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Department of Defense (DoD) Proposes Change to Increase Payment Period on Cost Type Contracts

The Department of Defense (DoD) has issued a proposed change to the DFARS that would extend the interim payment period on invoices submitted by contractors under cost reimbursement service-related contracts.

DFARS 232.906 currently stipulates that payment for invoices, under these types of contracts, be made to contractors within fourteen (14) days after the payment office has received the invoice. The new rule would allow the DoD to extend that payment period to thirty (30) days, but only for companies not categorized as small businesses. In other words, the fourteen (14) day turnaround time would still apply to small businesses.

DOD concluded that extending the payment period to thirty (30) days would not contravene the Prompt Payment Act, and the change would allow the DoD “better cash management” in processing payment requests.

DCAA Guidance on Testing Compliance with New Rule on T&M Non-Commercial Contracts

DCAA issued new guidance to its auditors in a memo dated July 31, 2007, outlining audit responsibilities for ensuring compliance to a new FAR and DFARS rule for pricing and billing subcontractors.

The new rule, effective December 2006, requires that hourly labor rates for subcontractor work performed under non-commercial T&M and Labor Hour (LH) prime contracts be billed at the individual subcontractor’s hourly rates:

- For any DoD contract, whether competitive or non-competitive
- For any non-DoD contract, unless the award was made on the basis of adequate price competition

For non-DoD T&M and LH contracts awarded on the basis of adequate price competition, the rule allows subcontractor labor hours to be billed at the same schedule hourly rates as the prime contractor, often referred to as “blended rates” in other literature on this rule change.

DCAA has begun testing new contract awards, which include subcontractor labor hour effort, to ensure, among other things, that subcontractor hourly rates are the basis for forward pricing or billed labor dollars when such provisions are stipulated. The new provisions for T&M/LH non-commercial DoD contracts



have eliminated any opportunity for primes to bid or bill subcontractor effort at the prime hourly rates.

Compensation: One More Audit Challenge under FAR 31.205-6.

FAR 31.205-6 is, by any measure, the most ubiquitous regulation in terms of its coverage of many sub-components of compensation. In the January FAR, it encompasses nine pages and to the extent it incorporates (by reference) Cost Accounting Standards 412/413 (pensions) and 415 (deferred compensation), 31.205-6 is substantially more than nine pages. In fact, a very recent challenge by DCAA has further broadened the “other” regulations which could impact compensation costs associated with owners of closely held corporations.

All but overlooked, 31.205-6(a)(6)(iii) states that for owners of closely held companies, compensation in excess of the costs that are deductible as

compensation under the IRS Code (26 U.S.C) is unallowable. Although this FAR provision has fundamentally existed at least since the mid-1980's, in recent times it has almost never been cited as criteria used by DCAA to disallow compensation costs.



However, in a recent and ongoing development, DCAA has used this to challenge deferred compensation for company owners notwithstanding that these same costs were properly assigned under CAS 415. In the context of the relevant IRS code, one basic premise is that compensation is deductible to the corporation in the year it is taxable to the owner/employee. As the name implies, "deferred compensation" involves payments in future years, notwithstanding that the company has incurred an obligation (CAS 415.50). As recently applied by DCAA, we now have a "Catch-22" to the extent CAS 415 requires the costs be assigned to a current year, but the auditor interprets FAR 31.205-6 as disallowing the cost (until payment in a future year).

The other side of the "Catch-22", assuming the costs are claimed in a later year (when paid and taxable to the recipient), is that DCAA will presumably issue a CAS 415 non-compliance. This is even more ominous, if applied to pension costs (typically deductible to the corporation long before taxable to the owner/employee), which can result in a larger disconnect caused by conflicting regulations which can and do change independently of one another.

Perhaps the DCAA challenge will be logically resolved, as it should be; if not, "Houston, we have a problem."

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:

Federal Publications Seminars

Dates:

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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.

Specialized Training

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Future Newsletters

Beason & Nalley welcomes any feedback from the readers of this newsletter. We appreciate any suggestions that you may have as to future content, presentation and format, or interesting developments in the procurement community that would be of interest to our readers. Please provide any feedback or suggestions via our email address at dwalker@beasonnalley.com.

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