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newsletter

Government Contracts Consulting

Provided by Beason & Nalley, Inc.

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DCAA: The Continuing Declarations of Audit Independence

DCAA issued *Audit Guidance on Reporting Significant / Sensitive Unsatisfactory Conditions Related to Actions by Government Officials* (90-PAS-004(R), March 13, 2009) to significantly revise DCAA's processes for reporting such conditions.

In terms of defining the unsatisfactory conditions which may be reported, these include mismanagement, failure to comply with specific regulatory requirements or gross negligence resulting in substantial harm to the Government or taxpayers (although the "Government" and "taxpayers" would seem to be redundant--no doubt this has been added to avoid any future Congressional criticism, such as in 2008, that DCAA was to serve the taxpayers versus Government procurement or administrative contracting officers).

Examples of unsatisfactory conditions include a contracting officer which purposely excludes DCAA from performing or completing an audit to avoid a negative report or where a contracting officer ignores a DCAA report and takes action grossly inconsistent with procurement law or regulation.

Prior to the March 13, 2009 Audit Guidance Memo, issues with contracting officer "lack of support for DCAA audits" was almost exclusively a matter of raising the issue within the respective organizational chain of commands (e.g. DCMA and DCAA). Unless the unsatisfactory condition or action by a government official was illegal (e.g. a gratuity, bribe, kickback), DCAA never reported the action to an Office of Inspector General (OIG). In the future, the "most significant and sensitive issues" will now be reported to an OIG after the allegation goes through an internal DCAA review and approval process. However, only if DCAA Headquarters agrees with the assessment, will it go to an OIG.

Although DCAA's internal review process would seem to provide some reassurance that only the really important disagreements would go to an OIG, however, as with so many other government policies, "the devil is in the details". In this particular case, the "details" are the absence of definitions for reporting criteria coupled with the political climate impacting government contract audit and oversight. For example, how does the field auditor define "most significant" and/or "sensitive" as opposed to DCAA Headquarters' criteria for significant / sensitive? Regardless of differing views on significance, given that DCAA was strongly criticized for muzzling its field auditors, what are the chances that DCAA Headquarters will reject the action (not report it to the OIG) and risk a hotline call from the field auditor to the GAO or OIG?

Additionally, over the last few months, DCAA has changed its definitions of "significant" or reportable audit issues to the point that historically inconsequential

issues are not only reportable, but are now the basis for declaring a contractor accounting system as inadequate (reference DCAA Audit Guidance Memo 08-PAS-043(R), December 19, 2008). Given all that has occurred since July 2008 (the GAO report that certain DCAA Audits were not compliant with Government Auditing Standards), there is little question that in defining most significant and/or sensitive, DCAA will err in the direction of conservative/maximum reporting.

Over and above expectations that at least some actions (or inactions) by government officials will now be reported to an OIG, what are the other implications of the March 13 DCAA Memo?

Most obvious, that DCAA is wholly independent with respect to its traditional customers who are typically contracting officers. In this case, an unveiled threat that a contracting officer is in harm's way (of being second guessed by an OIG), if the contracting officer resolves a significant issue differently than as suggested by DCAA. Stated differently, regardless of the possibility that a DCAA audit opinion lacks merit, a contracting officer cannot exercise their contracting authority without repercussions in the form of the time and effort it will take to endure an OIG review. A risk averse contracting officer will almost always defer to the position of initial agreement with DCAA; thus a decision unfavorable to the contractor. A contracting officer willing to assume some risk will likely disagree with DCAA only after undergoing a rigorous internal review process which documents the basis for disagreement. In any case, disagreement with DCAA will become more structured and time-consuming; thus injecting additional time into the issue resolution process which has been insufferably long in most cases.

DCAA's March 13, 2009 memo will not only have a chilling effect on contracting officers, it will introduce an element of risk for everyone involved including the contracting officer as well as the DCAA field offices and the field managers. One reason DCAA has not historically invited the OIG in to referee is because the OIG will invariably review and second guess all related actions including some that are tangential at best. In other words, even if the disputed contracting officer decision is ultimately deemed to be the correct decision, there will be other secondary OIG observations which will require corrective actions (plans, actions and reporting).

Rest assured that internal disagreement between DCAA and a contracting officer on a significant issue will result in some after the fact OIG criticism(s) of actions by one or both. When they are invited into an issue, neither the OIG nor the GAO restricts themselves to the narrowly defined issue at hand.

It remains to be seen if the March 13, 2009 memo will actually change much within a contractor's overall dealings with contract audits and audit resolution. Recent experience has shown that many contracting officers have already succumbed to DCAA in the context of blindly endorsing DCAA audit opinions; however, the recent memo will give cause for other contracting officers to rethink their decisions which do not support a DCAA audit opinion. One more reason why audit issues, once reported, will be difficult to resolve.

FAC (Federal Acquisition Circular) 2005-32, Interim Rules for the Recovery Act

As published in the Federal Register on March 31, 2009 (Volume 74, Number 60), the subject FAC introduced a number of interim rules which should give one "cause to pause" before pursuing government contracts or grants which are funded by the Recovery Act (also known as the American Recovery and Reinvestment Act of 2009). The interim rules address six areas and we will briefly discuss three of those in this article.

Item II, FAR Case 2009-012, provides for Whistleblower Protections incorporated into FAR section 3.907 via contract clause 52.203-15. Employers are prohibited from discharging, demoting or discriminating against employees as reprisal for certain disclosures. If an employee makes such disclosures, he or she is protected without regard to the validity of the disclosure; moreover, the employee has almost no burden of proof (that retaliation has occurred) whereas the employer has substantial burdens in establishing that a subsequent act (unfavorable to the employee) was not retaliation.

Items V and VI (FAR Cases 2009-011 and 2008-026, respectively) pertain to GAO/IG access to contractors and subcontractors under contracts containing Recovery Act funds. This access includes the GAO right to interview contractor and subcontractor personnel with the agency IG limited to interviewing contractor personnel. The revised access to records provisions apply to commercial items and acquisitions under the simplified threshold to the extent either is funded by the Recovery Act.

The expanded GAO or IG authorities might also apply to existing contracts by virtue of the contracting parties' bilateral agreement to modify existing contracts to include the new clause. The preamble to the interim rule states that a contractor will not be eligible for Recovery Act funds if that contractor rejects the "bilateral" modification of its existing contracts. It seems to be confusing "unilateral" with "bilateral" but the end result is that a contractor can choose to play in the Recovery Act sandbox and allow the GAO/IG broad access authority or simply forego the opportunity to receive Recovery Act monies.

In addition to the three items discussed, the interim rules to the Recovery Act introduce Buy-American, Publicizing Contract Actions and Reporting Requirements with recipients of Recovery Act funds carrying most of the additional administrative burden. By any and all measures, a recipient of Recovery Act funds will experience no shortage of strings attached to these funds caused in large part by the early failings of oversight over government bailout programs. These strings attached (purposefully by the government without any measure of the hidden administrative costs) are what they are and as the adage goes, "he who controls the purse-strings wins".

White House & SBA Initiatives for Helping Small Business

The Acting Administrator of the U.S. Small Business Administration (SBA) recently announced a White House initiative in assisting small businesses to "address the economic challenges facing small businesses and entrepreneurs across the country".

Effective March 16, 2009, the SBA will:

- "Temporarily raise guarantees to up to 90 percent on SBA's 7(a) loan program, through calendar year 2009, or until the funds are exhausted. This increase in guaranteed levels will help provide banks with the greater confidence they need to extend credit during the current recession, will mean more capital available to small business owners around the country".
- "Temporarily eliminate fees for borrowers on SBA 7(a) loans and for both borrowers and lenders on 504 Certified Development Company loans, through calendar year 2009, or until the funds are exhausted. This will mean more capital available to small businesses at a lower cost. The fee elimination is retroactive to February 17, the day the Recovery Act was signed. SBA is developing a mechanism for refunding fees paid on loans since then".

The White House also noted that the Treasury Department will "commit up to \$15 billion to help unlock the frozen credit markets by purchasing small business loan securities currently frozen on the secondary market".

GAO Study Finds Small Business HUBZone Fraud and Abuse

At the same time as the SBA is addressing economic challenges faced by small businesses, it is also dealing with the fallout from the GAO study (GAO-09-440) which found continuing issues with HUBZone contractor misrepresentations.

Initially identified as a problem with the program in Washington DC, the GAO subsequently determined that contractor HUBZone misrepresentations extend into other locations (Alabama, Texas and California were examined). Basically, a

number of HUBZone contractors are not actually located in the designated HUBZone; in one case, the contractor address was a trailer in a mobile home park for which the occupant of the trailer had no connection whatsoever to the contractor.

As a result of the GAO study, the SBA process of approving HUBZone applications is taking significantly longer than the one-month goal and one can expect (or hope) that the SBA will strengthen its controls over various small business programs primarily to assure that small business self-certifications are valid. In other words, a company attempting to tap into the small business set-asides can expect that process will be more time consuming and subject to some scrutiny/validation.

Training Opportunities

2009 Beason & Nalley Sponsored Seminar Schedule

Fundamentals of Cost Accounting Standards

Date: June 4, 2009

Location: Beason & Nalley, Inc.
Huntsville, AL

Time: 8:15 am – 4:45 pm

FAR Part 31 Cost Principles

Date: June 23, 2009

Location: Beason & Nalley, Inc.
Reston, VA

Time: 8:15 am – 4:45 pm

Understanding Government Audits and How to Resolve Audit Issues

Date: August 4, 2009

Location: Beason & Nalley, Inc.
Huntsville, AL

Time: 8:15 am – 4:45 pm



Cost and Price Analysis in Government Contracting

Date: September 10, 2009
Location: Beason & Nalley, Inc. Huntsville, AL
Time: 8:15 am – 4:45 pm

FAR Part 31 Cost Principles Basics Class and Advanced Workshop

Date: November 17-18, 2009
Location: Beason & Nalley, Inc. Huntsville, AL
Time: 8:15 am – 4:45 pm (each day)

2009 Federal Publications Sponsored Seminars Schedule

A Practical Guide to Incurred Cost Submission

May 5-6 – La Jolla, CA
September 15-16 – Washington DC
October 20-21 – Las Vegas, NV

A Manager's Guide to EVMS

June 2-3 – Las Vegas, NV
November 5-6 – Washington DC
December 2-3 – Las Vegas, NV

Government Contract Accounting Systems Compliance

May 19-20 – Washington DC
June 16-17 – Las Vegas, NV
September 22-23 – Huntsville, AL
October 6-7 – Washington DC
December 8-9 – Las Vegas, NV

Government Contract Audits: Dealing with Auditors and Mitigating Audit Risk

June 10-11 – Las Vegas, NV
September 15-16 – Washington DC

Instructors

- Mike Steen
- Darryl Walker
- Scott Butler
- Chad Braley
- Courtney Edmonson
- Cyndi Dunn
- David Miller

Go to www.fedpubseminars.com and click on the Government Contracts tab or call Beason & Nalley, Inc. at 800-416-1946.

Specialized Training

Beason & Nalley, Inc. will develop and provide specialized Government contracts compliance training for client / contractor audiences. Topics on which we can provide training include estimating systems, FAR Part 31 Cost Principles, TINA and defective pricing, cost accounting system requirements, and basics of Cost Accounting Standards, just to name a few. If you have an interest in training, with educational needs specific to your company, please contact Ms. Sandra Baker at sbaker@beasonnalley.com, or at 800-416-1946.

Reader Inputs for Future Newsletters

Beason & Nalley, Inc. develops its topics based upon recent regulations, information, publicly accessible Government policies and our experience in assisting clients with regulatory compliance. However, we are also interested in the ongoing compliance experiences of our readers; hence, we invite your input in terms of suggestions for topics based upon your compliance experiences. Suggested topics along with any background information (i.e., your experience) should be sent to lmiller@beasonnalley.com.

Beason & Nalley, Inc. provides accounting, business, financial and consulting services with a focus on serving government contractors. Beason & Nalley, Inc. goes well beyond the bounds of what one would normally consider to be "typical" services. We provide services such as government contracts services, outsourced accounting, audit, tax and Deltek Costpoint® consulting and more. Our goal is to provide the business owner with options for their financially related administrative needs. Our service list is comprehensive. Contact us:

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