

newsletter

Government Contracts Consulting

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Inourcing Contractor Jobs: The Political Debate Continues

Senate hearings were held on May 20 to discuss the merits of bringing jobs currently held by contractors into the federal work force, with Senator George Voinovich, ranking member of the Senate Homeland Security and Government Affairs Subcommittee on Oversight of Government Management, chairing those discussions. The debate involved both members of the committee and witnesses to include representatives from the OPM, the government union NTEU, and the Professional Services Council (PSC).

The hearings stem from the presidential acquisition reform memo issued in March 2009, stressing the need to re-examine continued contracting out of those jobs that could be more effectively performed by federal employees. Following that memo, the OMB issued a proposed policy defining “inherently governmental” and “closely associated” with inherently government functions. The purpose of that proposed policy memo was to define those functions which should be performed completely or partially by federal employees.

Notable debate of this issue included concerns that, should data support the conversion of government contractor jobs to the federal work force, the federal hiring process lacked the capabilities to effectively and timely hire those personnel (as federal employees). Jeffrey Neal, an official at the Homeland Security Department, emphasized the possibility of directly converting existing contractor personnel to federal employees, and other testimony stressed that regardless of personnel whom are “insourced”, an extensive training program for new federal employees must be in place.

Mr. Alan Chvotkin, Executive Vice President of the Professional Services Council (PSC) cautioned against insourcing as a pre-conceived notion that moving private sector jobs to the federal ranks resulted in more effective and efficient job performance. Such a predetermined notion would be a mistake. Mr. Chvotkin noted that the first and foremost consideration for moving jobs currently held by the private sector to the federal employment work force should be a decision that best serves the interest of the taxpaying public.

Based on the dialogue we reviewed from these hearings, there appears to be a clearly skewed initiative for moving functions from the private to federal sector. Of interest, Ms. Maureen Gilman, legislative director of NTEU, one of the largest federal employee unions, commented that government agencies should be planning for the conversion of contractor to federal employees. Her comments clearly indicate a notion that substituting federal union employees in place of existing contractor positions results in more efficiency. NTEU also told the subcommittee “the explosion in contract spending has led to a drastic increase in the size of the contractor workforce, which has eroded the in-house capacity of agencies to perform many critical functions and has undermined their ability to accomplish their missions.” Whether that statement is based on factual data is questionable given that Ms. Gilman provided no empirical data to support her statement. Further, OFPP Administrator Daniel Gordon stated that “we need to improve hiring” (meaning federal agency practices) implying that the federal government is an “employer of choice”.

Interim Rule Restricts Use of Mandatory Arbitration Agreements

The Defense Department issued an interim rule on May 19 to restrict the use of arbitration in cases under title VII of the Civil Rights Act of 1964, or cases related to sexual assault or harassment. Government contractors that restrict settlement to arbitration for these offenses would not be considered for future Department of Defense contract awards.

The rule, which is effective immediately, was introduced by Sen. Al Franken, D-Minn., and purportedly resulted from experiences sustained by former female employees stationed in Iraq.

The new rule would restrict the DOD from awarding contracts, as well as task and delivery orders and contract modifications, to companies that use arbitration to settle claims of sexual assault or harassment, assault and battery, intentional infliction of emotional distress, false imprisonment, or negligent hiring, supervision or retention.

The rule would not apply to contracts awarded less than \$1 million or for the acquisition of commercial items. For those contracts to which the rule applies, prime contractors would be required to certify compliance on behalf of its subcontractors.

FAR Councils Consider Rule to Disallow Losses on Defined Benefit Pension Plans

OFPP (Office of Federal Procurement Policy) has requested the FAR Councils consider proposing a rule which would render unallowable investment losses associated with defined benefit pension plans. OFPP is associating these losses with a shortcoming within the existing rules (CAS 412-413) which allow the recognition of actuarial losses (and gains) to be amortized over a period of time. More specifically, the shortcoming is that the current approach does not incentivize contractors to make prudent investment decisions and management actions within the best interest of the taxpayers. Translated, to the extent a contractor's pension plan assets lose value because of market declines, those losses should be absorbed solely by the contractor because the contractor should have been more prudent within its investments.

Of note, OFPP seems to ignore the flip-side, which is the investment gains which have frequently eliminated the need for any current period funding. In many cases, these gains eliminated not only current period funding, but also any predictable funding within out-year forecasts, thus little or no defined benefit pension costs on current government contracts as well as in pricing future government contracts. In contrast, defined contribution pension plans may have investment gains and losses; however, there is no contractor accounting for such gains and losses which simply accrue to the favor or disfavor of the participants.

In spite of the government's willingness to readily accept the benefits of market gains when the markets are positive, oddly enough OFPP views it quite differently when the markets “go south”. In fact, OFPP seems to be silent with respect to the need for the regulations to address investment gains in a manner which would be consistent with non-recognition of investment losses. The apparent logic (or perhaps illogic), contractors who prudently manage pension assets within the best interests of the taxpayer would never have any losses. An ideal state achievable only if those investments are conservative to the point of producing minimal gains.

OFPP's request to the FAR Councils does not actually address investment losses, but would disallow costs which are attributable to “contractor behavior and practices with respect to pension plan assets, including but not limited to investment

decisions and strategies, excessive fees, mismanagement of plan assets and liabilities and excessive benefits”. In fact, FAR currently addresses all of these attributes in terms of FAR 31.201-3 “Determining reasonableness” and more specifically FAR 31.205-6 “Compensation for personal services”. However, reasonableness is essentially measured against one’s peers and when all or most of one’s peers are suffering pension plan investment losses, those losses are reasonable. OFPP apparently prefers that this longstanding concept of reasonableness be disregarded in deference to the ideal and unachievable state of never incurring any investment losses based upon the assumption that investment losses could be avoided by simply improving contractor behavior, practices and investment decisions.

Or more accurately, if a contractor suffers investment losses, the contractor simply cannot recover against government contracts notwithstanding the fact that the government will remain quite willing to share in the investment gains. Such a view is not exactly conducting business with integrity, fairness and openness as envisioned by the guiding principles of FAR 1.102(b)(3) and rather short-sighted on the part of OFPP given that the predictable impact of this proposed rule will be to increase pension costs. If subjected to this rule, contractors would have absolutely no incentive to invest in assets which could yield significant gains; hence, all but eliminating the many years in which defined benefit plans had no current costs combined with no costs estimated in a number of future years. At least historically, the “good years” have yielded significant investment gains which have more than offset the “bad years” with investment losses. How soon we (the government) forget.

DFARS Proposed Rule on Award Fees

In the wake of continuing criticism (Inspector General Reports, GAO Reports, and Congress) regarding award fees, DOD proposed a change to DFARS which would require the use of objective data in determining award fees and would eliminate provisional award fee payments.

Award fees continue to draw unwelcome attention, including a recent DOD-IG report regarding the award fee process used by the Army Corps of Engineers (USACE) in administering task orders in Iraq and Afghanistan (Report No. D-2010-049, dated April 1, 2010). In many cases, including the USACE task orders, the issue is the lack of objective criteria coupled with the lack of documentation to support the amount of the award fee. Unfortunately, in the absence of objective award fee criteria, it is highly predictable that documentation will fail any audit test because subjective criteria does not lend itself to audit verification or validation.

With respect to the elimination of provisional award fee payments the proposed rule would require that at least 40 percent of the award fee be held until the final evaluation; thus “encouraging performance” through the life of the contract. By implication, the proposed rule assumes that provisional award fee payments “discourage performance” through the life of the contract albeit supported by no empirical evidence that performance inexplicably deteriorates if award fees are provisionally paid. The final evaluation by the award fee official would be required within 45 days of the end of the performance period and the award fee would be consistent with the contractor’s performance against cost, schedule and measured outcomes.

Obviously the proposed rule will be a negative cash-flow consideration for any contractor faced with a potential award fee contract or task order and seemingly inconsistent with respect to contracts subject to EVMS (Earned Value Management Systems). The government incurs significant expense through its contractual requirements for EVMS for the purpose of tracking contractor performance against cost, schedule and outcomes; hence, it would be an obvious contradiction to rely on EVMS reporting other than for purposes of award fees on a provisional basis.

In any case, award fees are now under the microscope because of alleged failures by contracting officers in making award fee determinations and as with most every other procurement activity and new or revised regulation, when contracting officers fail, contractors ultimately bear the financial brunt of the revised rules and regulations.

Training Opportunities

2010 Beason & Nalley Sponsored Seminar Schedule:

June 17, 2010 – FAR Part 31 Cost Principles

Location: Reston, VA
Time: 8:15 AM – 4:45 PM
Cost: \$450 per person

June 24, 2010 – Fundamental Requirements of Cost Accounting Standards

Location: Huntsville, AL
Time: 8:15 AM – 4:45 PM
Cost: \$325 per person

September 16, 2010 – FAR Part 31 Cost Principles

Location: Huntsville, AL
Time: 8:15 AM – 4:45 PM
Cost: \$325 per person

October 21, 2010 – FAR Part 31 Cost Principles

Location: Reston, VA
Time: 8:15 AM – 4:45 PM
Cost: \$450 per person

November 9, 2010 – Understanding Government Audits and How to Resolve Audit Issues

Location: Huntsville, AL
Time: 8:15 AM – 4:45 PM
Cost: \$325 per person

November 17, 2010 – Cost and Price Analysis in Government Contracting

Location: Reston, VA
Time: 8:15 AM – 4:45 PM
Cost: \$450 per person

If you need additional information, please contact Lori Beth Miller at lmiller@beasonnalley.com or 256-533-1720.

2010 Federal Publications Sponsored Seminar Schedule

June 8-9, 2010, Las Vegas, NV – Government Contract Audits: Dealing with Auditors and Mitigating Audit Risks

June 9-10, 2010, Las Vegas, NV – A Manager’s Guide to EVMS

June 22-23, 2010, Las Vegas, NV – Government Contract Accounting Systems Compliance

July 13-15, 2010, Hilton Head, SC – The Masters Institute in Government Contract Costs

August 2-3, 2010, Arlington, VA – A Contractor’s Guide to the Incurred Cost Submission (ICS)

August 2-3, 2010, Arlington, VA – Government Contract Accounting Systems Compliance

August 4-5, 2010, Arlington, VA – Government Contract Audits: Dealing with Auditors and Mitigating Audit Risks

August 4-6, 2010, Washington, DC – The Masters Institute in Government Contract Costs

September 21-22, 2010, Seattle, WA – Government Contract Accounting Systems Compliance

October 13-14, 2010, Las Vegas, NV – A Contractor’s Guide to the Incurred Cost Submission (ICS)

October 19-20, 2010, Herndon, VA – Government Contract Audits: Dealing with Auditors and Mitigating Audit Risks

October 25-26, 2010, Washington, DC – Government Contract Accounting Systems Compliance

November 30-December 1, 2010, Las Vegas, NV – A Manager’s Guide to EVMS

December 6-7, 2010, Las Vegas, NV – Government Contract Accounting Systems Compliance

Instructors

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

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. Lori Beth Miller at lmiller@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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