



Regulatory Update and Report on Recent Developments

September 14th , 2010

Agenda

- **Regulatory Update**

- Final Rule – Definition of Cost or Pricing Data
- Final Rule - Changes to Acquisition Thresholds
- Proposed Rule – Unclassified Data Security
- Proposed Rule – Disclosure Requirements Regarding Executive Compensation
- Other Regulatory Updates
- CAS Updates
- DCAA Audit Guidance Memoranda Issued

- **Recent Developments**

- Efficiency Initiative Introduced by the Secretary of Defense
- Implications of Transition from DoD to Department of State on Iraq Contracts
- DCAA Initiatives
 - Subcontract Management
 - Coordination with DCMA
- Business System Audits (ICAPS)
 - Proposed Rule
 - Industry Feedback

Regulatory Update

Final Rule – Definition of Certified Cost or Pricing Data

Final Rule published in the Federal Register on August 30, 2010 and is effective on October 1, 2010.

- Clarifies definition of certified cost or pricing data and makes the definition consistent with the Truth in Negotiations Act (TINA) definition.
- Eliminates the term “information other than cost or pricing data” and replaces it with “data other than certified cost or pricing data”
- Certified cost or pricing data is required to be submitted in accordance with FAR Part 15.4 and is intended to assist the Contracting Officer in establishing a fair and reasonable price.
- Data other than certified cost or pricing data is also intended to assist the Contracting Officer in establishing a fair and reasonable price. It may be a complete set of data or a partial set of data, but is not certified as being current, accurate and complete in accordance with TINA.

Regulatory Update

Final Rule – Definition of Certified Cost or Pricing Data (cont.)

Final Rule maintains the current order of preference for determining the types of cost or pricing data required to establish fair and reasonable prices.

Certified cost or pricing data must be submitted if required by FAR Part 15 and TINA.

Data other than certified cost or pricing data includes:

- Data obtained from the contractor
- Data obtained from sources other than the contractor
- Data available to the government

Final Rule does not encourage or require Contracting Officers to obtain more data than is required to establish a fair and reasonable price.

Regulatory Update

Proposed Rule – Elimination of Provisional Award Fee Payments



DOD Proposed Rule Would Eliminate Provisional Award Fee And Defer Substantial Award Fee Payments

- The Department of Defense recently proposed a rule that would revise guidance for award-fee evaluations to require:
 - The incorporation of award-fee plans into all DOD award-fee contracts,
 - The use of objective criteria to the maximum extent possible to measure contract performance including, where appropriate, use of formula-based incentives rather than or in addition to an award fee,
 - The elimination of provisional award-fee payments, *i.e.*, payments made prior to evaluation of contractor performance, which have been allowed since 2003 in accordance with DFARS 216.405-2, and
 - Reservation of at least 40% of the available award fee pool for payment after the final evaluation period.
 -

75 Fed. Reg. 22728-29 (April 30, 2010).

Regulatory Update

Final Rule – Acquisition Thresholds

Final Rule is effective October 1, 2010. New Thresholds include:

- Simplified Acquisition Threshold (FAR Part 13) moved from \$100K to \$150K.
- Commercial Items test program moved from \$5.5M to \$6.5M (FAR Part 13.5)
- Cost or pricing data contract threshold moved from \$650K to \$700K (FAR Part 15.4)
- Prime contractor subcontracting plans moved from \$550K to 650K (FAR Part 19.7)
- Construction prime contractor subcontracting plans moved from \$1M to \$1.5M (FAR Part 19.7)

Regulatory Update

Proposed Rule – Unclassified Data Security

On March 3, 2010, DoD issued an Advanced Notice of Proposed Rulemaking (ANPR) adding new requirements for the proper safekeeping and handling of unclassified DoD information.

- This new rule will apply to all DoD prime contracts and subcontracts regardless of the contract dollar value.
- New safeguards will probably increase contract costs.

DoD continues to try to achieve better uniformity and consistency in its policies and procedures surrounding the protection of its sensitive information.

Regulatory Update

Proposed Rule - Executive Compensation

An interim rule amending the Federal Acquisition Regulation (*FAR Subpart 4.14 revision*) to implement section 2 of the Federal Funding Accountability and Transparency Act of 2006, as amended by section 6202 of the Government Funding Transparency Act of 2008, which requires the Office of Management and Budget (OMB) to establish a free, public, website containing full disclosure of all Federal contract award information.

- This rule will require contractors to report executive compensation and first-tier subcontractor awards on contracts expected to be \$25,000 or more, except classified contracts, and contracts with individuals.
 - Until September 30, 2010, any newly awarded subcontract must be reported if the prime contract award amount was \$20,000,000 or more;
 - From October 1, 2010, until February 28, 2011, any newly awarded subcontract must be reported if the prime contract award amount was \$550,000 or more; and
 - Starting March 1, 2011, any newly awarded subcontract must be reported if the prime contract award amount was \$25,000 or more.
- Contracting officers shall modify existing indefinite-delivery indefinite-quantity (IDIQ) contracts on a bilateral basis in accordance with FAR 1.108(d)(3) to include the clause for future orders.
- The clause is required in commercial item contracts, including commercially available off-the-shelf (COTS) item contracts, as well as actions under the simplified acquisition threshold, meeting the \$25,000 threshold.

Regulatory Update

OFPP Sets Executive Compensation Cap for FY 2010 and Beyond

On April 15, 2010 the Office of Federal Procurement Policy set the new executive compensation cap for FY 2010 and beyond at **\$693,951**.

[Federal Register Notice Volume 75, Number 72] FY2009 was \$684,181

The cap applies to all compensation costs incurred on or after January 1, 2010 to Defense and Civilian agency contractors subject to the FAR Part 31 Cost Principles. Specifically see FAR Part 31.205-6.

- The cap applies to senior executives as defined in FAR Subparts 31.205-6(p)(2)(i) and (ii).
- Applies to top 5 executives at home office and each segment
- Applies to contractor fiscal year (CFY) 2010

Regulatory Update

Proposed DDTC Rule & 2010 Supplemental Appropriations Act

Export Control Advisory - DDTC Proposes New Regulations Regarding Dual Nationals and Third Country Nationals

- August 12, 2010 On August 11, 2010, the US Department of State, Directorate of Defense Trade Controls ("DDTC") published a proposed rule, 75 Fed. Reg. 48,625-48,627 (Aug. 11, 2010), which would amend the International Traffic in Arms Regulations ("ITAR"), 22 C.F.R. Parts 120-130, to exempt certain export control approval requirements applicable to dual nationals and third country nationals employed by foreign end-users and consignees who are otherwise authorized by DDTC to receive defense articles and services. This action is not an interim final or final rule with the immediate force and effect of law. DDTC will be accepting public comments on the proposed exemption for 30 days until September 10, 2010.

On July 29, 2010, President Obama signed the supplemental appropriations bill which contained a provision amending the Clean Contracting Act of 2008

- This legislation gave rise to the Federal Awardee Performance and Integrity Information System ("FAPIIS") for DOD, GSA and NASA
 - As a result of the new language ("the Administrator shall post all such information, excluding past performance reviews, on a publicly available Internet website"), information in FAPIIS must be made available to the public, except for past performance reviews.
 - Primarily posting criminal, civil, administrative legal proceeding info

Regulatory Update

Revision of Department of Homeland Security Acquisition Regulation

Department of Homeland Security Regulation Update

- The Department of Homeland Security (DHS) is proposing to amend its Homeland Security Acquisition Regulation (HSAR) to implement a statutory requirement limiting the use of subcontractors on cost-reimbursement type contracts entered into by the Department to facilitate the response to or recovery from a natural disaster or act of terrorism or other man-made disaster.

DHS Clamps Down on Lead System Integrators

- On July 15, 2010, the Department of Homeland Security issued an interim rule which mirrors a DoD rule, restricting contractors from acting as lead system integrators in the acquisition of DHS major systems if they have direct financial interests in the development or construction of individual systems or elements of any system that they integrate.
 - Effective immediately, the rule contains several exceptions and also provides detailed definitions of lead system integrators and direct financial interests.

Regulatory Update

DFARS Revisions

DoD is issuing a final rule amending the DFARS to revise and combine contract clauses addressing assumption of risk of loss under contracts that furnish aircraft to the Government:

- Adding a requirement for inclusion of the clause in subcontracts at all tiers;
- Adding a statement that the Government property clause is not applicable if the Government withdraws its self-insurance coverage;
- Adding a statement that commercial insurance costs or self-insurance charges that duplicate the Government's self-insurance are unallowable

CAS Updates

- Effective June 16, 2010, the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council introduced an interim rule that attempts to align FAR with the revised Cost Accounting Standards Board Clause, Disclosure and Consistency of Cost Accounting Practices for Contracts Awarded to Foreign Concerns [Revised March 26, 2008]
- Disclosure and Consistency of Cost Accounting Practices-Foreign Concerns, in CAS covered contracts and subcontracts awarded to foreign concerns.
 - FAR 30.201-4(c)(1) and (2) the prescription for use of FAR clause 52.230-4 is revised
 - FAR 30.201-4(d) is revised to include use of FAR clause 52.230-6, Administration of Cost Accounting Standards
 - FAR clause 52.230-4 is replaced in its entirety and re-titled “Disclosure and Consistency of Cost Accounting Practices—Foreign Concerns”
 - FAR clause 52.230-6, Administration of Cost Accounting Standards, is revised to include reference to FAR clause 52.230-4

CAS Updates

Aligning FAR with CAS 412 and 415 – ESOP Clarification

- Effective June 16, 2010, the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council have issued an interim rule with request for comments aligning the FAR with the revised CAS 412, “Cost Accounting Standard for composition and measurement of pension cost,” and CAS 415 “Accounting for the cost of deferred compensation”, which were amended In May of 2008.
- Primary change is “that the accounting of Employee Stock Ownership Plan (ESOP) costs, regardless of type, would be covered by the provisions of CAS 415 only and not by CAS 412.”
- **Harmonization of Cost Accounting Standards 412 and 413 with the Pension Protection Act of 2006**
 - 75 FR 25982, Notice of Proposed Rulemaking (May 10, 2010)
- Continue to assess need for inclusion of **Post Retirement Benefit** costs in CAS 413 – not currently addressed. Company recognized benefit as earned, not when paid.

DCAA Audit Guidance and Audit Management Guidance Update

Memorandums for Regional Directors (MRDs)

Date	MRD Number	Subject	CAM Ref	5-Digit Activity Code
7/29/2010	10-PPS-019(R)	Delegation of Signature Authority for Audit Reports	NA	NA
6/4/2010	10-PSP-018(R)	Audit Alert on Reporting on Forward Pricing Rates in Pricing Proposals	NA	NA
6/1/2010	10-PPS-017(R)	Delegation of Signature Authority for Provisional Approval of Public Vouchers	NA	NA
5/27/2010	10-PAS-015(R)	Guidance on Resolving Contract Audit Recommendations	1-403.3 & 1-403.4	NA
5/25/2010	10-PSP-016(R)	Transmittal of Department of Air Force Memorandum on Timely Undefined Contract Action (UCA) Definitization/Negotiated Awards and Contractor Responsiveness	NA	NA
5/13/2010	10-PAS-014(R)	Audit Alert on Supplemental Revisions to Working Papers after Report Issuance	NA	NA
4/23/2010	10-PPD-012(R)	Audit Guidance on the Executive Compensation Cap for Contractor Fiscal Years 2010 and Beyond	NA	NA

DCAA Update

- Actions remain underway in response to GAO report findings:
 - Business System Audits
 - Revised approach to Quality Assurance/Report Reviews
 - New audit approaches in areas like assessment of adequacy of accounting systems, billing systems
- New/Continued Areas of Audit Focus
 - Contractor Code of Conduct/ Ethics Program Assessments
 - Focus on overpayments
 - Renewed focus and more rigorous audits of Forward Pricing Rate Proposals and use of appropriate opinions regarding disclaimers or limitations if audit not completed
- New Escalation Path – DCMA Contract Management Board of Review

Recent Developments

Efficiency Initiative Introduced by Secretary of Defense

(Gates Proposes 10% Cut in Government Contractor Support Gates Admits In-sourcing has Failed)

August 9, 2009 - While Gates looks to reduce the number of white collar government contractor support, even while recently admitting an in-sourcing effort has failed to show cost savings.

- Proposes sweeping plan to save money in a variety of other ways.
- Plans to cut contractor support base rather than people
- Plans to add to freeze amount of full time positions in the Office of the Secretary of Defense and other defense agencies after 2010.

The subsequent slides provide further detail on Gates plan to eliminate the Department of Defense's reliance on contractor support to perform inherently governmental functions.

Recent Developments

Efficiency Initiative Introduced by the Secretary of Defense (cont.)

Aug. 9, 2010 – Defense Secretary Robert M. Gates set out his plans to reform the way the Pentagon does business by eliminating duplicative, unnecessary costs.

- Gates said the steps he is taking will help the U.S. military fight the wars it faces now, and help ready the force for the wars it may face in the future.
- Plans to review 26 government IT projects worth a total of \$30 billion.
- Intended to determine if IT spending has lax oversight which has led to cost overruns, delays, and the implementation of obsolete systems

The Secretary of Defense has targeted multiple DoD offices and organizations. Some of the proposed moves include:

- Reduce funding for support contractor personnel by 10 percent a year for the next three years.
- Close the offices of the assistant secretary of defense for network intelligence and integration and the Joint Staff's section for command, control, communications and computer systems.
- Eliminate the Business Transformation Agency.
- Freeze at fiscal 2010 levels the number of Office of the Secretary of Defense, defense agency and combatant command positions for the next three years; Gates said this is a first step in examining leadership organizations.

Recent Developments

Efficiency Initiative Introduced by the Secretary of Defense (cont.)

Defense Secretary's proposed moves (continued):

- Freeze at fiscal 2010 levels the number of senior DOD officials; Gates will appoint a senior task force to assess the number of general and flag officers, senior executive service employees and political appointees.
- Increase use of common IT functions to mitigate disparate, decentralized IT systems throughout DOD that result in cumulative costs and cyber vulnerabilities.
- Freeze the overall number of required oversight reports and cut by a quarter the money allocated for such reports.
- Eliminate DOD boards and commissions that have outlived their usefulness and cut funding to such boards by 25 percent.
- Reduce by 10 percent funding for intelligence advisory and assistance contracts, freeze the number of senior executive service positions in the DOD intelligence apparatus and end needless intelligence duplication.

One of the more significant suggestions is the elimination of Joint Forces Command which employs about 6,000 people and is based in Virginia

- Secretary of Defense expects to dismantle the command over the coming year, although not all functions will be eliminated.
- Gates has demanded action plans for most items within three to four months

Recent Developments

Implications of Transition from Department of Defense to Department of State in Iraq on Government Contractors

US military forces are to complete their exit from Iraq by 12/31/2011, and by 8/31/2010, the American troop strength in Iraq should be no more than 50,000.

- The resources of State's Diplomatic Security Service are 'inadequate to the extreme challenges in Iraq,' according to an April 7, 2010 letter to DoD's lead acquisition officer from Ambassador Patrick Kennedy, Under Secretary of State for Management
- The Kennedy letter also requested that DoD allow State to continue using the military's LOGCAP contract and Defense Logistics Agency support.
 - There is a critical need for logistical and life-support services provided under the Army's worldwide LOGCAP (Logistics Civil Augmentation Program) contract.
- As U.S. military forces leave Iraq, they will take vital services with them, ahead of the final exit target date of 12/31/2011.
- State will have no practical alternative to meet its continuing security and support needs in Iraq than by greatly increasing its contracting.
- State and DoD have established high-level interagency contacts.
- The Departments of Defense and State have listed more than 1,000 tasks and functions that must be addressed in the DoD-to-State transition in Iraq.

Recent Developments

Implications of Transition from Department of Defense to Department of State in Iraq on Government Contractors (cont.)

States “Lost Functionality” list contains 14 security related tasks now performed by DoD that State must provide as the military drawdown in Iraq, including:

- Recovering killed and wounded personnel
- Recovering damaged vehicles
- Recovering downed aircraft
- Clearing travel routes
- Operations-center monitoring of private security contractors (PSCs)
- PSC inspection and accountability services
- Convoy security
- Explosive-ordnance disposal
- Counter-rocket, artillery, and mortar notification
- Counter-battery neutralization response
- Communications support
- Tactical-operations center dispatch of armed response teams
- Policing Baghdad’s International Zone
- Maintaining electronic counter-measures, threat intelligence, and technology capabilities

Recent Developments

Implications of Transition from Department of Defense to Department of State in Iraq on Government Contractors (cont.)

The Department of State currently has roughly 2,700 private security contractors

- A State Department official testified at a June 2010 Commission hearing that the Department will need “between 6,000 and 7,000 security contractors” for the future – more than doubling its current PSC numbers.

Recent Developments

DCAA Initiatives

Subcontract Administration

- There has been increased oversight by government auditors relative to Subcontract Management by Prime and Upper-tier contractors
- Contractor Purchasing and Billing Systems have been deemed inadequate due to a lack of proper oversight of subcontractors
- The DCAA made several recommendations relating to Subcontract Management. Those recommendations include:
 - Contractor Purchasing Systems should ensure that the government is receiving fair and reasonable prices for subcontractor products and services
 - The proposed rule for business systems permit the DCMA to impose with holds on payments for inadequate purchasing systems
- Contingency Operations (i.e., Iraq and Afghanistan) have also been cited as problematic.
 - Auditors have questioned whether there is true competition in this area
 - Fitzgerald stated that it would be in the government's best interests if these subcontract prices were based on cost
- Improved coordination with DCMA

Recent Developments

DCAA Initiatives

Improved Relationship between DCAA and DCMA:

- At the highest levels of DCMA and DCAA, there is an attempt to improve relations between the two organizations
- There is the appearance that COs and ACOs are unwilling to go against DCAA findings
- There appears to be overlaps concerning EVM and Purchasing System Audits. This causes some disagreements.

Recent Developments

Business Systems Audits (ICAPS) – Proposed Rule



On January 15, 2010, the Department of Defense (“DoD”), Defense Acquisition Regulation (“DAR”) Council proposed a new rule (DFARS Case 2009-D038) to amend the definition and requirements around contractor business systems:

- The proposed rule is intended to improve the effectiveness of DoD oversight of contractor business systems
- Currently, there are ten contractor business systems identified in the DCAA Contract Audit Manual
- The proposed rule will reduce the number of business systems to six. The six systems proposed are:
 - Accounting
 - Estimating
 - Material Management and Accounting
 - Purchasing
 - Earned Value Management
 - Government Property
- The proposed requirements appear to more closely align with requirements surrounding pre-award surveys (SF1408)

Recent Developments

Industry Concerns in the Business System Audit Area

Based upon meetings with major government contractors, there are many areas of concern for contractors with regards to the proposed business systems changes.

Those concerns include:

- The FAR is ambiguous as to the requirements for adequate business systems and internal controls.
- The proposed DFARS business systems rule consolidating the current ten ICAP system audits to six systems is not specific relative to audit criteria or the key system attributes/capabilities that would result in an “adequacy” determination. As a result
 - Industry seeks a definition of the business system audit “standard” and uniformity in its application.
 - Relayed that current DCAA business system audit methodology is not uniform and consistent amongst its offices and/or in its application to different contractors.
 - Concerns were expressed regarding the lack of guidance relative to materiality and the proposed use of DCMA decrements.
 - In the past, the DCAA used to collaborate and issue guidance on consistent application of internal control audit procedures however, it appears that the agency no longer does this.

Recent Developments

Industry Concerns in the Business Systems Audit Area (cont.)

Other Areas of Concern:

- The “zero tolerance” tactics being employed by the DCAA relative to business system audits are not practical, they are frustrating the federal procurement process and they significantly impacting the cost of compliance, which results in higher contract prices to the government.
- DCAA appears to be standing up audit teams that focus entirely on system audits. While this may have some advantages, these specialized teams do not have a working knowledge of the contractor, its business or its business systems which could result in inefficiencies and misunderstandings.
- The DCMA is moving to Ft Lee, VA. It is expected that this will result in the retirement of several key senior personnel from the DCMA.
 - There are already concerns in industry that COs, ACOs, CACOs and DACOs are hesitant to make decisions that are contrary to DCAA recommendations / guidance and the retirement of senior personnel could exasperate the issue.
 - Note: The DCMA also has a new CO type (System Administrative Contracting Officer “SACO”).

Recent Developments

Industry Concerns in the Business Systems Audit Area (cont.)

There appear to be two different faces of the DCAA

- External / higher level face
 - We want to work with industry.
 - Policy speeches for industry associations support this position.
 - The government claims that the DCAA and the DCMA are working together
- Internal / local level face
 - We are not open to discussion with the contractor in many areas because we must remain independent.
 - It appears that the DCAA has released guidance (DCAM) which may not be entirely consistent with applicable procurement regulations.
 - Business systems are being deemed inadequate for a lack of perfection and sometimes minor reasons.
 - In addition, many submissions to the DCAA (i.e., ICSPs, cost proposals, CAS cost impacts, FPRPs, etc...) are deemed inadequate for seemingly minor reasons. Sometimes reasons that could be quickly resolved.
 - Difficulties are being experienced both in obtaining initial system audits and then in convincing the DCAA to return in a timely manner when systems are deemed inadequate. Even though the contractor may have corrected the deficiencies, the systems remain inadequate.
 - The high rate of turnover in the DCAA, the lack of experience and the lack of an adequate understanding of business issues frustrates the audit process.

Recent Developments

Industry Concerns in the Business Systems Audit Area (cont.)

Business System/ICAPS Roundtable

- Plans to meet with DCAA and DCMA to set forth industry's concerns and thoughts on best practices relevant to business systems and internal controls.
 - Concerns are expressed above.
 - Also concerned that Industry concerns and/or recommendations will be perceived by the government as complaining and that industry will not be able to influence needed changes.
 - Concerns also expressed that DCAA will probably not advance useful ideas or guidance in these important areas and that the DCAA would probably be unwilling to participate in meaningful dialogue given their decision to no longer participate in Integrated Product Teams with contractors.

Thank you.

Please visit our website for more examples of
our thought leadership.