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newsletter

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Employee Travel Costs: How to Interpret the Cost Principle

In determining allowability, or unallowability, of employee travel costs via FAR 31.205-46 verbiage, one must be diligent in understanding the costs to which this principle applies, and recognizing the extent to which other government travel regulations are integrated within this principle. Government contractors must also understand that unless a specific travel cost element is actually named and stated to be unallowable (expressly unallowable), then allowability determination of specific travel cost elements not otherwise explicitly rendered as unallowable are governed by the “reasonableness” and “allocability” FAR provisions.

Frequently, government auditors and contractors read too much judgment into this cost principle in discerning which travel costs are, and are not, allowable,

and thus perpetuating long-term false illusions that certain travel costs are always unallowable, when in fact the cost principle is actually silent on certain costs.

One of the most common misperceptions regarding the travel cost principle application is that ALL provisions of the JTR, FTR, and/or State Dept travel regulations are incorporated within this cost principle. Wrong!!! There are only three narrowly-defined regulatory provisions of these government travel regulations (applicable to government civilian and military personnel) that are incorporated into FAR 31.205-46 and thus applicable to government contractors. These are:

- Definition of per diem--lodging, meals and incidentals (M&I)—note that for measuring allowability to ceiling per diem values, lodging taxes are excluded from this amount, and incidentals no longer include laundry for travel covered under the FTR. Lodging taxes and laundry expense are defined as “miscellaneous

expenses”, and therefore not components of “per diem”

- Maximum per diem rates—limited to ceilings specified in the JTR, FTR or State Dept travel regulations (also applicable to federal civilian and military personnel)
- Special or unusual situations for exceeding maximum per diem amounts

Contractor employees are not held to other provisions of the Federal government travel regulations, such as long-term temporary duty per diem limitations, specific calculations of partial day travel per diem allowability, restrictions on use of autos, or any of the administrative processes placed upon Federal personnel. Contractors, for example, often interpret the provision in FAR 31.205-46(a)(6)(ii), which states that maximum per diem daily rates “would not constitute a reasonable daily charge...” for partial travel days, as a mandate to use 75% of the maximum rate to determine the allowable partial day per diem under this cost principle—the cost principle prescribes no such factor or

calculation methodology—that 75% rule applies to federal employees (in some cases) but not to government contractors. Thus, the cost principle leaves it up to the contractor to determine a reasonable partial day value.

Determining allowable ceiling per diem amounts are to be calculated on a daily basis, and the measurement to this allowable daily ceiling, under the cost principle, is viewed at the total lodging and M&I value—that is, the cost principle does not hold a contractor to the individual ceilings for each component of per diem (lodging and M&I). Additionally, the travel cost principle does not consistently place cost restrictions on lodging taxes because the lodging taxes are not incorporated into the FTR “lodging” per diem definition, but are incorporated into the JTR and State Department ceiling as part of the lodging per diem value. Because of this inconsistency and confusion, the lodging taxes are sometimes misapplied by both contractors and by government auditors.

With the exception of airline fares and use of company-owned or leased aircraft, specific parameters for allowable transportation costs are not defined. Airline fares are limited to the “lowest price airfare available to the contractor during normal business hours...”, and there are specific restrictions for company owned or chartered aircraft costs. However, the cost principle does not (1) stipulate that auto rental costs are limited only to a the cost for a compact auto, bicycle, or Moped, (2) define when airline tickets should be purchased to achieve best value (this is a business judgment), (3) stipulate that when on extended TDY more than 60 days, a contractor must negotiate less expensive daily lodging values, (4) confine an employee to a certain auto rental agency, (5) specifically state that mileage costs for employee owned vehicles be calculated at the IRS approved mileage rate, or (6) hold a

contractor to other criteria that are sometimes foolishly considered an implicit requirement of this cost principle.

A complete understanding of any cost principle requires a reading of its contents literally and highlighting those cost items that are specifically addressed in the principle’s verbiage. All other travel costs (that is, those not specifically discussed with named cost restrictions of conditions for allowability) should not be automatically considered unallowable; conversely, those costs should be considered allowable but nevertheless subject to reasonableness and allocability regulatory criteria.

FY 2010 Defense Authorization Act: OMB A-76 Competition Limits

The fiscal year 2010 DOD Authorization Act, recently signed by President Obama, places new restraints and parameters on DOD private-public competitions administered under the OMB A-76 program, which essentially allows the outsourcing of services to private industry using a competitive award process that also considers DOD federal agencies’ ability and cost in performing those services.

The restrictions are designed to determine if sufficient studies are being performed to compare cost for outsourcing limited scope services to private industry vs. retaining those services “in-house” before converting those services to the private sector. In other words, is the DOD using proper due diligence in gauging the efficiency in continued outsource of smaller contracted work.

The restrictions fall in line with the Administration’s on-going initiative to limit the outsourcing of work inherently considered federal tasks, especially when

such work may be more efficiently performed by federal agencies rather than government contractors.

Included within the final DOD act bill are a number of new initiatives with a focus on exercising more diligence in comparing cost for in-sourcing vs. outsourcing, and consequently reigning in excessive costs that may otherwise be paid by the taxpayer for services provided by the private sector.

A few notable initiatives include:

- Limits the duration of public-private competitions for 24 months, but then allows an extension of up to 33 months if complexity of competition makes the completion of the competition process impossible;
- Extends GAO’s bid protest authority to bids where conversions of functions currently held by the DOD are initially awarded to private industry, and allows cancellation of the private-public solicitation as a quick remedy to the dispute;
- Extends the mission of the Congressional Commission on Wartime Contracting whose responsibilities, in part, are to identify remedies for eliminating wasteful contracting spending such as was observed in Iraq and Afghanistan;
- Expands DOD’s authority to by-pass OMB A-76 competition methods and fill federal acquisition positions for which there is a shortage of critical personnel;
- Requires GAO to evaluate frequency of using factors other than cost or price were deemed more important in the selection of contract recipients;
- Allows federal agencies to re-employ retired employees on a limited basis, and;
- Requires the Secretary of DOD to identify certain congressional earmarks, outline award factors

employed in selecting recipient, identify contract types for each earmark, and determine if the merits of “competitive or merit-based” procedures were used to award the earmarks.

FAR Change to Allowable Airline Travel Costs

A final FAR Rule (FAC 2005-38) has implemented changes to the FAR cost principle covering employee travel costs, specifically allowable airfares. Old verbiage with FAR 31.205-46(b) pronounced air fares in excess of “lowest customary standard, coach or equivalent airfare” as unallowable. The changed verbiage within FAR 31.205-46(b) removes this verbiage and replaces it with “lowest price airfare available to the contractor during normal business hours...” as the benchmark for allowability.

Primary reason for removing the “coach” and “standard” verbiage was because such terms do not describe actual classes of airline service available. Moreover, in some cases, contractors were able to negotiate airfares lower than “coach fares” (available at the time of travel), but claiming the higher coach fares available to the general public. Thus, the new verbiage was an attempt to make it clear that contractors will not be allowed airline ticket costs exceeding the actual fares paid for airline tickets, in cases where tickets at lower than customary coach fares are “available” to the contractor (via negotiated arrangements) for travel to those destinations requiring business travel.

Unfortunately, the revised wording will not resolve some longstanding issues with government auditors in the context of the actual airfare versus the lowest available, and may actually broaden the government’s challenges of airfare allowability. For example, the “lowest available” for any given trip is rarely going

to be the actual airfare unless a contractor can always purchase an airline ticket at the lowest price available for a particular flight. This is a virtual impossibility given the volatility of airline ticket pricing. Moreover, the lowest available price may be an advance purchase or it may be a last minute purchase; both “available” but at differing points in time prior to the trip. Unless a contractor can magically purchase an airline ticket at the lowest offered (available) price, it will potentially have after the fact government audit issues.

Notwithstanding the problems with obtaining the lowest available airfare for any given trip, the revised regulation will make it implausible for a contractor to allow certain employees to book business or first class airfare and to claim the equivalent of the most expensive “coach class” ticket. In many cases, the most expensive “coach class” was actually more expensive than restricted or advance purchase business class tickets; hence, this approach would theoretically yield no unallowable airfare.

The revised FAR wording may have resolved one issue concerning allowable airfare, but it remains to be seen if government auditors will accept a reasonable, but unstated interpretation that the lowest available should be at the time the contractor purchased the airline ticket as opposed to the absolute lowest price for that particular flight.

Government Fraud Recoveries in 2009

The Department of Justice announced in November 2009 that its fraud recoveries (under the FCA or False Claims Act) were \$2.4B for the government fiscal year 2009. Within those recoveries were \$422 million for Department of Defense contracts and \$1.6B for healthcare fraud; the latter continues to lead the pack as has been the case for several years

running (Department of Health and Human Services has recovered approximately two-thirds of all fraud recoveries since the False Claims Act of 1986).

With respect to recoveries from defense contracts, false claims recoveries for 2009 were approximately three and one-half times those for 2008 including \$59 million related to Iraq/Afghanistan. In some respects, the recoveries associated with wartime contracting are notable; however, the defense fraud recoveries suggest that the more significant recoveries are not related to wartime contracting.

The Department of Justice also disclosed that approximately 85 percent of the fraud recoveries were associated with qui tam actions reporting that of the approximate \$2B associated with qui tam lawsuits, the qui tam relators were awarded approximately \$260 million. Perhaps unintended, but the qui tam “industry” is apparently thriving as further reinforced by the Department of Justice references to 985 pending health care fraud cases wherein the government has made a decision to intervene on 315 while considering the remaining 670.

The Department of Justice fraud recoveries and the references to qui tam lawsuits also serves as a reminder that during government fiscal year 2009, the FAR incorporated certain mandatory disclosure requirements (FAR 52.203-13) which require that certain actions, including fraud, be reported to an agency inspector general’s office when a contractor has credible evidence of certain reportable violations (these rules have been discussed in a number of our 2009 newsletters). In addition to mandatory disclosure, FAR 52.203-14 requires mandatory posting of agency inspector General hotline posters or contractor hotline posters (under certain conditions).

It should be self-apparent that it is a serious business with serious risks in being a government contractor. A government contractor is ultimately responsible for its actions as well as those of its management and employees, with any one of them (employees) having the potential to be the cause of an issue as well as the source of a qui tam lawsuit. Hence, the need for internal controls which provide reasonable assurance of detecting improprieties with those internal controls including an internal hotline or other reporting mechanism which allows and/or otherwise encourages any employee to report improprieties. Internal controls do come at a cost, but nowhere near the cost of an action involving a government investigation of an alleged fraud on a government contract.

Government Agencies in the News – Unfortunately

The Bureau of Engraving and Printing recently suspended its ongoing gift-card program which had offered a \$75 gift card to employees who “voluntarily” returned their government owned desktop printer which would then be replaced by access to a network printer. The cost saving measure was apparently questioned by a Congressman from California (Representative Darrell Issa) who questioned the need to pay government employees for returning government-owned printers. The Government not only suspended the gift card program, but also suspended its activities to retrieve the desktop printers. Of passing note, the desktop printers are primarily held by senior officials; hence, the gift-cards would have primarily benefitted those employees lucky enough to be in physical possession of the government-owned desktop printers.

Although the gift-card program would have cost a mere \$40K, we have to agree with Representative Issa who stated that the program defied common sense. Why

would any government agency offer gift-cards to employees to incentivize the employee to return government-owned printers? The program not only defied common sense, it bordered on the absurd.

Not to be out-done by another government agency, several government agencies were highlighted in an OMB (Office of Management and Budget) report on improper payments. In total the government’s FY2009 improper payments were a “mere” \$98B with a notable 33 percent increase over FY2008. The overall rate for improper payments was 5 percent with three programs at or above 20 percent. If government contractors came anywhere near the 5 percent error rate (much less the 20 percent error rate), those contractors would soon be out of business at least with respect to government contracts.

Finally, an IG (Inspector General) reported that \$12.3 million in Smithsonian property is missing including 89 laptop computers. The pilfered items, mostly office equipment, have led to only one action wherein an employee was held accountable for \$40 worth of missing property. The Smithsonian promised to enforce policies in the future.

All of this further reinforces the implied government motto, “Do as I say, not as I do”.

DPAP Intervenes on DCAA-DCMA

In a memorandum dated December 4, 2009, DPAP (Defense Procurement and Acquisition Policy) issued a policy apparently designed to reduce some of the “dysfunctionality” existing between DCAA and DCMA (reference to statements made by the Commission on Wartime Contracting). The policy leads in with a statement reinforcing the Department’s full support for contracting

officers making informed decisions within the scope of their authority utilizing the advice of specialists in audit, law, engineering, etc., while obtaining the best business deal for the taxpayers. Similarly, the document ends with a statement that it is the contracting officer’s ultimate responsibility to determine fair and reasonable contract values.

In spite of the reaffirmation of the contracting officer’s authority, the DPAP memorandum seems to dilute that long standing authority. In particular, that “significant disagreements” between a contracting officer and DCAA now involve a structured process which could rapidly escalate to high levels within DCAA and DCMA and ultimately involve DPAP. A significant disagreement is when the contracting officer’s pre-negotiation objective plans to sustain less than 75 percent of the DCAA questioned costs on proposals valued at \$10 million or more. When significant disagreements occur the contracting officer must discuss with DCAA, document those discussions and obtain approval for the negotiation objective.

Beyond the initial discussions, should the auditor disagree with the contracting officer, DCAA management may request a higher level DoD component review and all DoD components must implement procedures to implement the DPAP policy. Although the DPAP memorandum suggests that the auditor maybe persuaded to agree with the contracting officer, practical experience suggests otherwise. Auditors are partial to their audit exceptions and we believe that most will hold firm to their audit exceptions (pride of ownership or authorship so to speak). Moreover, auditor independence, reinforced by multiple GAO reports on DCAA audits, suggests that auditors will not succumb to contracting officer arguments lest the auditor be at risk for having waived on their independence.

Although the DPAP memorandum would seem to impede a contracting officer from a significant disagreement with DCAA, it remains to be seen if and how it serves that purpose. In particular, the policy applies to a pre-negotiation position as opposed to actual negotiations. Hence, nothing would seem to procedurally address a contracting officer failure to sustain DCAA during the heat of battle (contract negotiations).

Additionally, the new policy fails to address other contentious issues including the contracting officer's decision to negotiate a contract in spite of a DCAA adverse opinion recommending that a contract not be negotiated based upon a contractor's "inadequate" proposal. Of particular note, a common reason for a DCAA adverse opinion is the magnitude of unsupported costs; however, the DPAP memorandum specifically excludes unsupported costs from the definition of a significant disagreement. In other words, the DPAP memorandum indicates or at least implicates that unsupported costs need not be considered by a contracting officer.

Finally, the DPAP memorandum only addresses audit resolution on proposals leaving untouched those audit opinions addressing business systems, incurred costs, etc. Given the complexities of the many current issues which exist in terms of DCAA versus the Contracting Officer, it is entirely possible that the DPAP memorandum is simply a petulant response to growing congressional pressures. But in so doing, at the very least DPAP should stay within the parameters of the Federal Acquisition Regulations which is for contracting officers to determine and negotiate a fair and reasonable price. In absolutely no context is a fair and reasonable price the same as "the best business deal for the taxpayers" (reference to the first paragraph in the DPAP memorandum).

Training Opportunities

2010

January 12, 2010 – Preparing for Challenges of CY 2010 Government Procurement & Audit Oversight High Risk Issues and Trends Lunch Event

Time: 11 AM – 1:30 PM

Cost: \$40 per person

Location: Beason & Nalley
101 Monroe Street
Huntsville, AL

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. Sandra Baker at sbaker@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.



We deliver objectives.

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