

Take a Memo, Please

Written by Nick Sanders
Monday, 24 June 2013 00:00

We all know that DCAA has developed a taste for checklists. It's not just DCAA; the DAR Council thinks checklists are a wonderful thing as well. As a result, they are busy [revising the DFARS](#) to make use of checklists mandatory. But unlike the DCAA checklists, the DFARS checklists are completed by contractors and submitted to a Contracting Officer for review. The DCAA checklists are completed by auditors and, [in some circumstances](#), can actually take the place of a detailed, GAGAS-compliant audit addressing the allowability, allocability, and reasonableness of a contractor's claimed final direct and indirect costs.

For those contractors whose interaction with DCAA is limited to the auditor filling-out the checklist to assure that the proposal to establish final billing rates (aka "the incurred cost proposal") is adequate—in the eyes of DCAA—what happens next? Well, DCAA will issue a Memorandum to the cognizant Administrative Contracting Officer (ACO) "listing the audit steps taken to assure that the contractor's submission was 'adequate' and DCAA's internal records will record that the contractor's submission was audited, but that no report was issued. Questioned costs and total exception dollars will be reported as being zero.

A DFARS Class Deviation was issued by the Director, Defense Procurement and Acquisition Policy (DPAP) that permits DCMA Contracting Officers to use the DCAA Memoranda "for purposes of satisfying the audit requirements at FAR 4.804-5(a)(12), 42.705-1(b)(2), and 42.705-2(b)(2)(i)." Since the DCAA Memoranda will not show any recommended cost disallowances, we assume that DCMA will simply accept the dollars and indirect rates proposed by the contractor, and establish final billing rates on that basis.

What Congress will do when somebody tallies up the amount of dollars not audited by the Defense Contract Audit Agency remains to be seen.

But of course that's not the end of the story. As [we told our readers](#), DCAA will also issue Memoranda in lieu of GAGAS-compliant audit conclusions supported by evidentiary matter as contractors' submissions near (or pass) the six-year statute of limitations found in the Contract Disputes Act. We've been told that those Memoranda will contain recommended disallowances and/or cost decrements based on average questioned cost issues related to that year (for partially completed audits) or based on average questioned costs related to prior years (for audits not performed at all). The key point is that DCAA will not be expressing a conclusion—just telling the CO about some issues—and so the agency believes it can issue

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these Memoranda without getting gigged for GAGAS noncompliances.

DCAA's track record on GAGAS compliance is [not particularly noteworthy](#), according to the DOD Inspector General. The agency can certainly reduce the risk of future scathing IG reports if it stops issuing audit reports. What Congress, GAO, and the IG will make of DCAA's new risk-reduction strategy remains to be seen.

The onus will be on the DCMA COs and ACOs to establish final billing rates based on those Memoranda. There will be decrements and recommended disallowances, but it seems that those recommendations will be built on a foundation of sand, in terms of support. In other words, our information is that DCAA will be unable (or perhaps unwilling) to support the contents of the Memos, because they will generally lack much (if any) evidentiary support. We predict the situation is going to leave the DCMA folks in a quandary, especially if the contractor pushes back.

Our best information at this time is that if the DCMA CO/ACO believes the DCAA-recommended decrements lack merit or cannot be defended, then the contractor's proposed costs and rates *will be accepted and used to establish final billing rates*.

Of course, DCAA's penchant to issue Memoranda in lieu of formal audit reports is not particularly new. It first came to our attention in connection with the now infamous [Contractor Recovery Initiative](#)

. In 2011, DCAA issued [special audit guidance](#)

to permit its auditors to support this high-priority Pentagon initiative. The audit guidance permitted DCAA auditors to calculate their own Rough Order of Magnitude (ROM) estimates of the dollars allegedly owed to the Government from CAS noncompliances and voluntary changes in cost accounting practice, and to issue those ROMS without worrying about pesky requirements such as GAGAS. We suspected at the time that that cunning plan was not going to go well for either DCAA or DCMA.

While we don't have a lot of evidence as to whether or not our suspicions will be validated, we note (for the record) that the four CAS matters Raytheon [recently argued](#) at the ASBCA were each generated out of the Contractor Recovery Initiative. Raytheon prevailed on three of the four, based on untimely Government claims. The fourth matter will be litigated on the merits, and the resulting decision will give us some insight into how well DCAA and DCMA fare

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in their strategy.

You had better get used to DCAA-issued Memoranda. Until somebody—be it the Courts, Congress, or Pentagon leadership—decides that such Memos are a poor substitute for actually doing audit work in compliance with GAGAS, they seem to be the new norm.