS board meets it will consider a schedule for the recommended revision.

The full report is 57 pages long and contains the detailed steps that the GAO took to evaluate pension costs. See the detailed report for additional discussion. •

DoD's Implementation of Justification for 8(a) Sole-Source Contracts ([GAO Audit Report GAO-13-308R](#))

BY: KELLY LYNCH

In recent years, oversight and scrutiny have increased on the award of sole-source contracts to 8(a) firms. Before 2009, no Federal Acquisition Regulation (FAR) requirement was in place for documented justification when awarding a contract greater than \$20 million to an 8(a) firm using non-competitive means. The timeline of the key changes to this process is as follows:

- October 2009: The FY 2010 National Defense Authorization Act (NDAA), Section 811, required that the FAR be revised to include the requirement that written justification be provided for sole-source awards to 8(a) firms.
- March 2011: The FAR was updated to reflect the requirement set forth in the FY 2010 NDAA. Agencies were required to implement the new justification requirement. The FAR requires that, as a minimum, the justification include five criteria:
 - o Description of the needs of the agency concerned for the matters covered by the contract
 - o Specification of the statutory provision providing the exception from the requirement to use competitive procedures in entering into the contract
 - o Determination that the use of a sole-source contract is in the best interest of the agency concerned
 - o Determination that the anticipated cost of the contract will be fair and reasonable
 - o Such other matters as the head of the agency concerned shall specify for purposes of this section
- December 2012: The Government Accountability Office (GAO) issued "Federal Contracting: Slow Start to Implementation of Justifications for 8(a) Sole-Source Contracts," a report that highlighted the following:
 - o Delayed implementation of the requirement across agencies
 - o Lack of awareness and confusion amongst contracting and Small Business Administration (SBA) officials

- o Significant decrease in the number of sole-source contracts greater than \$20 million being awarded to 8(a) firms since the final FAR rule was published

In February 2013, GAO issued a review of the Department of Defense's (DoD) implementation of the requirement that written justification be provided for 8(a) sole-source contract awards greater than \$20 million. In the review, GAO provided a supplemental evaluation of DoD implementation of the new FAR requirement. The focus of the review was on contracts awarded after March 16, 2011, when the interim rule was published in the FAR. Between March 16, 2011, and March 31, 2012, DoD awarded eight sole-source 8(a) contracts of an amount greater than \$20 million. GAO found that six of the awards did not meet FAR requirements. The audit found that the requirement was not met because the contracting office did not prepare a justification or did not prepare justification that met the five criteria stated in the FAR. GAO did not issue additional recommendations based on the review, but did highlight the recommendations made in the December 2012 report that included clarification for both contracting officers and SBA officials. •

OMB PROPOSED GUIDANCE

OMB Reform of Federal Policies Relating to Grants and Cooperative Agreements; Cost Principles and Administrative Requirements (Including Single Audit Act) - Proposed Rules (Federal Register Vol. 78, No. 22)

On February 1, 2013, the Office of Management and Budget (OMB) issued proposed guidance that serves to streamline existing guidance related to grants and cooperative agreements involving state, local, and tribal Governments, as well as institutions of higher education and non-profit organizations. The proposed guidance would supersede existing guidance currently dispersed among various OMB Circulars. Comments to the proposed rule are due on June 2, 2013. Please see BRG's overview of the proposed guidance in our feature article, which can be found as an [Appendix](#) to this edition of the Research Report. •

KEY FEDERAL ACQUISITION REGULATION (FAR) UPDATES

Nondisplacement of Qualified Workers Under Service Contracts – Final Rule (FAR Case 2011–028)

BY: RYAN BYRD

This final rule adds FAR subpart 22.12, “Nondisplacement of Qualified Workers Under Service Contracts,” and a related contract clause.

The regulations require that workers on a Federal service contract who would otherwise lose their jobs as a result of the completion or expiration of a contract be given the right of first refusal for employment with the successor contractor. The regulations apply to all service contracts (prime and subcontractor) above the simplified acquisition threshold (currently \$150,000) and their solicitations, except those excluded, that succeed contracts for the same or similar services at the same location. The FAR excludes certain types of contracts and employees from its requirements, and allows the head of a contracting department or agency to exempt any of its contracts from the regulations if it finds the requirements would not serve the purposes of the Equal Opportunity Act or would impair the Federal Government's ability to procure services economically or efficiently.

Under the regulations, a successor contractor may reduce the size of the workforce, give first preference to certain of its current employees, and offer employment to the predecessor's employees in positions for which they are qualified other than those which they held previously.

The new regulations include provisions for investigating and resolving complaints of non-compliance. The regulations also provide for remedies and sanctions for violations—including payment of back wages, withholding of funds for unpaid wages, and exclusion from Federal contracting. •



Prohibition on Contracting With Inverted Domestic Corporations – Final Rule ([FAR Case 2012-13](#))

BY: ERIN WILKERSON

This final rule, effective January 29, 2013, prohibits the award of contracts using appropriated funds to any foreign incorporated entity that is treated as an inverted domestic corporation or to any subsidiary of such entity.

An inverted domestic corporation is one that used to be incorporated in the United States, or used to be a partnership in the United States, but now is incorporated in a foreign country, or is a subsidiary whose parent corporation is incorporated in a foreign country. This regulation impacts an offeror that is an inverted domestic corporation that wants to bid on Government contracts; domestic entities are not directly impacted by this rule. FAR 9.108-4 allows for a waiver of the prohibition if an agency head determines in writing that the waiver is required in the interest of national security, documents the determination, and reports it to Congress. •

Extension of Sunset Date for Protests of Task and Delivery Orders – Final Rule ([FAR Case 2012-007](#))

BY: KELLY LYNCH

Effective January 29, 2013, the interim rule that extended the sunset date on the protest of task and delivery orders from May 27, 2011, to September 30, 2016, was published as final. This rule resulted from National Defense Authorization Act (NDAA) for Fiscal Year 2008, which expanded the Government Accountability Office's (GAO) jurisdiction to hear protests related to the issuance of task or delivery orders when the value is greater than \$10 million or "the order increases the scope, period, or maximum value of the contract under which the order is issued." The interim rule was written in order to implement Section 825 of the 2011 NDAA, which extended the sunset date for DoD, NASA, and Coast Guard contracts to September 30, 2016. In addition, the interim rule implemented Section 813 of the 2012 NDAA, which extended the sunset date for civilian agencies until September 30, 2016, as well. The extension of the sunset date is based on the assessment that there has been no

significant workload increase on GAO based on the increased jurisdiction related to the 2008 NDAA rule. •

Unallowability of Costs Associated with Foreign Contractor Excise Tax ([FAC 2005-65](#), [FAR Case 2011-011](#))

BY: RYAN BYRD

This final rule amends FAR 31.205-41, 52.229-3, 52.229-4, 52.229-6, and 52.229-7 to implement certain requirements of section 301 of the James Zadroga 9/11 Health and Compensation Act of 2010 (Pub. L. 111-347), which imposes a 2-percent excise tax on certain Federal procurement payments to foreign persons. The law amended the Internal Revenue Code by adding a new section 5000C.

Per the final FAR rule, the costs associated with the excise tax on goods or services are unallowable if the goods or services are produced in a country that is not party to an international procurement agreement with the United States. The statute applies to contracts entered into on or after January 2, 2011, and does not apply if the imposition of the tax would be inconsistent with any international agreement. The tax will be collected in a manner similar to other U.S. taxes withheld on payments to foreign persons.

The Department of Treasury will provide specific guidance regarding the application of the tax and procedures for withholding the tax. •

Definition of Contingency Operation – Interim Rule ([FAC 2005-66](#), [FAR Case 2013-003](#))

BY: HOMER WINTER

This interim rule updates the text of Federal Acquisition Regulation (FAR) Part 2.101, "Definitions," to ensure consistency with the change in definition made by paragraph (b) of Section 515 of the National Defense Authorization Act for Fiscal Year 2012. Published by the DoD, NASA, and GSA on February 28, 2013, the rule altered the FAR definition of "contingency operation" to include a reference to section 12304a of Title 10, United States Code. Section 12304a contains a new specification calling for treatment of any operation as a contingency op-

eration when the Secretary of Defense activates Reserves in response to a major disaster or emergency declared by the President.

The updated definition of “contingency operation” within FAR Part 2.101 could potentially have a positive impact on local small entities. For example, FAR 19.502–2(a) requires simplified acquisitions during a contingency operation within the United States to be automatically reserved for small businesses. The simplified acquisition threshold for contingency operations in the United States is \$300,000 instead of the usual \$150,000. Additionally, the Robert T. Stafford Disaster Relief and Emergency Assistance Act specifies a preference for local entities when contracting for major disaster or emergency activities. •

Changes to Time-and-Materials and Labor-Hour Contracts and Orders – Final Rule ([FAC 2005-66](#), [FAR Case 2011-025](#))

This final rule provides contracting officers with additional guidance addressing requirements for raising the ceiling price or otherwise changing the scope of a time-and-materials (T&M) or labor-hour (LH) contract. The rule applies to both commercial and non-commercial T&M and LH contracts and to orders under those contracts. The rule requires that changes in the general scope of a contract or order should be justified as noncompetitive new work. The language makes a distinction between the procedures to be followed in justifying and documenting a change to a contract versus a change to an order issued under a contract. Specifically, changes to the scope or ceiling price of contracts must follow the procedures set forth at FAR 6.303, which essentially requires a sole-source justification for the scope or ceiling price change.

Separately, for Federal Supply Schedule (FSS) orders under contracts, FAR 8.405-6 governs the justification and documentation requirements; and for multiple award task-order contracts, FAR 16.505(b)(2) governs the justification and documentation requirements. Regardless, the justification requirement is one of a single-source, noncompetitive procurement. This restricts contracting officers from changing contracts and orders based only

upon a determinations and findings (D&F) and forces them to address the noncompetitive nature of the procurement change in scope or price ceiling. •

Extension of Authority for Use of Simplified Acquisition Procedures for Certain Commercial Items – Final Rule ([FAR Case 2013-007](#))

BY: SAJEEV MALAVEETIL

This final rule extends the authority of the Commercial Item Test Program at FAR Subpart 13.5 from its current expiration date of January 1, 2012, to January 1, 2015. FAR 13.5 authorizes the use of simplified acquisition procedures for certain commercial items in amounts greater than the simplified acquisition threshold, if the contracting officer can reasonably expect that offers will include only commercial items. The final rule only modifies the effective date of the test program and does not modify either the respective thresholds or the applicability of the test program.

The test application of simplified acquisition procedures to commercial items may be applied to acquisitions not exceeding \$6.5 million. If the acquisition is for commercial items that, as the head of an agency determines, are to be used in support of a contingency operation or to facilitate the defense against or recovery from nuclear, biological, chemical, or radiological attack; then the threshold is \$12 million. •

Small Business Protest and Appeals – Proposed Rule ([FAR Case 2012-014](#))

BY: KELLY LYNCH

The FAR council is proposing to amend the FAR to update the small business size and small business status protest and appeal procedures and timeframes, and to address the application of the Small Business Administration’s (SBA) Office of Hearing and Appeals (OHA) decisions on a protested concern’s size and other small business status determinations. The proposed changes are consistent with previously issued interim and final rules concerning SBA size and eligibility determinations (76 FR 5680), Women-Owned Small Business (WOSB) protest and ap-

peal decisions (77 FR 1857), and SBA North American Industry Classification System (NAICS) determinations (76 FR 8222). Comments to the proposed rule are due on May 6, 2013. •

Defense Base Act – Proposed Rule ([FAR Case 2012-016](#))

BY: RYAN BYRD

FAR Case 2012-016, published on March 20, 2013, proposes to revise FAR clause 52.228-3 to clarify contractor and subcontractor responsibilities to obtain workers' compensation insurance or to qualify as a self-insurer, including the requirement to include flow down of this clause to all subcontractors to which the Defense Base Act applies, and other requirements, under the terms of the Longshore and Harbor Workers' Compensation Act as extended by the Defense Base Act. •

KEY DFARS UPDATES

Electronic Subcontracting Reporting System – Final Rule ([DFARS Case 2009-D002](#))

BY: SAJEEV MALAVEETIL

On February 28, 2013, DoD adopted as final, with some changes, an October 2010 [interim rule](#) to amend the DFARS to conform to FAR policy and procedures related to the Electronic Subcontracting Reporting System (eSRS). The interim rule amended the DFARS to provide DoD-specific procedures and policies related to eSRS. The procedures are as follows:

1. The Individual Subcontract Report (ISR) shall be submitted to the contracting officer at the procuring contracting office, even when contract administration has been delegated to the Defense Contract Management Agency.
2. A Summary Subcontract Report (SSR) for other than a commercial subcontracting plan, or construction and related maintenance repair contracts, shall be submitted in eSRS to the department or agency within DoD that administers the majority of the Contractor's individual subcontracting plans.

The rule also specifies Government responsibility for acknowledgement of receipt, and rejection of the eSRS submissions. •

Proposal Adequacy Checklist – Final Rule ([DFARS Case 2012-D042](#))

BY: SAJEEV MALAVEETIL

On March 28, 2013, the DFARS was updated to include contractor requirements to prepare and submit a proposal adequacy checklist with all proposals that require the submission of certified cost or pricing data (i.e., those proposals subject to the Truth in Negotiations Act (TINA)). The requirements to prepare and submit the proposal adequacy checklist will be incorporated into solicitations subject to TINA through a new provision 252.215-7009, "Proposal Adequacy Checklist."

According to the DoD, the revisions to the DFARS are intended to ensure offerors take responsibility for submitting thorough, accurate, complete, and current proposals.

In preparing the checklist, an offeror will be required to provide the location—within its proposal—of each of the 36 required items on the checklist, as applicable. To the extent that one of the items on the checklist is not included in the proposal, the offeror will be required to provide an explanation as to why the requested information is not included in the proposal. Offerors, should they chose, may have their prospective subcontractors use the same or similar checklist, if appropriate.

The original [proposed rule](#), which was published on December 2, 2011, received 16 comments from both industry and the Government. Many commented that that the rule is duplicative to the DCAA's existing checklists and would result in increased costs and efforts to both the Government and contractors. Others commented that the checklist should not be incorporated into the DFARS, but rather in the DFARS Procedures, Guidance, and Information (PGI).

Despite these comments, the DoD incorporated a modified version of the proposed checklist into DFARS, citing

that it is the contractor's responsibility to ensure that a proposal is consistent with existing requirements of the FAR and DFARS.

Contractors should modify their pricing procedures to incorporate use of the DFARS Proposal Adequacy checklist in all proposals subject to TINA. While not required, contractors may consider incorporating a requirement for prospective subcontractors to prepare a similar checklist for subcontractor proposals requiring the submission of certified cost or pricing data.

A list of the items on the proposal adequacy checklist is included in Appendix B. •

Unallowable Fringe Benefit Costs - Proposed rule (DFARS Case 2012-D038)

BY: RYAN BYRD

DFARS case 2012-D038 proposes to add paragraph 231.205-6(m)(1) to explicitly state that fringe benefit costs incurred or estimated that are contrary to law, employer-employee agreement, or an established policy of the contractor are unallowable. FAR 31.205-6(m) currently states that the costs of fringe benefits (which include employee healthcare benefits) are allowable to the extent that they are reasonable and are required by law, employer-employee agreement, or an established policy of the contractor. Although fringe benefit costs that do not meet these criteria are not allowable, the FAR does not make them expressly unallowable.

Specifying these fringe benefit costs as expressly unallowable in the DFARS makes it clear that the penalties at FAR 42.709-1 are applicable if a contractor includes such unallowable fringe benefit costs in a final indirect cost rate proposal or in the final statement of costs in-

curred or estimated to be incurred under a fixed-price incentive contract. FAR 42.709-1(a) provides penalties that apply if the indirect cost is expressly unallowable under a cost principle in the FAR, or an executive agency supplement to the FAR. The section applies to all contracts in excess of \$700,000, except fixed-price contracts without cost incentives or firm-fixed-price contracts for the purchase of commercial items. •

LATEST ON SEQUESTRATION AND GOVERNMENT SPENDING

Ashton Carter Memo - Handling Uncertainty in FY 2013

BY: RYAN BYRD

On January 10, 2013, Deputy Secretary of Defense Ashton Carter issued a [memorandum](#) for the secretaries of the various military departments regarding the handling of the budgetary uncertainty in fiscal year 2013.

In the memo, Mr. Carter identifies two sources of the budgetary uncertainty: the Continuing Resolution (CR) and the potential of the deferred sequestration.

According to Mr. Carter, each of these issues poses significant challenges to the DoD when faced in isolation, negatively impacting the department's ability to maintain a ready force and perform wartime operations.

To mitigate the impact of the budgetary uncertainty, Mr. Carter provides the following guidance to reduce the impact on its workforce, operations, and unit readiness in the near term. He notes that due to the temporary nature of the CR, any actions below would need to be reversible at a later date in the event that Congress acts to remove the risk of the budgetary certainty regarding the CR.



Ashton Carter's Near-Term Actions to Address Budgetary Uncertainty Related to the CR

- Freeze civilian hiring
- Provide authority to terminate employment of temporary hires and to notify term employees that their contracts will not be renewed
- Reduce base operating funding
- Curtail travel, training, and conferences
- Curtail facilities maintenance or Facilities Sustainment, Restoration, and Modernization
- Curtail administrative expenses such as supply purchases, business IT, ceremonies, etc.
- Review contracts and studies for possible cost savings
- Cancel third- and fourth-quarter ship maintenance availabilities and aviation and ground depot-level maintenance activities
- Clear all research and development (R&D) and production contracts and contract modifications that obligate more than \$500 million with the USD (AT&L) prior to award
- For Science and Technology accounts, provide the USD (AT&L) and the assistant secretary of Defense (Research & Engineering) with an assessment of the impact that budgetary uncertainty may have on meeting departmental research priorities

Longer-term budgetary challenges resulting from sequestration will have a greater impact on the DoD. As such, Mr. Carter provides the following guidance—specifically related to the DoD civilian workforce—to prepare for and mitigate the impact of sequestration.

Ashton Carter's Long-Term Actions Regarding the Civilian Workforce to Address Budgetary Uncertainty Related to Sequestration

- Release temporary employees
- Do not renew term hires
- Impose hiring freezes
- Authorize voluntary separation initiatives and early retirements
- Consider the possibility of furloughs of up to 30 calendar days or 22 discontinuous workdays

Per Mr. Carter's guidance, when developing their draft budget plans, components should exempt military personnel funding and fully protect funding related to war-time operations and Wounded Warrior programs from any sequestration reduction. In addition, per the guidance, components should strive to protect family programs, funding associated with military readiness, and investments funded in overseas contingency operations.

With a discrete focus on the civilian DoD workforce and non-mission-critical research and development spending, Mr. Carter's memo gives insight into areas within the DoD that will be impacted most by the budgetary uncertainty. •

Sequestration and the Fiscal Cliff: Planning for Uncertainty with Respect to Fiscal Year 2013 Budgetary Resources

On January 14, 2013, Office of Management and Budget (OMB) Acting Director Jeffrey Zients issued a [memo-randum](#), "Planning for Uncertainty with Respect to Fiscal Year 2013 Budgetary Resources." In this guidance, he recognizes the budgetary uncertainty in the coming months brought about by sequestration, and the expiration of the continuing appropriations resolution.

The memorandum urges Congress to take immediate action to avoid sequestration and lists a series of services that the Federal Government will need to curtail. It lists six guiding principles in planning to operate with reduced budget resources:

1. Reduce operating risks and minimize impacts to the Agency's core mission
2. Identify and address operational challenges that could affect the Agency's mission or otherwise raise life, safety, or health concerns
3. Identify means to reduce the civilian workforce including:
 - a. Hiring freezes
 - b. Releasing temporary employees and not renewing term/contract hires
 - c. Authorizing voluntary separation incentives and voluntary early retirements
 - d. Implementing administrative furloughs
4. Review grants and contracts to determine where cost savings may be achieved
5. Consider funding flexibilities like reprogramming and transfer authority
6. Be cognizant of the Worker Adjustment and Retraining Notification (WARN) Act

Agencies should also work with their OMB resource management office (RMO) on the appropriate timing to submit contingency plans for operating under sequestration. •

Sequestration and the Fiscal Cliff: Issuance of the Sequestration Order

The March 1, 2013, [memorandum](#) issued by Office of Management and Budget (OMB) Acting Director Jeffrey Zients—"Issuance of the Sequestration Order Pursuant to Section 251A of the Balanced Budget and Emergency Deficit Control Act of 1985, as Amended"—informs executive departments and agencies that the President issued the sequestration order on that date. It requires that nonexempt budget accounts be reduced by the amount in OMB's sequestration report, OMB Report to the Con-

gress on the Joint Committee Sequestration for Fiscal Year 2013. Summary spending cuts from this report are as follows:

- 7.8-percent reduction in non-exempt defense discretionary funding
- 5.0-percent reduction in non-exempt nondefense discretionary funding
- 2.0 percent to Medicare
- 5.1 percent to other non-exempt nondefense mandatory programs
- 7.9 percent to non-exempt defense mandatory programs

Because these cuts must be achieved over seven months versus twelve months, the effective reduction rate will be approximately 13 percent for nonexempt defense programs and 9 percent for non-exempt nondefense programs. Detailed cuts by budget account are enumerated in OMB's sequestration report. •



OTHER NEWS

Department of Defense Procurement and Acquisition Policy (DPAP) Prohibition on the Use of Cost-Type Contracting

On March 11, 2013, pursuant to Section 811 of the National Defense Authorization Act (NDAA) for Fiscal Year (FY) 2013, the Director of Defense Procurement and Acquisition Policy issued a [prohibition on using cost-type contracts](#) for Department of Defense prime contracts involving the production of major defense acquisition programs (MDAP). An MDAP is defined as being designated by the Under Secretary of Defense (Acquisition, Technology, and Logistics) (USD (AT&L)), or estimated by the USD (AT&L), to require an eventual total expenditure for Research, Development, Test and Evaluation (RDT&E) of more than \$365 million in FY 2000 constant dollars or, for procurement, of more than \$2.19 billion in FY 2000 constant dollars.

There are two exceptions to this prohibition if USD (AT&L) submits to congressional defense committees:

1. A written certification that the particular cost-type contract is needed to provide a required capability in a timely and cost-effective manner
2. An explanation of the steps taken to ensure the use of cost-type pricing is limited to only those line items or portions of a contract where such pricing is needed to achieve the purposes of the exception

Ostensibly, this measure was taken to minimize risk to the Government on cost-type contracts. However, it fails to recognize that fixed-price contracts may carry the same risk profile on these types of programs, especially during the RDT&E stages. That is, they may be more costly to the extent that they trigger costly change orders, requests for equitable adjustment, and/or claims. •

The DCAA Website Gets a Facelift

BY: KELLY LYNCH

The Defense Contract Audit Agency (DCAA) website (www.dcaa.mil) has received a facelift. The website now provides contractors with detailed instructions on how to request an audit; the site also provides a more direct path for contractors to understand the DCAA processes for all audits the agency conducts. Unfortunately, the new website will not help contractors receive more timely audits; however, it provides more information on what to expect during an audit.

If you notice that something is missing from the DCAA website, or if there is something you think should be added, we would love to hear from you. •

BRG'S GOVERNMENT CONTRACT BLOG

Many of the items in this edition of the Research Report were first reported 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.

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This publication is intended to distribute information only and is not a substitute for professional advice.

APPENDIX A – FEATURED ARTICLE OMB PROPOSED GUIDANCE

Reform of Federal Policies Relating to Grants and Cooperative Agreements; Cost Principles and Administrative Requirements

OVERVIEW

On February 1, 2013, the Office of Management and Budget (OMB) issued proposed guidance that serves to streamline existing guidance related to grants and cooperative agreements involving state, local, and tribal Governments, as well as institutions of higher education and non-profit organizations. The proposed guidance would supersede existing guidance currently dispersed among various OMB Circulars. The primary goals associated with the proposed guidance include the following:

- Increasing the efficiency and effectiveness of the Federal grant-making process to ensure the best use of the \$500 billion in Federal funds spent through grants annually
- Eliminating rules that are outdated, ineffective, or excessively burdensome
- Reducing the “red tape” attached to grants and cooperative agreements by eliminating unduly burdensome, duplicative, or low-priority recordkeeping requirements
- Refocusing the Single Audit tool on programs and practices that pose the greatest risk of improper payments, fraud, waste, and abuse

The most significant component of the proposed guidance is the consolidation and streamlining of the provisions of eight existing OMB Circulars and 45 Code of Federal Regulations (CFR) Part 74 applicable to grants and cooperative agreements into a single uniform set of guidelines under one OMB Circular. The new uniform guidelines will include appendices and supplemental guidance that remains due to the unique differences in recipients (e.g., hospitals versus state and local Governments). The consolidation is aimed at eliminating current overlaps and duplication across the OMB Circulars, while continuing to recognize explicit differences across the differing types of entities where needed.

PROPOSED GUIDELINES – FORMAT AND CONTENT

Today’s authoritative guidance comprises the following OMB Circulars and CFR sections:

OMB Circular	Title
OMB A-21	Cost Principles for Educational Institutions
OMB A-87	Cost Principles for State, Local, and Indian Tribal Governments
OMB A-122	Cost Principles for Non-Profit Organizations
OMB A-89	Federal Domestic Assistance Program Information
OMB A-102	Grants and Cooperative Agreements with State and Local Governments
OMB A-110	Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations
OMB A-133	Audits of States, Local Governments, and Non-Profit Organizations
OMB A-50 Relevant Sections	Guidance on Audit Act Follow-up
45 CFR Part 74, Appendix E	Principles for Determining Costs Applicable to Research and Development Under Grants and Contracts with Hospitals

The newly proposed consolidated requirements will be contained in a single OMB Circular, “OMB Uniform Guidance: Cost Principles, Audit, and Administrative Requirements for Federal Awards” (hereinafter called “Proposed Uniform Guidance” or “proposed guidance”). The Proposed Uniform Guidance will contain the following subchapters and appendices.

Subchapter A – General Provisions

Subchapter B – Pre-Award Requirements

Subchapter C – Federal Award Notice

Subchapter D – Inclusion of Terms and Conditions in Federal Award Notice

Subchapter E – Post Federal Award Requirements

Subchapter F – Cost Principles

Subchapter G – Audit Requirements

Subchapter H – Appendices, including:

Appendix I – Definitions

Appendix II – Full Text of Notice of Funding Opportunity

Appendix III – Contract Provisions for Recipient and Subrecipient Contracts

Appendix IV – Indirect (F&A) Costs for Educational Institutions

Appendix V – Indirect Costs for Non-profit Organizations

Appendix VI – State/Local – Wide Central Service Cost Allocation Plans

Appendix VII – Public Assistance Cost Allocation Plans

Appendix VIII – State and Local Indirect Cost Proposals

Appendix IX – Non-profit Organizations Exempted from Subchapter F Cost Principles

Appendix X – Hospital Cost Principles

Appendix XI – Audit Data Collection Form (SF-SAC)

Appendix XII – Single Audit Compliance Supplement

From an overview standpoint, each aforementioned subchapter contains consolidated guidance applicable to all entities receiving Federal grants and cooperative agreements. The following discussion is intended to summarize the contents of each subchapter.

Subchapter A – General Provisions

The General Provisions establish that the guidance provides uniform cost principles, audit requirements, and administrative requirements for all Federal grants and cooperative agreements awarded to applicable entities.

Subchapter B – Pre-Award Requirements

This subchapter puts forth previously unpublished, Government-wide policy that would be universally required of Federal agencies awarding grants and cooperative agreements. Per the Proposed Uniform Guidance, Federal awarding agencies will be required to provide a 90-day notice of Federal financial assistance programs in a “Catalog of Federal Financial Assistance” (CFFA) to be maintained by the General Services Administration. The CFFA will replace the current Catalog of Federal Domestic Assistance. A standard format for announcing funding opportunities will be required of all awarding agencies.

Awarding agencies will be required to announce specific funding opportunities via public notice. Prescribed formats and announcement text is included in the proposed guidelines. These announcements will now have to include disclosure of the specific criteria that will be used in agency review of applications. Appendix II provides the full text required for notices of funding opportunities.

The proposed guidelines specify that prior to making an award, an awarding agency 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, among other criteria.

Subchapter C – Federal Award Notice

Subchapter C provides guidance regarding the information that Federal awarding agencies must include in their notices of Federal awards to awardees and the general public for certain awards (e.g., a unique award identification code, Federal award project description, date and amount of award). The proposed guidelines include a requirement to provide formal notice to the general public of awards above \$25,000. This section also requires that awarding agencies provide notice to grantees of the specific terms and conditions included in their award.

Subchapter D – Inclusion of Terms and Conditions in Federal Award Notice

Grant and cooperative agreement awards must include the following general terms and conditions:

- Administrative and national policy requirements, including items such as the Federal Funding Accountability and Transparency Act of 2006, which includes guidance on executive compensation
- Agency, program, or Federal award-specific terms and conditions
- Award performance goals, including the timing and scope of outcomes intended to be achieved by the program

Appendix III to the proposed guidance includes specific “Contract Provisions for Recipient and Subrecipient Contracts.” These include termination provisions, Equal Employment Opportunity, Davis-Bacon Act when required, Access Rights, Debarment and Suspension, and the Byrd Amendment.

Subchapter E – Post Federal Award Requirements

This section puts forth the consolidated financial, administrative, procurement, and program management standards that had been encompassed in OMB A-110. In addition, the subchapter now incorporates new requirements for the monitoring and management of subrecipients and subawards, and consolidates requirements that were previously located in multiple OMB circulars. These requirements provide more clarity regarding the expectations on Federal awardees with respect to subrecipient and subaward oversight and management.

Record retention requirements have been clarified as part of the post-award requirements such that award recipients would be required to retain documents for three years after submission of the final expenditure report under an award.

Subchapter F – Cost Principles

Subchapter F establishes the consolidated principles for determining allowable costs incurred by non-Federal agencies under Federal financial assistance awards. Per the proposed guidance, agencies are not expected to place additional restrictions on individual items of cost. This subchapter consolidates OMB Circulars A-21, A-87, and A-122. Interestingly, the cost principles specific to hospitals (45 CFR Part 74) are maintained in Appendix X in the proposed guidance.

Entity-specific cost principle guidance and the entities to which they relate are included in the appendices. These appendices retain entity-specific cost allocation and indirect rate computation and negotiation practices that are historic and vary by entity type. The entity-specific guidance includes:

- Appendix IV – Educational Institutions
- Appendix V – Non-profit Organizations
- Appendix VI and VIII – State/Local Governments
- Appendix VII – Federally financed programs administered by State Public Assistance Agencies
- Appendix X – Hospitals (45 CFR 74 Cost Principles adopted as is)

Based on initial feedback received, OMB proposes to conduct further review of the cost principles for hospitals.

Subchapter G – Audit Requirements

This subchapter sets forth the consolidated audit standards for non-Federal entities receiving Federal financial assistance awards. This subchapter replaces previous OMB Circular A-133. Most significantly, the threshold triggering a single audit or program-specific audit requirements is proposed to be increased to \$750,000 or more in annual Federal awards. These requirements will apply equally to recipients and subrecipients under Federal programs. The proposed guidelines incorporate an exception to these audit requirements for non-U.S. based entities expending Federal awards.

PROPOSED REFORMS

One overarching principle driving the Proposed Uniform Guidance is a desire for sweeping reform and standardization of the existing requirements for Federal financial assistance awards that currently differ across agencies and by type of entity receiving awards. The primary reforms that OMB is attempting to accomplish with the proposed guidance are discussed below.

Proposed Changes Related to Indirect Cost Rates

Use of Indirect Rates Over Four Years

The Proposed Uniform Guidance would provide all entities the option of extending negotiated indirect cost rates for up to four years subject to approval of the indirect cost-cognizant agency. This one-time extension will only be approved if there have been no major changes in indirect costs.

If an extension is granted, the entity would not be allowed to request a rate review until the extension period ends. The OMB's stated desire is that the extension of the negotiated rate may provide a reduction in burden by reducing the frequency of negotiations.

Use of Flat Rate for Entities without Negotiated Rates

The Proposed Uniform Guidance also allows those entities without negotiated rates to utilize a minimum flat rate of 10 percent of modified total direct costs to recover indirect costs. The minimum flat rate would be permitted for a period no longer than four years, in which time it is anticipated that the entity would develop the capacity to develop and negotiate its own indirect rates.

Pass-through Entities Honoring of Indirect Rates

The Proposed Uniform Guidance would require pass-through entities (i.e., prime recipients or higher-tier awardees) to either honor the indirect cost rates negotiated at the Federal level for subrecipients, negotiate a rate in accordance with Federal guidelines, or provide the 10 percent minimum flat rate. This new provision is designed to ensure that entities who receive Federal funds primarily through a pass-through are appropriately reimbursed for the allowable costs associated with the award of funds.

Examples of Indirect Cost Proposal Documentation Requirements

The cost principles for nonprofit organizations as currently contained in OMB A-122 do not provide examples of indirect cost proposals or of documentation required to support such proposals. However, examples do exist in cost principles applicable to other entities.

In the Proposed Uniform Guidance, OMB has decided to eliminate examples of indirect cost proposals for all entities. OMB intends to provide guidance on documentation for justification of indirect cost rates in the form of a future instruction manual.

Certification of Indirect Costs

The Proposed Uniform Guidance includes a provision whereby organizations receiving grants and cooperative agreements will be required to certify indirect costs in connection with Negotiated Indirect Cost Rate (NICRA) submissions. Currently, similar requirements exist for some entities; however, the requirement is not found in all existing OMB Circulars. Examples of certifications are included in the appendices to the proposed guidance. The proposed certification is as follows:

CERTIFICATION OF COST ALLOCATION PLAN

This is to certify that I have reviewed the cost allocation plan submitted herewith and to the best of my knowledge and belief:

(1) All costs included in this proposal [identify date] to establish cost allocations or billings for [identify period covered by plan] are allowable in accordance with the requirements of OMB guidance, “Uniform Guidelines for Grants and Cooperative Agreements” and the Federal award(s) to which they apply. Unallowable costs have been adjusted for in allocating costs as indicated in the cost allocation plan.

(2) All costs included in this proposal are properly allocable to Federal awards on the basis of a beneficial or causal relationship between the expenses incurred and the awards to which they are allocated in accordance with applicable requirements. Further, the same costs that have been treated as indirect costs have not been claimed as direct costs. Similar types of costs have been accounted for consistently.

I declare that the foregoing is true and correct.

Name of Organization: _____

Signature: _____

Name of Official: _____

Title: _____

Reforms to Cost Principles

For the most part, these “reforms” are primarily a consolidation of existing cost principles currently in OMB Circulars A-21, A-87, and A-122; and the Cost Principles for Hospitals in the Department of Health and Human Services’ Regulations (45 CFR Part 75, Appendix E) into a uniform set of cost principles for all grant and cooperative agreement recipients, regardless of entity type. The goal of the reform is to reduce confusion on the part of Federal agencies, auditors, and pass-through entities that deal with more than one type of grant recipient entity. OMB has proposed to perform further review of the cost principles for hospitals, as they are essentially incorporated as they stand today in Appendix X.

Detailed Discussion of Proposed Cost Principle Revisions Impacting Award Recipients

The Proposed Uniform Guidance incorporates a number of extensive changes to existing cost principles that warrant further discussion. These changes may significantly impact award recipients.

Standards for Substantiating Time and Effort

OMB has introduced possible alternatives to current reporting requirements for validating the costs of salaries and wages (i.e., time reporting requirements). The alternatives to time and effort reporting are a result of OMB’s long-term goal of tying assessment to the achievement of programmatic objectives rather than measurement of effort (hours) expended. OMB acknowledges, however, that time-and-effort reporting is considered an important tool for the audit community. Within the proposed guidance, OMB has consolidated reporting requirements that previously differed

across types of entities and eliminated specific examples in an attempt to clarify the broad principles as to how an entity may establish the internal controls that would allow it to validate each employee's compensation (professional or nonprofessional) charged in whole or in part, directly to Federal awards.

The Proposed Uniform Guidance establishes the following alternative methodology for documenting compensation and personnel costs:

1. For employees in single indirect cost activity functions: no documentation beyond the payroll distribution system
2. For employees who work on a single direct project during a specific period: periodic (no less than semi-annual) certification signed by the employee or the employee's supervisor that the employee worked only the one project during the certification period.
3. For employees whose compensation is charged, in whole or in part, direct: documentation in the form of certified reports reflecting the distribution of charges within the employee's payroll report. Reports may be certified by the employee or the employee's supervisor(s).

Clarifying Criteria for Direct Charge of Directly Allocable Administrative Support

OMB's intent with these changes is to ensure that all costs for administrative support costs directly associated with a Federal award are appropriately classified to the award. The movement reflects a less-strict interpretation of direct costs, wherein any item or activity may be charged directly to a grant if it is clearly allocable to that award, as opposed to an activity that supports multiple projects. The type of task performed will not be relevant to this determination.

Treating Certain Computing Devices as Allowable Direct Supplies Cost

Per the Proposed Uniform Guidance, computing devices below an entity's capitalization threshold would be treated within the category of costs contemplated as supplies, without further requirements to add a line item in the budget for such devices.

Cost for Collecting Improper Payments

The Proposed Uniform Guidance introduces a new cost principle for costs incurred for the collection of improper payments. Per the proposed guidance, the costs incurred by a recipient to recover improper payments are allowable as either direct or indirect costs, as appropriate.

Contingency Provisions on Certain Awards

Recognizing that the budgeting of contingency funds associated with Federal awards for the construction or upgrade of a large facility or instrument, or for information technology systems, is an acceptable and necessary practice, and that the method by which contingency funds are managed and monitored is at the discretion of the Federal funding agency, the proposed guidance provides clarification in distinguishing such contingency funds as allowable and separate from otherwise unallowable contingency reserves.

Clarification of Cost Principles for Information Technology and Software

The Proposed Uniform Guidance has made provisions that treat general interest on debt (or financing costs) to acquire, construct, or replace capital assets as allowable. Per the proposed guidance, beginning January 1, 2016, these capital assets will include intangible assets, such as patents and computer software. The software may be developed for internal use, developed for the recipient by a contractor, or acquired from a contractor. For software development projects, only interest attributable to the portion of the project costs capitalized in accordance with Government Accounting Standards Board Statement 51 is allowable.

In addition, the Proposed Uniform Guidance includes information technology systems among the equipment that, when no longer needed by the Federal program for which it was purchased, may be used to support other Federally funded activities.

Residual Inventory of Unused Supplies

In the Proposed Uniform Guidance, OMB has established \$5,000 as the threshold for an allowable maximum residual inventory of unused supplies as long as the cost was properly allocable to the original agreement at the time of purchase.

Provisions Related to Contracts Covered by Cost Accounting Standards (CAS)

The proposed OMB guidance attempts to address the issue of CAS-covered contracts awarded to entities covered by the guidance. Currently, neither OMB Circulars nor CAS address the inconsistencies between the requirements of the various cost principles and the requirements of CAS. In the Proposed Uniform Guidance, to the extent a CAS-covered contract is awarded to an entity subject to the guidance, the entity and the cognizant Federal agency would establish an advance agreement on how the entity will comply with applicable CAS requirements when estimating, accumulating, and reporting costs under CAS-covered contracts. Per the proposed guidance, the advance agreement will indicate whether CAS requirements would be applicable to other Federal awards.

While the proposed OMB guidance indicates that only one set of records needs to be maintained by the entity, the proposed guidance seems to suggest that an entity with CAS-covered contracts would have, in theory, two sets of cost accounting practices: one subject to CAS-covered awards and another subject to all other Federal awards.

As it relates to grants and cooperative agreements, OMB has removed from the guidance reference to CAS and eliminated the requirement for universities to file a CAS Board Disclosure Statement and have it approved by the awarding agency. This change applies only to the guidance for grants and cooperative agreements, and does not alter requirements per the Federal Acquisition Regulation and CAS as it applies to entities receiving awards in the form of contracts.

Individually and collectively, the cost principles within the proposed guidance have not been updated to address the vast differences in methodologies across the various organizations. In addition, with the exception of clarifying the applicability of CAS to contracts, the cost principles do not resolve the conflicts with CAS requirements that many of these entity types now wrestle with. This area seems ripe for additional comments and ongoing reform.

Reforms to Disclosure Requirements and Cost Accounting Practice Disclosures

The Proposed Uniform Guidance steps away from CAS requirements for filing CAS Disclosure Statements that currently exist in OMB-A21, “Cost Principles for Educational Institutions.” However, the proposed guidance states that it is “essential for all recipients to document their cost accounting standards and to provide auditors with any and all documentation required to satisfy audit inquiries.”

To that end, the OMB in the Federal Register Notice discusses the retention of existing A-110 requirements (currently at Subpart C, “Post Federal Award Requirements,” Section .21, “Standards for Financial Management Systems”) for recipients to document their cost accounting practices. These requirements have been incorporated into the Proposed Uniform Guidance at Subchapter E, “Post Federal award Requirements,” Section .502, “Standards for Financial and Program Management,” paragraph (c). OMB suggests that these requirements are sufficiently comprehensive. The Financial System Management requirements, as outlined in the Proposed Uniform Guidance, are summarized in the table below.

Proposed OMB Guidance Subrecipient Financial Management System Requirements

(1) Accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the reporting requirements set forth in section 505, “Performance and Financial Monitoring and Reporting.” If a Federal awarding agency requires reporting on an accrual basis from a recipient that maintains its records on other than an accrual basis, the recipient shall not be required to establish an accrual accounting system. These recipients may develop such accrual data for their reports on the basis of an analysis of the documentation on hand.

(2) Records that identify adequately the source and application of funds for Federally funded activities. These records shall contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, outlays, income, and interest.

(3) Effective control over and accountability for all funds, property, and other assets. Recipients shall adequately safeguard all such assets and assure that they are used solely for authorized purposes.

(4) Comparison of outlays with budget amounts for each Federal award. Whenever possible, financial information should be provided in the context of performance accomplishments of the award (e.g., unit cost data).

(5) Written procedures to minimize the time elapsing between the transfer of funds to the recipient from the U.S. Treasury and the issuance or redemption of checks, warrants, or payments by other means for program purposes by the recipient. To the extent that the provisions of the Cash Management Improvement Act (CMIA) (Pub. L. 101-453) govern, payment methods of state agencies, instrumentalities, and fiscal agents shall be consistent with CMIA Treasury-State Agreements or the CMIA default procedures codified at 31 CFR 205, “Rules and Procedures for Efficient Federal-State Funds Transfers.”

(6) Written procedures for determining the reasonableness, allocability, and allowability of costs in accordance with the provisions of the applicable Federal cost principles in this guidance and the terms and conditions of the Federal award.

(7) Accounting records, including cost accounting records, which are supported by source documentation.

These requirements are not disclosures of cost accounting practices, as the OMB suggests. They are, instead, the financial management requirements that have historically been applicable to institutions of higher education, hospitals, and not-for-profit organizations per the requirements of OMB A-110.

Reforms to Audit Requirements

The changes within the proposed guidance are primarily intended to combine the guidance in OMB A-133 and A-50 on Audit Follow-Up. The reforms include 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.

Concentrating Audit Resolution and Oversight on Higher Dollar Risks

The Proposed Uniform Guidance would raise the Single Audit threshold from \$500,000 to \$750,000. This would allow for audit focus and follow-up on higher-risk entities and provide administrative burden relief to roughly 5,000 non-Federal entities expending less than \$750,000 in Federal awards while maintaining single audit coverage over 99 percent of the funds currently covered.

The Proposed Uniform Guidance also modifies the process by which Major Program determinations are made. These changes include:

- Increasing the minimum threshold from \$300,000 to \$500,000 for a program to be Type A (Major)
- Refocusing the criteria of Type A programs as high risk when, during the most recent period, the program failed to receive an unqualified opinion, had a material weakness, or had questioned costs exceeding 5 percent
- Reducing the number of Type B programs that have to be tested as major programs from one-half to one-quarter the number of Type A programs
- Simplifying the calculation to determine relatively small Type B programs for which the auditor is not required to perform a risk assessment
- Reducing the minimum coverage required under the percentage-of-coverage rule from the current 50 percent for a regular auditee and 25 percent for a low-risk auditee to 40 percent and 20 percent, respectively

Questioned Costs

The proposed guidance would increase 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 would eliminate smaller dollar audit findings which require the utilization of resources for follow-up audits that are unlikely to indicate significant weaknesses in internal controls.

Streamlining Compliance Requirements

The proposed guidance would streamline the compliance requirements in the Circular A-133 Compliance Supplement. OMB proposes to limit the compliance requirements to the following:

- **Allowability:** Combined testing for allowed or unallowed activities and allowable costs. Testing would include elements of evaluating funding and matching.
- **Cash Management:** Testing of cash management to ensure the minimal time lapse between the transfers of funds from the U.S. Treasury or pass-through entity and the ultimate disbursement of the funds.
- **Eligibility:** An evaluation of eligibility to ensure those who received services or benefits, either directly or on behalf of someone else, were eligible to receive them and received them for the right amount (e.g., to assess whether benefits were provided in the right amount, to the right person, for the right purpose and the right time).
- **Reporting:** Evaluate Federal financial reports, performance reporting, claims for advances, and reimbursement; and to ensure amounts claimed as matching are accurate and include all activity of the reporting period, are supported by applicable accounting records, and are fairly presented in accordance with program requirements. This would also include review of documentation of amounts reported for matching.
- **Subrecipient Monitoring:** Testing to ensure that the pass-through entity only made awards to eligible entities; identified awards, compliance requirements, and payments to the subrecipient prior to disbursement; monitored subrecipient activities to ensure subrecipient compliance; and performed appropriate audit resolution.
- **Special Tests and Provisions:** Tests of requirements unique to the program.

Elements of compliance testing removed from the supplement (e.g., Davis–Bacon, Equipment and Real Property Management; Matching, Level of Effort, and Earmarking; Period of Availability of Federal Funds; Procurement and Suspension and Debarment; Program Income; and Real Property, Acquisition and Relocation Assistance) can be added into the Special Test and Provision testing upon request from the agency. These should only be added to the extent that compliance is required by statute, regulation, and when the agency makes a strong case for how noncompliance can increase the risk of improper payments, fraud, waste, or abuse.

It is OMB’s belief that by streamlining the requirements, the Compliance Supplement would be refocused to better target areas of risk, thereby reducing the audit burden on non-Federal entities and allowing agencies to concentrate their oversight and audit follow-up resources on the requirements targeting the highest risk of improper payments, fraud, waste, and abuse.

Comments to the Proposed Uniform Guidance were originally due on May 2, 2013. Per Federal Register notice on March 21, 2013 (Federal Register Vol. 78, No. 55), the comment period has been extended to June 2, 2013. Comments may be submitted at www.regulations.gov under docket OMB-2013-0001.

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APPENDIX B – DFARS PROPOSAL ADEQUACY CHECKLIST

Proposal Adequacy Checklist	
References	Submission item
GENERAL INSTRUCTIONS	
1. FAR 15.408, Table 15-2, Section I, Paragraph A	Is there a properly completed first page of the proposal per FAR 15.408 Table 15-2 I.A or as specified in the solicitation?
2. FAR 15.408, Table 15-2, Section I, Paragraph A(7)	Does the proposal identify the need for Government-furnished material/tooling/test equipment? Include the accountable contract number and contracting officer contact information if known.
3. FAR 15.408, Table 15-2, Section I, Paragraph A(8)	Does the proposal identify and explain notifications of noncompliance with Cost Accounting Standards Board or Cost Accounting Standards (CAS); any proposal inconsistencies with your disclosed practices or applicable CAS; and inconsistencies with your established estimating and accounting principles and procedures?
4. FAR 15.408, Table 15-2, Section I, Paragraph C(1)	Does the proposal disclose any other known activity that could materially impact the costs?
FAR 2.101, "Cost or pricing data"	This may include, but is not limited to, such factors as—(1) Vendor quotations; (2) Nonrecurring costs; (3) Information on changes in production methods and in production or purchasing volume; (4) Data supporting projections of business prospects and objectives and related operations costs;
	(5) Unit-cost trends such as those associated with labor efficiency; (6) Make-or-buy decisions;
	(7) Estimated resources to attain business goals; and
	(8) Information on management decisions that could have a significant bearing on costs.
5. FAR 15.408, Table 15-2, Section I, Paragraph B	Is an Index of all certified cost or pricing data and information accompanying or identified in the proposal provided and appropriately referenced?
6. FAR 15.403-1(b)	Are there any exceptions to submission of certified cost or pricing data pursuant to FAR 15.403-1(b)? If so, is supporting documentation included in the proposal? (Note questions 18-20.)

7. FAR 15.408, Table 15-2, Section I, Paragraph C(2) (i)	Does the proposal disclose the judgmental factors applied and the mathematical or other methods used in the estimate, including those used in projecting from known data?
8. FAR 15.408, Table 15-2, Section I, Paragraph C(2) (ii)	Does the proposal disclose the nature and amount of any contingencies included in the proposed price?
9. FAR 15.408 Table 15-2, Section II, Paragraph A or B	Does the proposal explain the basis of all cost estimating relationships (labor hours or material) proposed on other than a discrete basis?
10. FAR 15.408, Table 15-2, Section I, Paragraphs D and E	Is there a summary of total cost by element of cost and are the elements of cost cross-referenced to the supporting cost or pricing data? (Breakdowns for each cost element must be consistent with your cost accounting system, including breakdown by year.)
11. FAR 15.408, Table 15-2, Section I, Paragraphs D and E	If more than one Contract Line Item Number (CLIN) or sub Contract Line Item Number (sub-CLIN) is proposed as required by the RFP, are there summary total amounts covering all line items for each element of cost and is it cross-referenced to the supporting cost or pricing data?
12. FAR 15.408, Table 15-2, Section I, Paragraph F	Does the proposal identify any incurred costs for work performed before the submission of the proposal?
13. FAR 15.408, Table 15-2, Section I, Paragraph G	Is there a Government forward pricing rate agreement (FPRA)? If so, the offeror shall identify the official submittal of such rate and factor data. If not, does the proposal include all rates and factors by year that are utilized in the development of the proposal and the basis for those rates and factors?
COST ELEMENTS	
Materials and Services	
14. FAR 15.408, Table 15-2, Section II, Paragraph A	Does the proposal include a consolidated summary of individual material and services, frequently referred to as a Consolidated Bill of Material (CBOM), to include the basis for pricing? The offeror's consolidated summary shall include raw materials, parts, components, assemblies, subcontracts and services to be produced or performed by others, identifying as a minimum the item, source, quantity, and price.
Subcontracts (Purchased materials or services)	
15. DFARS 215.404-3	Has the offeror identified in the proposal those subcontractor proposals, for which the contracting officer has initiated or may need to request field pricing analysis?

16. FAR 15.404-3(c) FAR 52.244-2	Per the thresholds of FAR 15.404-3(c), Subcontract Pricing Considerations, does the proposal include a copy of the applicable subcontractor's certified cost or pricing data?
17. FAR 15.408, Table 15-2, Note 1; Section II, Paragraph A	Is there a price/cost analysis establishing the reasonableness of each of the proposed subcontracts included with the proposal? If the offeror's price/cost analyses are not provided with the proposal, does the proposal include a matrix identifying dates for receipt of subcontractor proposal, completion of fact finding for purposes of price/cost analysis, and submission of the price/cost analysis?
Exceptions to Certified Cost or Price Data	
18. FAR 52.215-20 FAR 2.101, "commercial item"	Has the offeror submitted an exception to the submission of certified cost or pricing data for commercial items proposed either at the prime or subcontractor level, in accordance with provision 52.215-20?
	a. Has the offeror specifically identified the type of commercial item claim (FAR 2.101 commercial item definition, paragraphs (1) through (8)), and the basis on which the item meets the definition?
	b. For modified commercial items (FAR 2.101 commercial item definition paragraph (3)); did the offeror classify the modification(s) as either—
	i. A modification of a type customarily available in the commercial marketplace (paragraph (3)(i)); or
	ii. A minor modification (paragraph (3)(ii)) of a type not customarily available in the commercial marketplace made to meet Federal Government requirements not exceeding the thresholds in FAR 15.403-1(c)(3)(iii)(B)?
	c. For proposed commercial items "of a type", or "evolved" or modified (FAR 2.101 commercial item definition paragraphs (1) through (3)), did the contractor provide a technical description of the differences between the proposed item and the comparison item(s)?
19. FAR 15.408, Table 15-2, Section II, Paragraph A	Does the proposal include a price analysis for all commercial items offered that are not available to the general public?
20. FAR 15.408, Table 15-2, Section II, Paragraph A(1)	Does the proposal support the degree of competition and the basis for establishing the source and reasonableness of price for each subcontract or purchase order priced on a competitive basis exceeding the threshold for certified cost or pricing data?

Interorganizational Transfers	
21. FAR 15.408, Table 15-2, Section II, Paragraph A.(2)	For inter-organizational transfers proposed at cost, does the proposal include a complete cost proposal in compliance with Table 15-2?
22. FAR 15.408, Table 15-2, Section II, Paragraph A(1)	For inter-organizational transfers proposed at price in accordance with FAR 31.205-26(e), does the proposal provide an analysis by the prime that supports the exception from certified cost or pricing data in accordance with FAR 15.403-1?
Direct Labor	
23. FAR 15.408, Table 15-2, Section II, Paragraph B	Does the proposal include a time phased (i.e.; monthly, quarterly) breakdown of labor hours, rates and costs by category or skill level? If labor is the allocation base for indirect costs, the labor cost must be summarized in order that the applicable overhead rate can be applied.
24. FAR 15.408, Table 15-2, Section II, Paragraph B	For labor Basis of Estimates (BOEs), does the proposal include labor categories, labor hours, and task descriptions—(e.g.; Statement of Work reference, applicable CLIN, Work Breakdown Structure, rationale for estimate, applicable history, and time-phasing)?
25. FAR subpart 22.10	If covered by the Service Contract Labor Standards statute (41 U.S.C. chapter 67), are the rates in the proposal in compliance with the minimum rates specified in the statute?
Indirect Costs	
26. FAR 15.408, Table 15-2, Section II, Paragraph C	Does the proposal indicate the basis of estimate for proposed indirect costs and how they are applied? (Support for the indirect rates could consist of cost breakdowns, trends, and budgetary data.)
Other Costs	
27. FAR 15.408, Table 15-2, Section II, Paragraph D	Does the proposal include other direct costs and the basis for pricing? If travel is included does the proposal include number of trips, number of people, number of days per trip, locations, and rates (e.g. airfare, per diem, hotel, car rental, etc.)?
28. FAR 15.408, Table 15-2, Section II, Paragraph E	If royalties exceed \$1,500 does the proposal provide the information/data identified by Table 15-2?
29. FAR 15.408, Table 15-2, Section II Paragraph F	When facilities capital cost of money is proposed, does the proposal include submission of Form CASB-CMF or reference to an FPRA/FPRP and show the calculation of the proposed amount?

FORMATS FOR SUBMISSION OF LINE ITEM SUMMARIES	
30. FAR 15.408, Table 15-2, Section III	Are all cost element breakdowns provided using the applicable format prescribed in FAR 15.408, Table 15-2 III? (or alternative format if specified in the request for proposal)
31. FAR 15.408, Table 15-2, Section III, Paragraph B	If the proposal is for a modification or change order, have cost of work deleted (credits) and cost of work added (debits) been provided in the format described in FAR 15.408, Table 15-2.III.B?
32. FAR 15.408, Table 15-2, Section III, Paragraph C	For price revisions/redeterminations, does the proposal follow the format in FAR 15.408, Table 15-2.III.C?
OTHER	
33. FAR 16.4	If an incentive contract type, does the proposal include offeror proposed target cost, target profit or fee, share ratio, and, when applicable, minimum/maximum fee, ceiling price?
34. FAR 16.203-4 and FAR 15.408 Table 15-2, Section II, Paragraphs A, B, C, and D	If Economic Price Adjustments are being proposed, does the proposal show the rationale and application for the economic price adjustment?
35. FAR 52.232-28	If the offeror is proposing Performance-Based Payments—did the offeror comply with FAR 52.232-28?
36. FAR 15.408(n) FAR 52.215-22 FAR 52.215-23	Excessive Pass-through Charges—Identification of Subcontract Effort: If the offeror intends to subcontract more than 70% of the total cost of work to be performed, does the proposal identify: (i) the amount of the offeror's indirect costs and profit applicable to the work to be performed by the proposed subcontractor(s); and (ii) a description of the added value provided by the offeror as related to the work to be performed by the proposed subcontractor(s)?

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