

A large aircraft carrier is shown at sea, viewed from an elevated perspective. The deck is filled with numerous fighter jets, and several crew members are visible on the deck. The ship's superstructure is prominent on the left side. The ocean is a deep blue, and the sky is clear.

# Hot topics in government compliance

January 10, 2018

# Agenda

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**DCAA update**

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**Small vs. large business government oversight**

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**2017/2018 National Defense Authorization Acts**

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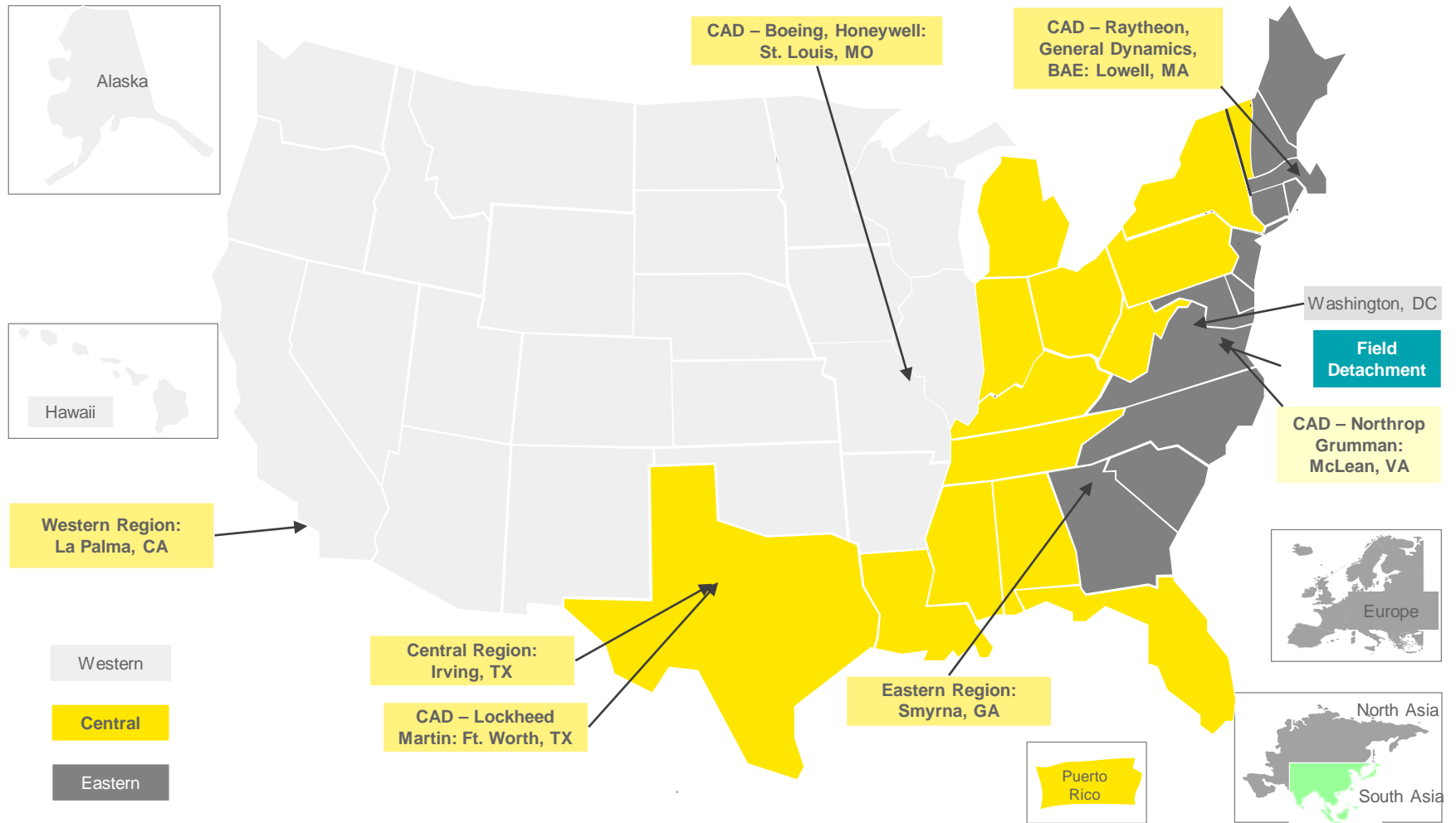
**Bios**

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# DCAA update

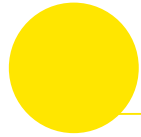


# DCAA reorganization



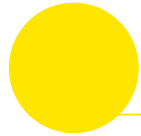
# DCAA FY 2018 priorities

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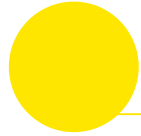
Meeting customers' needs on requested audits including meeting agreed-to-dates

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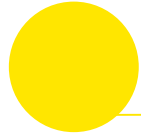
Completing incurred cost audits in a timely manner

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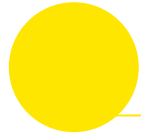
Performing high risk post award Audits (TINA/Truthful cost or pricing data)

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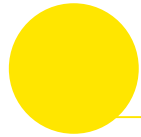
Performing high risk business system audits

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Completing termination audits in a timely manner

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Performing real-time testing of labor and materials

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# DCAA incurred cost strategy

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- ▶ Since BBP 2.0 (2013), it has been a DCAA goal to eliminate the Incurred Cost backlog
- ▶ DCAA approach
  - ▶ Developed a multi-pronged approach to working down backlog in an effective manner
    - ▶ Dedicated audit teams
    - ▶ Multiyear audit techniques
    - ▶ Increased staffing dedicated to Incurred Cost
    - ▶ Implementing a low-risk sampling approach to performing incurred cost audits

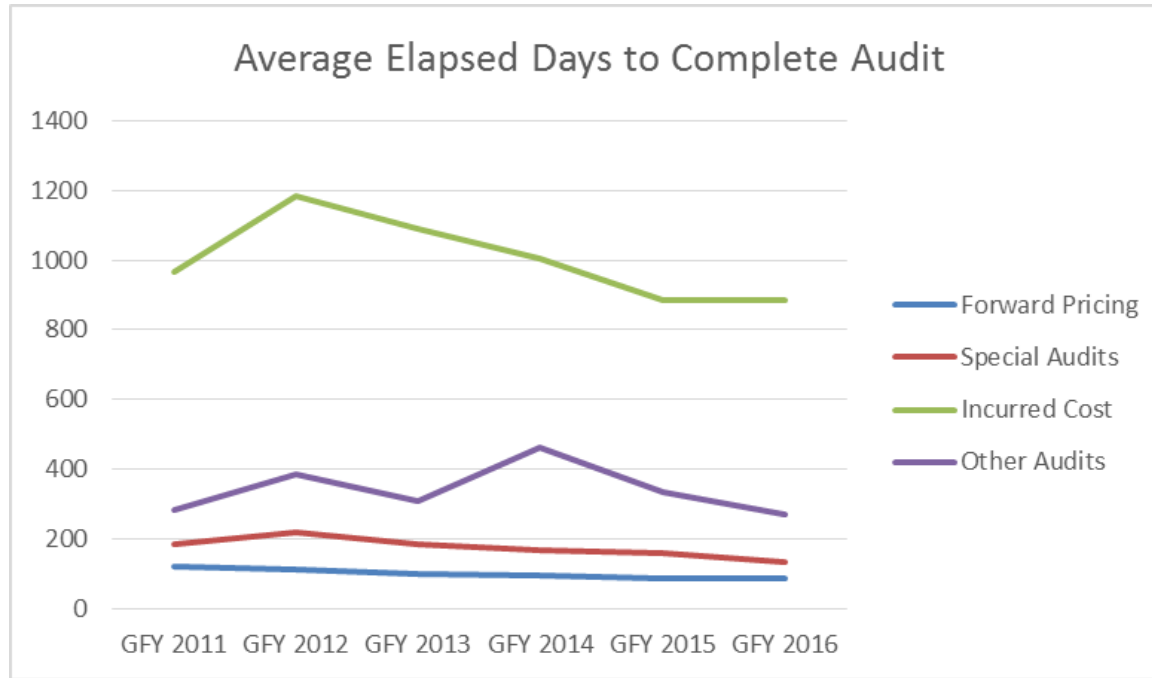
# DCAA forward pricing strategy

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- ▶ DCMA/DCAA Joint Communication Plan
  - ▶ Early coordination
  - ▶ Responsive to the buying commands
  - ▶ Eliminate duplication
- ▶ Tailoring audits to meet the customer's needs
- ▶ Timely completion of audits

# DCAA trends

## Number of days to complete audits GFYs 2012–2016



	Average Elapsed Days to Complete Audit					
Audit Report Type	GFY 2011	GFY 2012	GFY 2013	GFY 2014	GFY 2015	GFY 2016
Forward Pricing	120	110	97	95	85	86
Special Audits	184	217	184	165	159	133
Incurred Cost	965	1,184	1,090	1,006	883	885
Other Audits	283	384	309	461	333	268

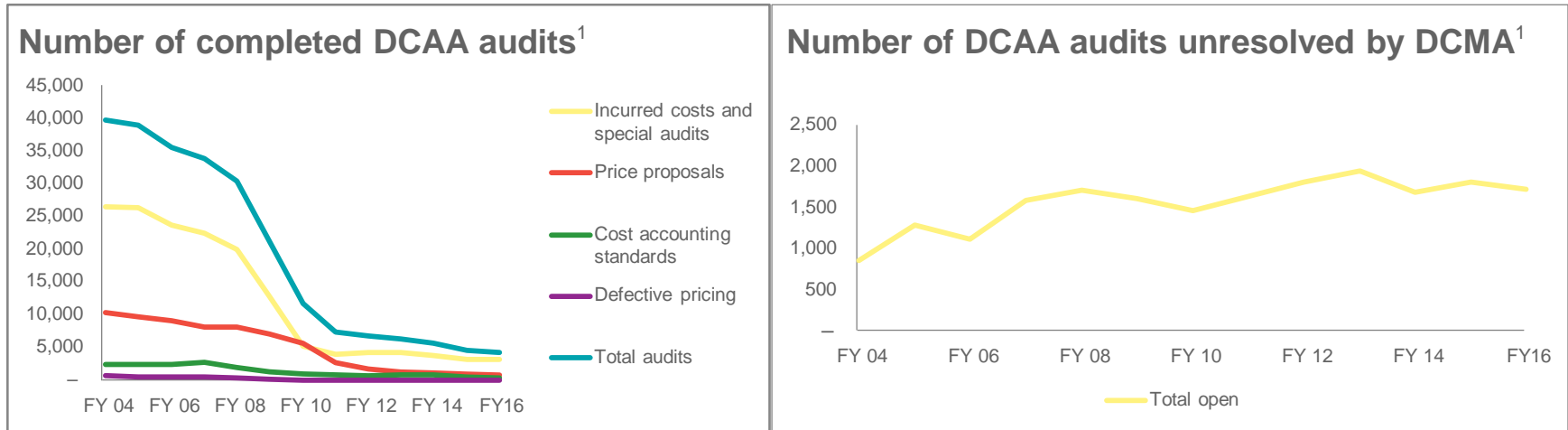
	Year-Over-Year Change					
GFY 2011	GFY 2012	GFY 2013	GFY 2014	GFY 2015	GFY 2016	
Forward Pricing	N/A	-8%	-12%	-2%	-11%	1%
Special Audits	N/A	18%	-15%	-10%	-4%	-16%
Incurred Cost	N/A	23%	-8%	-8%	-12%	0%
Other Audits	N/A	36%	-20%	49%	-28%	-20%

Source: DCAA Report to Congress on FY 2016 Activities, March 31, 2017. Graphical data prepared by EY's Government Contract Services.



# DCAA trends

## Completed DCAA audits GFYs 2004–2016



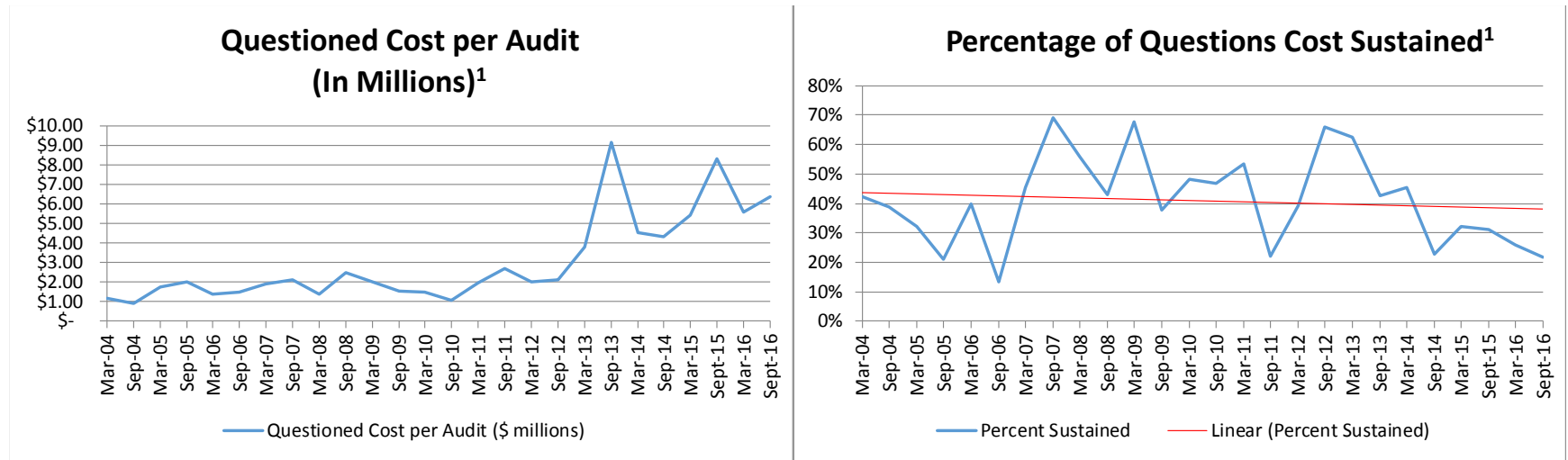
<sup>1</sup> From DoD-IG Semi-annual Reports to Congress  
Prepared by EY – Government Contract Services

Type of audits	Number of completed DCAA audits												
	FY 04	FY 05	FY 06	FY 07	FY 08	FY 09	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
<b>Incurring costs and special audits</b>	26,480	26,360	23,697	22,519	19,956	12,826	5,166	3,886	4,189	4,187	3,796	3,214	3,085
<b>Price proposals</b>	10,299	9,673	9,015	8,182	8,113	7,004	5,590	2,599	1,811	1,316	1,089	883	873
<b>Cost accounting standards</b>	2,340	2,426	2,413	2,648	1,927	1,292	916	874	680	725	779	423	276
<b>Defective pricing</b>	586	562	485	452	356	154	59	31	37	31	24	26	35
<b>Total audits</b>	39,705	39,021	35,610	33,801	30,352	21,276	11,731	7,390	6,717	6,259	5,688	4,546	4,269

Source: Previously issued annual DoDIG Semiannual Reports to Congress. Graphical data prepared by EY's Government Contract Services.

# DCAA trends

## Questioned costs GFYs 2004–2016



<sup>1</sup>From DoD-IG Semi-annual Reports to Congress

Prepared by Ernst & Young - Government Contract Services

Source: Previously issued annual DoDIG Semiannual Reports to Congress. Graphical data prepared by EY's Government Contract Services.

# DCAA future approach

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- ▶ Moving forward – increasing the Agency audit effort in:
  - ▶ Business Systems audits
  - ▶ Post award audits
  - ▶ Real-time Labor and Material audits
- ▶ Eliminating the Incurred Cost backlog
- ▶ Creating an Incurred Cost Proposal portal

# Small vs. large business government oversight



# Moving from “small to large” business in DoD contracting

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- ▶ Probability of more frequent oversight reviews conducted by DCAA and DCMA based on increased government contracts and/or dollar thresholds
  - ▶ DCAA audits of \$10m > fixed price and \$100m > cost type proposals
  - ▶ More frequent labor floor checks throughout a fiscal year
  - ▶ Stepped-up evaluation of provisional billing and forward pricing rates
  - ▶ Increase probability of post award audits based on DCAA “risk based” approach
  - ▶ Reviews of purchase existence and consumption (DCAA MAARS 13)

# Moving from “small to large” business in DoD contracting

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- ▶ Cost Accounting Standards (CAS) coverage from modified to full coverage and applicable disclosure statement filings
- ▶ Potential CAS Cost Accounting Changes and related cost impact submissions required to government
- ▶ Inclusion of DoD Business System clause in contracts, DFARS 252.242-7005
- ▶ Added scrutiny over subcontract management, cost/price analysis, and commerciality
- ▶ More frequent requests from the government for data and “probing” based on analytic historical data requests and access to internal audit processes

# Purchasing system



# Regulations, guidance and applicability

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Business system	Contractor purchasing system
DFARS Contract Clause Guidance	DFARS 252.244-7001
Threshold Level and Attributes	<p>Awards expected to exceed \$25m over the next 12-month period include those represented by prime contracts, subcontracts under government prime contracts, and modifications.</p> <p>Notes: 1) contractor purchasing system review is not performed for a specific contract; 2) the head of the agency responsible for contract administration may raise or lower the \$25m review level if considered to be in the government's best interest.</p>
Exemptions	Firm-fixed-price contracts awarded on a competitive basis; competitively awarded fixed-price contracts with economic price adjustment; and FAR Part 12 qualifying sales or commercial items
Cognizant Audit/Review Authority	DCMA

Note: CPSR guidebook, published January 18, 2017, establishes the CPSR threshold at \$50m in annual sales (an increase over the \$25m threshold established in Federal Acquisition Regulation (FAR) 44.302)



# Purchasing system criteria

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- ▶ 24 criteria\* under the DFARS clause, in summary:
  - ▶ Defined segregation of duties for subcontracting functions
  - ▶ Periodic formalized training, focusing on public laws and regulations, prohibited practices and importance of segregation of duties
  - ▶ Source selection adequately documented, including sole source justification
  - ▶ Purchasing file maintenance and documentation retained
  - ▶ Pricing and negotiation with subcontractors documented
  - ▶ Clause flowdown

\*See full text for criteria DFARS [252.244-7001](#), Contractor Purchasing System Administration

# Historical CPSR findings

Summary information of CPSR findings from FY2016 which could result in corrective actions, inadequate determinations, and disapproval:

Finding	Material	Non material	No finding
Debarred suppliers	66	15	45
Anti Lobbying FAR 52.203-12	48		78
Price analysis	43	17	66
DPAS	34		92
FFATA	31		95
Sole Source justifications	27	18	81
Policies & procedures	20	74	32
Commercial Item determinations	15		111
Documentation	12	52	62
TINA	12		114
Flowdowns		31	95
Training		25	101
Internal review/audits		24	102
Purchase reqs.		20	106
Negotiation evidence		18	108

# Leading practices in CPSR preparation

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Our experience has shown that most contractors that successfully navigate a CPSR typically share the following traits:

- ▶ Minimum six-month preparation prior to expected on-site CPSR activity
- ▶ CPSR readiness team to perform a comprehensive review of key CPSR topics
- ▶ Risk assessment of purchase orders and subcontracts, including an assessment of award type, dollar value, volume and prior related DCAA/DCMA findings
- ▶ An initial detailed analysis of a sample of procurement files by parties external to the purchasing function (e.g., government compliance, third-party consultants, internal audit)
- ▶ Detailed analysis of current purchasing policies, procedures and practices against recent DCMA guidance
- ▶ Analysis and remediation of procurement files
  - ▶ Based on initial assessments, may be a broad scrutiny of files or focused on certain aspects (e.g., cost/price analysis, certifications, file organization)
  - ▶ Often choose to analyze all files in scope for the CPSR
  - ▶ Development of a detailed audit support strategy, including participation by executive management, communication strategies, plans for system and process walk-throughs highlighting controls, and plans to address known risk areas that could generate findings

# FY18 focus areas

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- ▶ Recent comments from DCMA leadership discussed the following areas as being important for FY2018 CPSRs
  - ▶ Renewed emphasis on commercial items
    - ▶ Documenting market research
    - ▶ Conducting robust price analysis
    - ▶ Reviewing commerciality assertions
  - ▶ Counterfeit parts
    - ▶ Only applies to CAS covered contractors
    - ▶ Inadequate system can trigger disapproval of Purchasing system and withholds
    - ▶ Clause must be included in subcontracts including commercial item contracts for electronics or anything containing electronic parts
    - ▶ DFARS 252.246-7008 Sources of Electronic Parts creates new notification requirements
  - ▶ Buy American is a new CPSR report element
    - ▶ Not a flowdown but prime must ensure that the requirements are met
    - ▶ Applies to all purchases above the micro-purchase threshold except COTS items

# 2017/2018 National Defense Authorization Acts



# Sec. 803

## Performance of incurred cost audits

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- ▶ DCAA must notify contractors within 60 days whether the submission is adequate
- ▶ DoD is required to use a qualified private auditor to perform a sufficient number of incurred cost audits to ensure:
  - ▶ Incurred cost audits are completed no later than one year after the receipt of a qualified incurred cost submission
  - ▶ DCAA is able to devote ample resources to high priority audits
  - ▶ Qualified private auditors are used to perform a substantial number of incurred cost audits on an ongoing basis to improve the efficiency and effectiveness of incurred cost audits
- ▶ Strong non-disclosure requirements can subject private auditors to criminal sanctions for unauthorized disclosure of contractor data

# Sec. 803

## Performance of incurred cost audits

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### **Timeline for selection of qualified private auditors:**

- ▶ By October 1, 2018, DoD must provide the HASC and SASC copies of its acquisition plan including:
  - ▶ Description of the incurred cost audits DoD determines are appropriate to be conducted by qualified private auditors
  - ▶ Estimate of the number and dollar value of incurred costs audits to be conducted by qualified private auditors for each year of FY 2019–2025
- ▶ By April 1, 2019, DoD must award an IDIQ contract to two or more qualified private auditors to perform incurred cost audits
  - ▶ DCMA or other “authorized entity outside of DoD” is then authorized to issue task orders to perform incurred cost audits when needed

# Sec. 803

## Performance of incurred cost audits

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### Materiality standards for incurred cost audits:

Incurred cost proposal value	Materiality thresholds
< or = \$100k	4% of Cost
> \$100k but < \$500k	\$2,000 + 2% of Cost
>\$500k but < \$1m	\$5,000 + 1% of Costs
>\$1m but < \$5m	\$8,000 + 0.9% of Costs
>\$5m but < \$10m	\$13,000 + 0.8% of Costs
>\$10m but < \$50m	\$23,000 + 0.7% of Costs
>\$50m but < \$100m	\$73,000 + 0.6% of Costs
>\$100m but < \$500m	\$153,000 + 0.52% of Costs
>\$500m	\$503,000 + 0.45% of Costs

Does not address treatment of any expressly unallowable costs



# Sec. 820

## Cost accounting standards

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- ▶ Per Section 820, DoD Contractors may present to DCAA a summary of audit findings prepared by a commercial auditor if the firm previously performed an audit of the allowability, measurement, assignment to accounting periods, and allocation of indirect costs of the contractor; and
  - ▶ Such audit was performed using relevant commercial accounting standards and relevant commercial auditing standards established by the commercial auditing industry for the relevant accounting period.
  - ▶ DCAA shall rely on commercial audits of indirect costs without performing additional audits, except in cases where the companies or business units have a predominance of cost-type contracts as a percentage of total revenue

Source: Report 114-80, National Defense Authorization Act for FY 2017, November 30, 2016

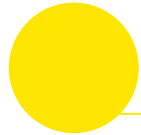
# Commercial Items

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- ▶ Section 846 – procuring commercial items from online marketplaces
- ▶ Section 848 – the DoD's use of commercial item procedures constitutes a determination that something is a commercial item
- ▶ Section 849 – review of DFARS for commercial items to be completed by December 18, 2018

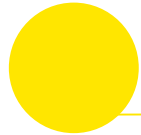
# Other highlights

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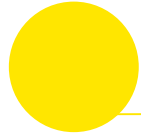
Section 805 increased the SAT to \$250k

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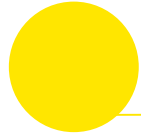
Section 806 increased the micro purchase threshold to \$10k

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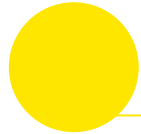
Section 811 increased the cost or pricing data threshold to \$2m

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Section 822 limits uses of LPTA

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Section 864 expands uses and thresholds for OTAs

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# DCAA rights to data and records



# DCAA rights to data and records

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- ▶ Access to records controlled under FAR 52.215-2, Audit and Records contract clause
- ▶ The government "... shall have the right to examine and audit all records and other evidence sufficient to reflect properly all costs claimed to have been incurred or anticipated to be incurred directly or indirectly in performance of this contract."
- ▶ "... right of examination shall include inspection at all reasonable times of the contractor's plants, or parts of them, engaged in performing the contract."
- ▶ "The contracting officer (or authorized representative) has the right to examine and audit all of the records (including computations and projections) in order to evaluate the accuracy, completeness, and currency."
- ▶ FAR 31.201-2 Determining allowability
- ▶ "A contractor is responsible for accounting for costs appropriately and for maintaining records, including supporting documentation, adequate to demonstrate that costs claimed have been incurred, are allocable to the contract, and comply with applicable cost principles in this subpart and agency supplements. The contracting officer may disallow all or part of a claimed cost that is inadequately supported."

# DCAA rights to data and records

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- ▶ Request can be verbal or in writing
- ▶ Time to retrieve or produce requested records needs to be “reasonable,” although DCAA’s standard of late is that records should be “readily available”
- ▶ Request should clearly state what support is needed and when it should be provided
- ▶ Request needs to be clearly defined for time periods, contracts covered, specific items ... unambiguous and not open ended
- ▶ Access does not mean uncontrolled access
- ▶ Electronic records are suitable as are paper copies
- ▶ Communicate with government representative(s) if clarification needed
- ▶ Don’t delay or ignore in responding to a formal request
- ▶ Avoid “Denial of Access to Records” determination

# What if DCAA is overreaching?

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- ▶ Communicate and clarify the nature and timing of the requested data
- ▶ Determine the relevance and availability of records requested – consider offering alternatives
- ▶ If records are lost, destroyed or stolen, or otherwise compromised, notify the DCAA and the ACO as well as internal legal counsel
- ▶ Request the DCAA auditor's supervisor be engaged in the conversation if a resolution cannot be achieved
- ▶ If the issue still cannot be resolved, elevate the issue, in writing, to the DCAA Field Audit Manager and engage with the DCAA Regional Audit Manager
- ▶ Finally, if mutual understanding still cannot be reached, the issue should be elevated, in writing, to a Senior Executive Service (SES) official at the cognizant DCAA Regional Office or DCAA HQ

# Contract closeout





# Contract closeout overview

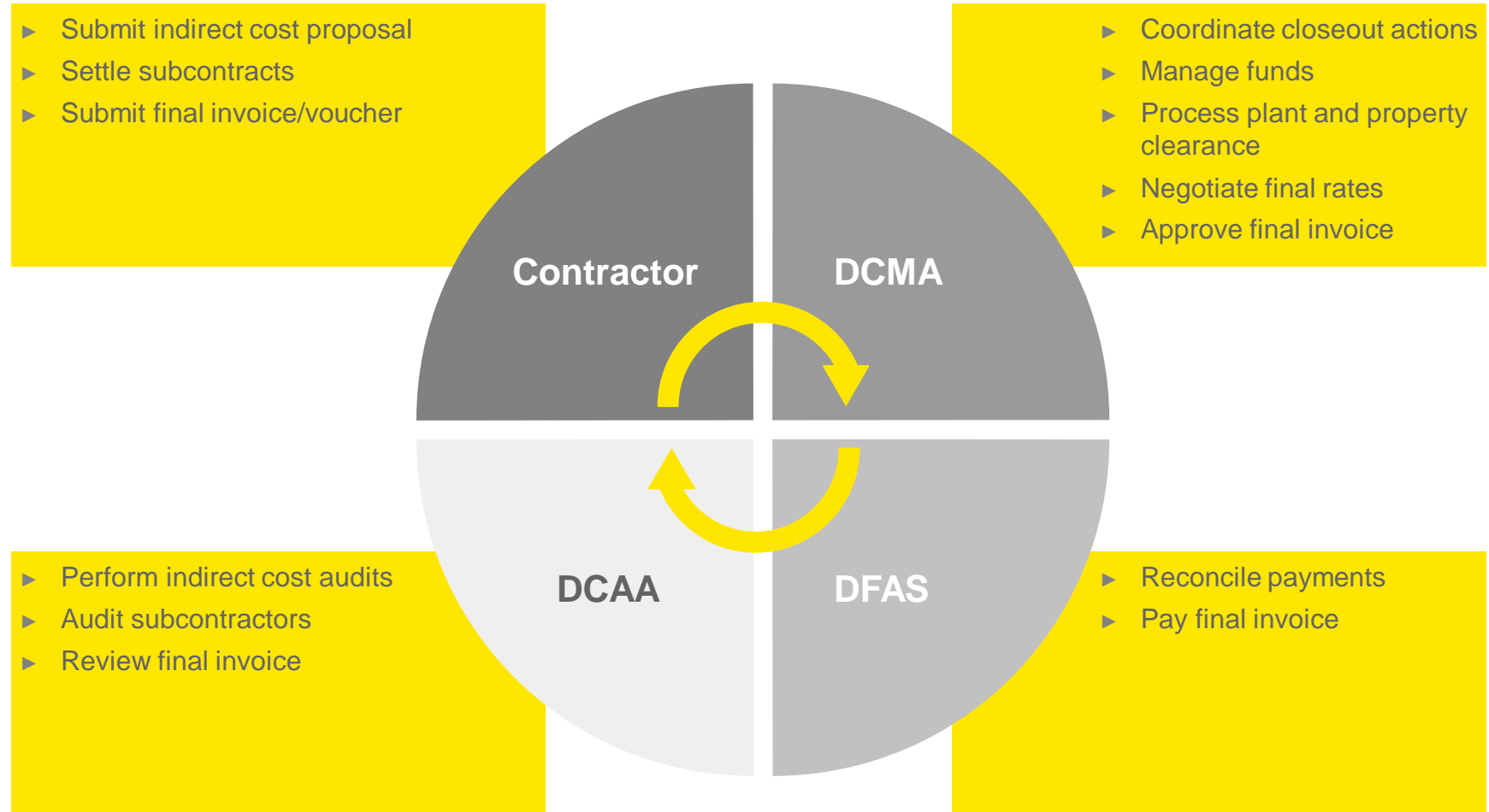
## What is contract closeout?

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- ▶ A process to finish or resolve all contractual requirements for a physically complete contract
- ▶ **The objective is to establish the final price and make the final payment.**
  - ▶ “Closeout is complete when all administrative actions have been completed, all disputes settled, and final payment has been made.” (DCMA Contract Closeout Guidebook)

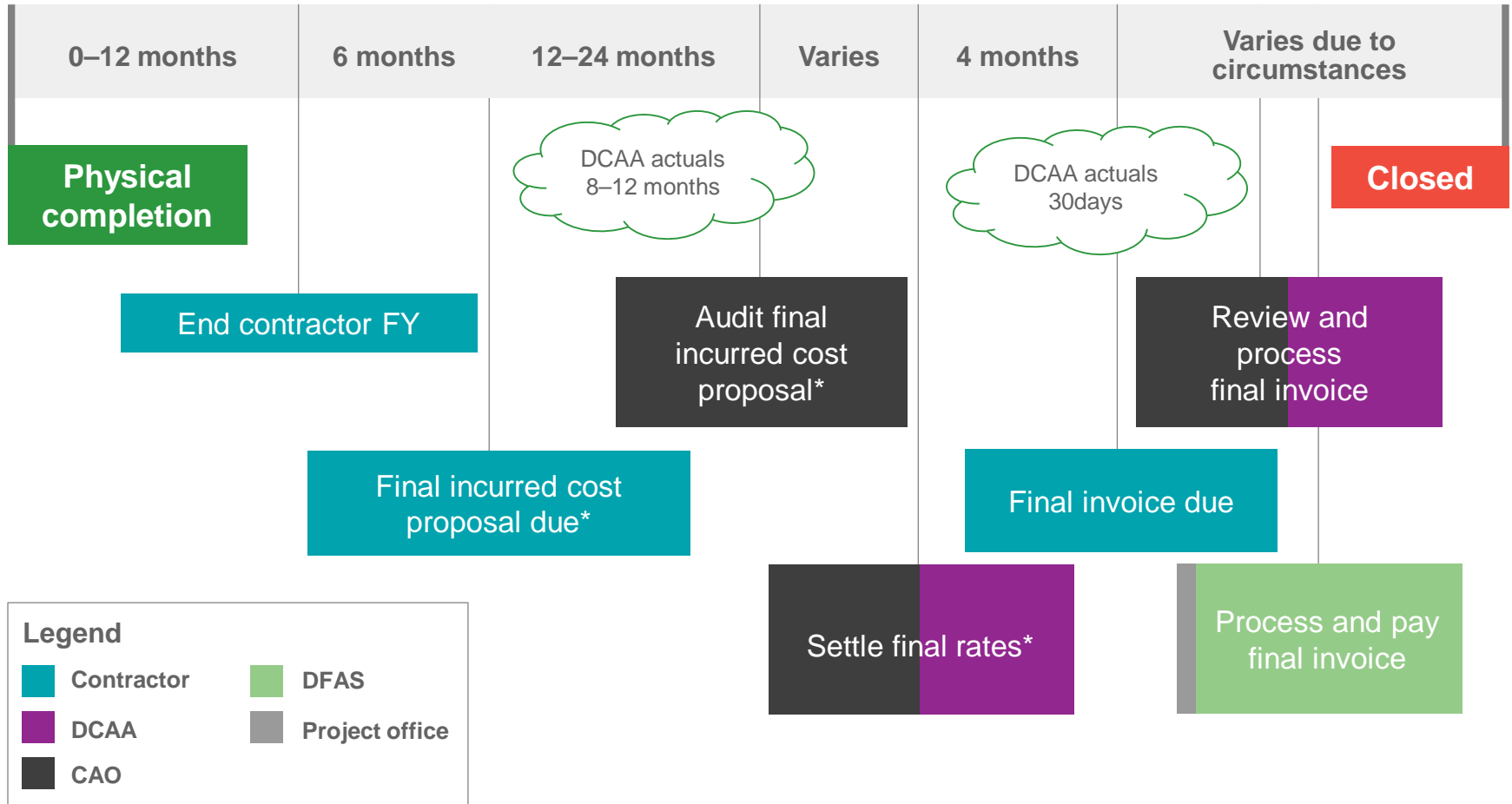
# Contract closeout overview

## Responsible personnel (DoD contracts)



# Contract closeout overview

## Timing guidelines



Source: DCMA

\* Not required for FFP contracts or CLINs – timeline should be reduced 30 months

# Contract closeout

## Leading practices

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- ▶ Retain detailed contract records
  - ▶ Contract type
  - ▶ Modifications
  - ▶ Currently active contracts
  - ▶ Contracts currently being bid on
- ▶ Develop a closeout plan
  - ▶ Assign roles and responsibilities in advance
- ▶ Actively manage inventory throughout the contract period of performance
- ▶ Exercise good recordkeeping skills and document control
  - ▶ Track costs and comply with requirements of Limitation of Cost/Funds Clause
  - ▶ Monitor indirect rates to mitigate payback responsibility

# Contract closeout

## Leading practices

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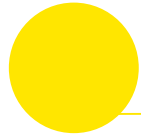
- ▶ Submit all Contractor requirements on time
  - ▶ Submit ICP six months after fiscal year end
  - ▶ True up all interim vouchers **60 days** after rates are settled
  - ▶ Close all subcontracts early
  - ▶ Once overhead rates are settled, prepare final voucher within **120 days**
- ▶ Identify any contracts that may be qualified for quick closeout
- ▶ Utilize available government guidance and resources
  - ▶ DoD Contract Closeout Checklist
  - ▶ DCAA CACWS
  - ▶ DCMA Contract Closeout Guidebook
  - ▶ DFAS Payment History Data

# Other areas



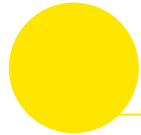
# Cybersecurity

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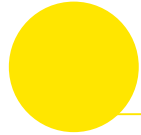
52.244-6 Subcontracts for Commercial Items

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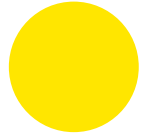
52.204-21 Basic Safeguarding of Covered Contractor Information Systems

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252.239-7010 Cloud Computing Services

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252.204-7012 Safeguarding Covered Defense Information and Cyber Incident Reporting

# Section 809 panel report

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- ▶ Section 809 interim report on simplifying acquisition was released in May 2017
  - ▶ Final report is expected in August 2018
  - ▶ A new award under the SAT would required the CO to address 431 clauses
    - ▶ 11 required clauses
    - ▶ 344 required if applicable clauses
    - ▶ 76 optional clauses
- ▶ Currently requesting help to identify the worst procurement regulations, laws and policies
  - ▶ <https://section809panel.org/50worst/>
  - ▶ \*Limited to 50



# Bios





**Ronald C. Meldonian, CPA**  
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### Background

- ▶ Ron Meldonian is an Executive Contractor in Ernst & Young LLP's Government Contract Services (GCS) practice. Prior to joining GCS, Ron had 34 years' experience in government contracting with the Defense Contract Audit Agency (DCAA) and was a member of DoD's Senior Executive Service (SES) for 9 years. His last position with DCAA was as Regional Director for the Northeastern Region which encompassed operational responsibility for 22 Field Audit Offices including overseas audit operations in Europe, Africa, the Middle East and Southwest Asia. Ron's extensive background has enabled him to speak at both government only and industry/government forums and conferences on multiple occasions.

### Skills and education

- ▶ Ron earned a Bachelor of Science in Accounting and a Master's in Public Administration from Suffolk University, Boston, Massachusetts
- ▶ A Certified Public Accountant (CPA) and Licensed Real Estate Broker in Massachusetts
- ▶ Member of the American Institute of Certified Public Accountants (AICPA)

### Experience

- ▶ With his extensive knowledge of Government Contracting, Ron is able to provide advice on a comprehensive array of services from proposal preparation, contract administration and closeout, indirect rate structures, incurred cost submissions, post-award audits, and review of applicable contract business systems. He has an in-depth knowledge of Generally Accepted Government Auditing Standards (GAGAS)
- ▶ Ron has wide-ranging operational experience and practical knowledge in the areas of Cost Accounting Standards, cost allocation, Federal Acquisition Regulation (FAR) and Defense Federal Acquisition Regulation Supplement (DFARS) contract provisions, including cost principles.
- ▶ Based on his broad operational and field experience, Ron brings common sense solutions and advice to existing and prospective government business opportunities. He is able to provide personalized direct consultation to clients and their senior executives who are responsible for conducting business with the US Federal Government.



**Timothy Ryan Manning, CPA, CFE, CIA and CISA**  
*Senior Manager*  
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### Background

- ▶ Timothy is a senior manager in the Fraud Investigation & Dispute Services (FIDS) practice and he is based out of the Boston, MA office. Timothy has been with FIDS for over 10 years and during this time and gained a broad range of experiences working on a variety of projects across many different industries. In more recent years he has focused on compliance matters for federal contractors. He has extensive experience related to key DoD business systems, Cost & Price analysis, indirect rates and responding to DCAA audit findings and corrective actions. Tim has worked on engagements related to CMS regulations, fraud investigations, forensic accounting reviews, and accounting remediation projects. He has also spent a portion of his career overseas supporting clients abroad. Timothy has managed multiple large teams and he has worked closely with many business functions such as Internal Audit, Supply chain, Contracts, and General Counsel's Office.

### Skills and education

- ▶ Timothy earned a BS in Business Administration in both Finance and Accounting from Western New England College
- ▶ A Certified Public Accountant (CPA), Certified Fraud Examiner (CFE), Certified Internal Auditor (CIA), Certified Information Systems Auditor (CISA)
- ▶ Professional affiliations include the American Institute of Certified Public Accountants (AICPA), Institute of Internal Auditors (IIA), National Contract Management Association (NCMA), the National Defense Industry Association (NDIA) and the Association of Certified Fraud Examiners (ACFE). Tim is also a CISA candidate.

### Experience

- ▶ Internal Audit Support – Timothy has been a lead, manager, and subject matter resource for clients conducting assessments of key business systems and performing other compliance audits. He has executed all phases of these engagements: planning, staffing, managing fieldwork, assessing weaknesses and risk factors, writing and presenting observations, and working to mitigate gaps. He has also supported other internal audit type projects such as reviews of policies and procedures.
- ▶ Supply Chain Compliance – Timothy has lead and support several engagements related to supply chain risks including CPSR preparation, remediation of corrective actions, subcontractor monitoring.
- ▶ Cost and Price Analysis – Timothy has supported multiple clients improve their processes for performing cost and price analysis on certified cost or pricing data provided by subcontractors. He has performed the analysis, liaising with subcontractors to make sure they understood the requirements, and managed teams of people performing the work.
- ▶ Rate Support – Timothy has worked on the review/audit of indirect rates for several different clients, including foreign clients (e.g., Japan). He has also been on two different engagements to help clients develop cost allocation plans.
- ▶ Overseas Government Remediation & Implementation – Timothy spent one year serving as the manager for the London-based accounting workstream on a large, highly confidential project for a government sector client. The project commenced in July 2009 with an investigation phase, and the project scope has subsequently transitioned to include assistance with the design and implementation of short-term, medium-term and long-term remediation actions. The project team has been led by FIDS, but includes team members from Advisory, Assurance, Tax, and TAS practices across the globe.

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