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DCAA Audit Guidance on the Use of DCAA Form 1

On September 7, 2007, DCAA's Memorandum for Regional Directors (MRD) was issued as an audit guidance alert on the use of the DCAA Form 1 to suspend or disapprove costs on cost reimbursement contracts. Typically, an audit alert is issued to re-emphasize existing DCAA audit policy as opposed to new guidance. By implication, the audit alert is a reaction to DCAA's internal observations that a policy exists, but isn't being consistently or fully implemented. In the case of this recent MRD, the introductory sentence is very telling in terms of identifying the most likely internal policy compliance issue. The MRD states, "Auditors should issue a DCAA Form 1 to suspend significant unsupported indirect costs at audit determined contractor locations or direct costs (at both audit determined and contractor-negotiated contractors) until the required data are received and a determination can be made as to the allowability of costs". Beyond DCAA's expectations that auditors will follow policy, we believe that there was a very

obvious disconnect because numerous clients have experienced audit exceptions pertaining to "inadequate support"; yet we were not aware of any client receiving a DCAA Form 1 suspending costs during the audit and few, if any, with disapprovals with immediate cost withholds. Clearly, DCAA is now encouraging its auditors to consider and to utilize a DCAA Form 1 when the auditor encounters "unsupported costs" pertaining to direct and indirect costs incurred.

Will DCAA Forms 1 become ubiquitous? There is no obvious answer noting that a DCAA Form 1 introduces internal time, effort and cost for DCAA and equally for the paying office (e.g. DFAS). However, a DCAA Form 1 is leverage towards the DCAA objective of more timely support by contractors. The best contractor strategy is (and has always been) to implement and maintain adequate accounting system(s) which provide for adequate documentation as transactions happen. Although it's a cliché, "an ounce (or perhaps a few ounces) of prevention equals a pound of cure".

Adequate Supporting Documentation and Records Retention

The previous article makes note of the fact that DCAA has recently issued guidance concerning the DCAA Form 1. The issuance of that guidance is something of a wake-up call to anyone with government contracts subject to audit cost verification during or after contract performance. "During contract performance," in the context of an



interim audit of a public voucher, is typically not an in depth audit, but like any audit, the audit scope will be determined by the auditor. If supporting records aren't provided timely and/or if the records are not sufficient to establish cost allowability (which actually includes allowability, reasonableness or allocability as defined in FAR 31.201.2-4), the probable consequence is now more likely to be a DCAA Form 1 suspending the inadequately supported costs. The voucher will not be paid (or only partially paid) and the contractor will have the administrative burden of providing additional support (data, information or explanation). If the voucher was selected to re-validate direct billing, inadequate support accompanied by a DCAA Form 1 could also lead to the rescission of direct billing; an administrative headache for everyone and an unfavorable cash-flow issue for the contractor.

After contract performance (in conjunction with the audit of the annual incurred cost proposal), inadequate or insufficient documentation is the singular reason for the largest amount of audit exceptions. As noted in the previous article, DCAA Forms 1 were almost never used to suspend costs, notwithstanding the fact that any given audit report include significant exceptions based upon "inadequate documentation". In some cases, the documentation may exist, but it's simply not been timely provided to the auditor (i.e. perceptions of unreasonable delays by a contractor). In other cases, the documentation cannot be located (if it existed, it's not been located). In an issue involving inadequate support, there maybe a legitimate difference of opinion in terms of adequate or sufficient documentation; however, the solution is to provide the documentation if it's feasible to do so. If it isn't feasible, make certain that the "lack of documentation" is fully explained by the auditor and make certain that it isn't a record whose retention period has lapsed. FAR 4.700 defines Contractor Records Retention which is generally 3 years after final payment; however FAR 4.705 through 4.705-3 provides specific retention periods for specified records. For example, pay administration records have a range of 2 to 4 years with timesheets being the shorter retention period. With timely incurred cost submissions and timely audits, there are few specific records whose retention period will have lapsed, but always consider FAR 4.700 if missing records is an issue. Additionally, insufficient records can be supplemented after-the-fact notwithstanding the fact that auditing standards may implicate less reliance, particularly if the supplemental information is generated after the fact and it's internally generated. In contrast, missing records involving unrelated third parties can be requested from the third party (either copies of original documents or third party statements pertaining to specific transactions). In conclusion, DCAA

auditors are more likely to be less tolerant of (perceptions) of contractor delays and more likely to consider a DCAA Form 1 which actually withholds money from the contractor.

Training Opportunities

Government Contract Accounting Systems Compliance

Brief Synopsis:

This course is designed to detail the components of a government contract accounting system and explain how an accounting system helps to ensure your compliance with government contracting rules and regulations.

Presented by:

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Dates:

October 30-31, 2007, Washington D.C.
December 11-12, 2007, Las Vegas, NV

Instructors:

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Go to www.fedpubseminars.com and click on the Government Contracts tab or call Beason & Nalley at 256.533.1720.

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Future Newsletters

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