Accounting System Review - What’s a Contractor to Do?

Companies face many challenges while trying to grow in the government contracting marketplace. Initially a company needs to identify a category of goods or services to provide and an agency that is in need. Once the first contract establishes a beachhead on the government contracting world, the desire for more work and larger programs is inevitable. One of the toughest hurdles is working through the fierce competition to be awarded more desirable contracts. This can be problematic when a company is not prepared when a Request for Proposal (RFP) requires that the bidder provide evidence that its accounting system is “adequate.”

Many RFPs for government contracts will list a requirement for a potential contractor’s accounting system to be deemed adequate prior to award. Unfortunately, many RFPs are not clear as to what level of documentation is required, and some stated requirements are simply impossible or unnecessary to attain prior to contract award. To add to the challenge, many prime contractors are requiring their subcontractors to demonstrate compliance with accounting system benchmarks - even when the subcontractor is not bidding on a cost reimbursable subcontract. This requirement results in many contract and subcontract awards being unnecessarily delayed and require companies to spend overhead or general and administrative (G&A) dollars to attain an approval that is not required and may not benefit the work in the long run. This “requirement” is misplaced since the only requirement contained in the Federal Acquisition Regulation (FAR) is located at FAR 16.301 which prohibits the award of a cost reimbursement contract without an adequate accounting system.

While the specific criteria to deem an accounting system adequate have not been spelled out in the FAR, a good benchmark is the Pre-Award Survey or Standard Form 1408 (SF 1408). The SF 1408 lists several requirements to determine if a “contractor’s accounting system is adequate for determining costs applicable to the contract or order” when a Pre-Award Survey is required per FAR 9.106. The SF 1408 asks if the contractor can segregate direct and indirect costs, has the ability to track costs by contract, tracks employees’ time by intermediate or final cost objective and uses a labor distribution system to charge labor costs to the appropriate job. It also asks if the contractor has a logical and consistent method for allocating indirect costs and tracks the actual costs to contract funding requirements.

If a company is bidding on a contract that will be subject to the requirements of the Cost Accounting Standards (CAS), the contract will likely be subject to the eighteen criteria contained in the Defense Federal Acquisition Regulation Supplement (DFARS) 252.242–7006, Accounting System Administration. The expectation is that the task of reviewing a potential contractor’s accounting system is the responsibility of the Defense Contract Audit Agency (DCAA) or the auditors of the civilian agency awarding the prime contract. Due to audit resource constraints, DCAA and other audit branches have many priorities assigned to other audit assignments, and a subcontractor’s Pre-Award Survey is not likely to be performed by DCAA even when required by the prime contract.

Any tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties imposed under the Internal Revenue Code or applicable state or local tax law or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein.
to be considered. For a subcontractor working under a prime, the government’s auditors are not likely to get the call.

So, what is a company supposed to do if the auditors do not come out? This is a common challenge for businesses that have not had a Pre-Award Survey performed on their accounting system. If a company does not have written approval, but its competitors do, what is stopping the competitors from being more attractive to customers?

Fortunately, even though there is no formal guidance, many contracting offices and prime contractors recognize the challenge and will generally offer the following options if no documentation is available:

- They may request the subcontractor to “self-certify” that their accounting system meets the requirements outlined in the SF 1408. Self-certification is fairly straightforward; however, subcontractors should understand the requirement and be confident the system is compliant before making that representation under a Federal contract.

- They may have an audit type function that they could offer to perform the review of their subcontractor’s accounting system. Most subcontractors we work with are not in favor of allowing a prime contractor to review their system simply because the prime may be a competitor, and providing access to proprietary cost information could be detrimental to winning future work.

- Some also offer an option to have the subcontractor provide a letter from a CPA firm “certifying” that the company’s accounting and billing system can track and account for costs and billings in accordance with FAR Parts 30 and 31. An accounting system attestation report by a CPA firm is not a guarantee that the approval will be acceptable to all government agencies or all primes. However, it is a stronger statement than the other options listed above.

At the end of the day, every procurement opportunity should be evaluated with the requirements contained in the solicitation document. If you want to bid on a solicitation, and it clearly states that you need to have documentation of an approval from a government agency – and you don’t – the time to act is before you deliver the bid. If you wait until after you submit your proposal, and then find out that you were not considered for award due to the lack of documentation – you are likely too late.

It is appropriate to request a clarification or submit a question to the contracting official and challenge their criteria before you submit your proposal. If you are working with a prime – consider the points above and see what latitude the subcontract administrator may have. Letting the sleeping dog lie is not a plan for success.

Dixon Hughes Goodman has extensive experience with cost accounting system compliance and, if needed, performing attest services to provide documentation for your proposals. In addition, we have assisted many companies with understanding the requirements in both the SF 1408 and the DFARS to
guide a contractor through the self-certification process or to assist in recommending and implementing controls and procedures to bolster your accounting system.

About the Authors

Brian Fee, Manager, Rockville, Maryland

Brian has more than 12 years of experience in government contracting. In this time he has assisted companies with issues associated with cost estimating, procurement, cost accounting and the approval of business systems. He has experience in the application and interpretation of rule, regulations and the standards applicable to government contractors.

Contact Brian: brian.fee@dhgllp.com | 240.403.3747

Bill Walter, Partner, Tysons, Virginia

Bill has more than 25 years of experience helping companies identify and resolve issues associated with cost accounting and financial management systems. He has an extensive background in the application and interpretation of rules, regulations, and standards applicable to government contractors.

Contact Bill: bill.walter@dhgllp.com | 703.970.0509

Mark Burroughs, Partner, Tysons, Virginia

Mark applies his 20 plus years of experience in auditing and consulting to assist government contractors ensure compliance with the complex rules associated with contracting with the Federal Government. Mark’s focus area is helping contractors understand real world, practical solutions when dealing with matters associated with contractor business systems, DCAA audits, the Federal Acquisition Regulation (FAR) and Cost Accounting Standards (CAS).

Contact Mark: mark.burroughs@dhgllp.com | 703.970.0519

About Dixon Hughes Goodman LLP: With more than 1,800 people in 11 states, Dixon Hughes Goodman is the largest certified public accounting firm based in the Southern U.S. and the 15th largest in the nation. Visit www.dhgllp.com for more information.

2014 Dixon Hughes Goodman LLP | dhgllp.com

Any tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties imposed under the Internal Revenue Code or applicable state or local tax law or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein.