

THE TOP 10 ISSUES OF THE TOP 3 BUSINESS SYSTEM AUDITS

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KEY DISCUSSION TOPICS

- Triggers and Audit Processes for the top 3 Business Systems
- Common Misunderstandings and Audit Failures Across Business Systems
- Interrelationship of the Business Systems
- Responsibilities of the Prime for Subcontractor's Business Systems
- The 4th pillar of your Business Systems: Cybersecurity





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TRIGGERS AND AUDIT
PROCESSES

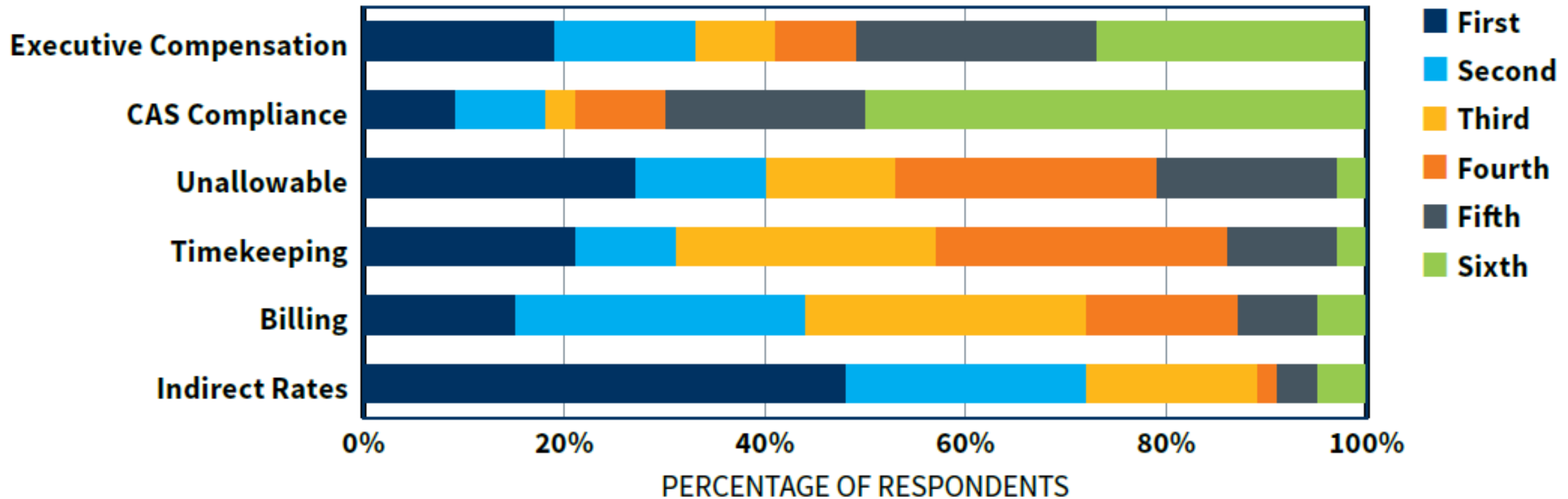
APPLICABILITY OF BUSINESS SYSTEMS

2018 GAUGE Report

SYSTEM	IMPLEMENTING DFARS CLAUSE	SUB	NOVICE PRIME	EXPERIENCED PRIME
Accounting	252.242-7006	◆	◆	◆
Earned Value Management (EVM)	252.234-7002			◆
Estimating	252.215-7002		◆	◆
Material Management and Accounting System (MMAS)	252.242-7004			◆
Property Management	252.245-7003		◆	◆
Purchasing	252.244-7001		◆	◆

BIGGEST AUDIT CHALLENGES

2018 GAUGE Report



ACCOUNTING SYSTEM AUDIT TRIGGERS

BUSINESS SYSTEM APPLICABILITY RULES				CRITERION APPLICABLE? INDICATE "YES" OR "NO"
SYSTEM		FAR, DFARS, PROVISIONS, and CLAUSES	CRITERIA	
ACCOUNTING (AS)	NON-DOD	FAR 16.301-3 Cost-Reimbursement Contracts - Limitations	1. Does your company have a Government cost-reimbursement contract? -AND-	
			2. Did the ACO determine a need for accounting system audit based on significant cost-reimbursement contracts, change in cost accounting practices, billing or invoicing issues, audit recommendation, or other rationale?	
	DOD	DFARS 242.7502(a) DFARS Clause 252.242-7006	1. Is your Company a DoD prime contractor or subcontractor?	
			2. Does any prime contract or subcontract contain a similar DFARS clause or language requiring an adequate accounting system?	
			3. Was the Company awarded or executed any of the following contract types:	
			(a) Cost-reimbursement contract (FAR 16)	
			(b) Incentive contract based on cost information	
			(c) T&M (Both Commercial FAR 12 and non-commercial FAR 15)	
			(d) Labor hour contracts	
(e) Contracts with progress payments made on the basis of costs incurred or on % completion				

ESTIMATING SYSTEM AUDIT TRIGGERS

BUSINESS SYSTEM APPLICABILITY RULES				CRITERION APPLICABLE? INDICATE "YES" OR "NO"
SYSTEM		FAR, DFARS, PROVISIONS, and CLAUSES	CRITERIA	
ESTIMATING (ES)	NON-DOD	FAR 15.407-5 Estimating Systems	1. Did the Company's CO under a prime contract determine a need for an estimating system review?	
	DOD	DFARS 215.407-5 Estimating Systems	1. Is your Company (DoD contractor or subcontractor) considered other than small as defined in the Small Business Administration? - AND -	
		DFARS Clause 252.215-7002 Estimating BusinessSystem	2. Did your Company receive in its preceding fiscal year a DoD <u>prime contract(s)</u> or <u>subcontract(s)</u> totaling \$50 million or more for which <u>certified cost or pricing data were required</u> ? or	
			3. Did your Company in its preceding fiscal year receive a DoD <u>prime contract(s)</u> or <u>subcontract(s)</u> totaling \$10 million or more (but less than \$50 million) for which <u>certified cost or pricing data were required</u> and the contracting officer, <u>with concurrence or at the request of the ACO</u> , determined it to be in the best interest of the Government?	
DETERMINE OVERALL SYSTEM APPLICABILITY				

PURCHASING SYSTEM AUDIT TRIGGERS

BUSINESS SYSTEM APPLICABILITY RULES				CRITERION APPLICABLE? INDICATE "YES" OR "NO"	
SYSTEM		FAR, DFARS, PROVISIONS, and CLAUSES	CRITERIA		
PURCHASING (CPSR)	DOD/NON-DOD	FAR Subpart 44.302 Requirements FAR Clause 52.244-2 Subcontracts	1. Did the Company's ACO determine the need for a CPSR based on, but not limited to, your past performance, and the volume, complexity, and dollar value of subcontracts? -AND-		
			2. In the next 12 months, your sales to the Government are expected to exceed \$25 million excluding:		
			(1) Competitively-awarded firm-fixed-price		
			(2) Competitively-awarded fixed-price with economic price adjustment		
			(3) Commercial items (pursuant to FAR Part 12)		
			As a preliminary CPSR eligibility evaluation:	TOTAL VALUE	
			3. Indicate estimated total value of sales to the Government as defined above and not including identified exclusions:		
			4. Indicate number of following contract/subcontract types received in past 12 months:	COUNT	TOTAL VALUE
			(a) Cost-reimbursement		
			(b) Time and Materials/Labor Hour		
	(c) Fixed-price competitively-awarded				
	(d) Fixed-price with economic price adjustment competitively awarded				
	(e) Contracts/subcontracts for sales of commercial items pursuant to FAR Part 12				
	(f) Fixed-price other than those in (c) and (d) above				
DOD ONLY	DFARS 242.7000 Contractor BusinessSystems DFARS Clause 252.242-7005 Purchasing System	1. Is your Company DoD prime contractor or subcontractor? - AND -			
		2. Does any prime contract or subcontract contain a similar DFARS clause or language requiring your company to maintain an adequate or approved purchasing system? - AND -			
		3. Will your Company be making purchases (services or supplies) under your prime contract or subcontract?			
DETERMINE OVERALL SYSTEM APPLICABILITY					

BUSINESS SYSTEM AUDIT PROCESSES

- Before the Onsite Visit:
 - Request and review org chart and policy/procedures documents
 - Request and review personnel training for business system
 - Request data on business system transactions
- At the Onsite Visit:
 - Conduct entrance briefing
 - Sample business systems transactions which are typically not identified before the onsite audit begins
 - Conduct daily discussions of findings with contractor personnel
 - Conduct exit briefing
- After the Onsite Visit:
 - Create draft report with findings and allow contractor to develop corrective actions
 - Create report for ACO in final format



COMMON MISUNDERSTANDINGS
ACROSS BUSINESS SYSTEMS

COMMON MISUNDERSTANDINGS ACROSS BUSINESS SYSTEMS

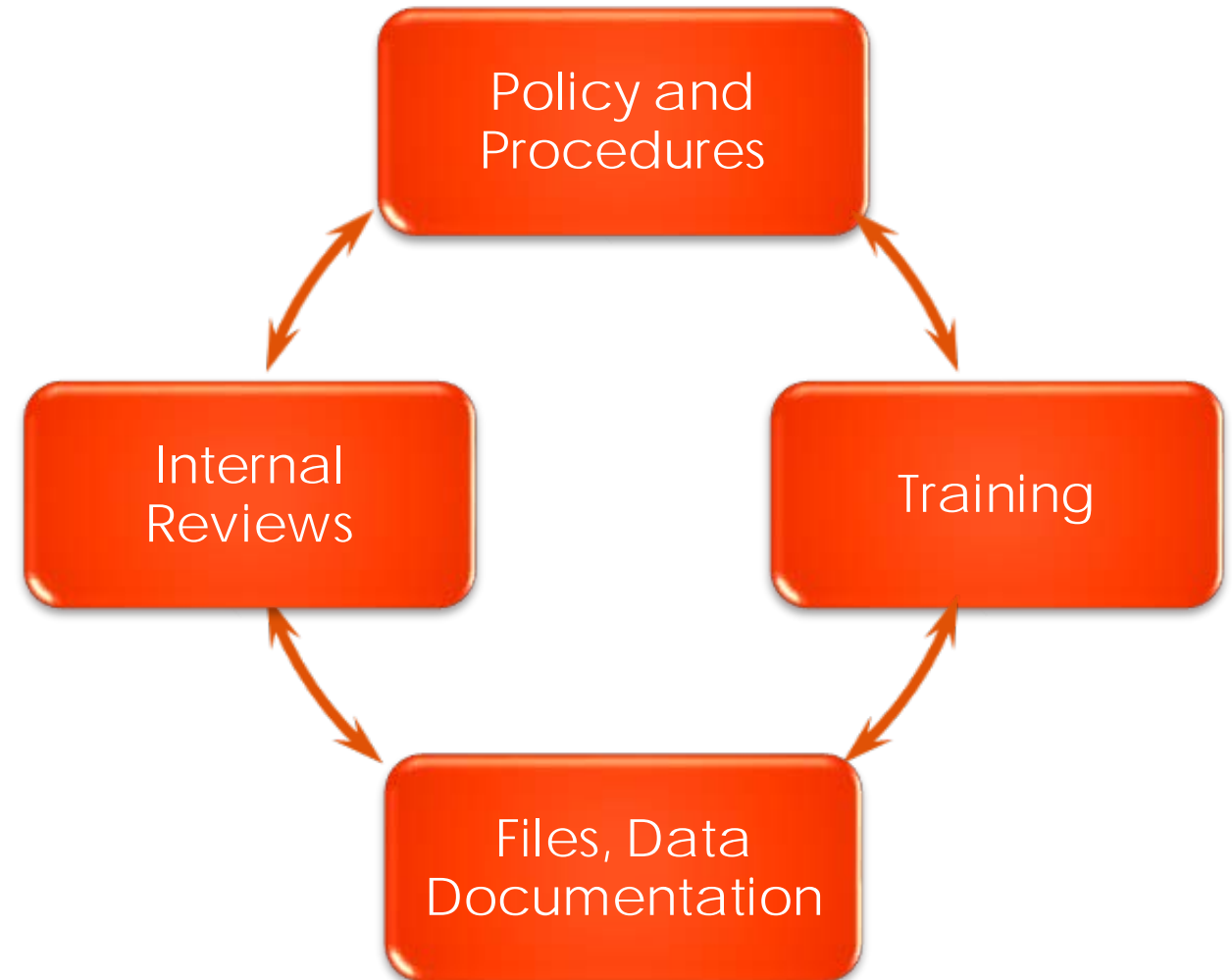
I'm CMMI Level X and ISO 900X certified compliant. Isn't that good enough?

I have the latest "LMNO" software package that the Government wants a Contractor to have. Isn't that good enough?



COMMON MISUNDERSTANDINGS ACROSS BUSINESS SYSTEMS

- Business Systems have four elements, as shown
- Business Systems are to be constantly being reviewed and updated
- Business Systems require controls



COMMON MISUNDERSTANDINGS ACROSS BUSINESS SYSTEMS

- Each Business System has many REQUIREMENTS:
 - Accounting System
 - 18 Requirements from DFARS 252.242-7006
 - DCAA Audit Program
 - Estimating System
 - 17 Requirements from DFARS 252.215-7002
 - DCAA Audit Program
 - Purchasing
 - 24 Requirements from DFARS 252.244-7001
 - 30+ DCMA Checklist items
 - 11 Requirements from FAR Part 44.303

COMMON MISUNDERSTANDINGS ACROSS BUSINESS SYSTEMS

- Policy and Procedures
 - Must have written policy and procedures that address the all applicable requirements
 - Actual practices have to mirror policy and procedures, no “paper tiger”
 - Policies and procedures must provide an adequate description of how your system operates and roles/responsibilities
- Training
 - Personnel participating in the business system must be trained annually at a minimum
 - Documentation of provided training must be retained (i.e. training materials)
 - Employees must have proof of having received training (i.e. sign-in sheets, rosters)



COMMON MISUNDERSTANDINGS ACROSS BUSINESS SYSTEMS

- Files, Data, Documentation
 - Establish and maintain adequate documentation to provide a complete and accurate history of business system transactions and controls
- Internal Reviews
 - At least one review of your business system annually by either your:
 - Compliance Officer
 - Internal Quality Control Group
 - Internal or External Audit Team





COMMON BUSINESS
SYSTEMS AUDIT FAILURES

COMMON BUSINESS SYSTEM AUDIT FAILURES

1. Policy and Procedures:
Inadequate, not written, not used
2. Processes:
Do not follow Policy and Procedures, have inadequate controls
3. Training:
Staff inadequately trained, or training is not provided on a continuous basis
4. Internal Reviews:
No comprehensive review of entire business system, policies, training, all artifacts
5. Artifacts/Files/Reports:
Lack of consistency across reports/files/artifacts
No evidence of following policy and procedures, especially timely reviews



— **SPECIFIC BUSINESS
SYSTEMS AUDIT FAILURES**

Learning and
Development

ACCOUNTING SYSTEM IMPORTANCE

PURPOSE (from DFARS Part 242.242-7006 -- Accounting System Administration) [Selecting contract type: FAR 16.104(i) & 42.302(a)(12)]

“Accounting system” means the Contractor’s system or systems for accounting methods, procedures, and controls established to gather, record, classify, analyze, summarize, interpret, and present accurate and timely financial data for reporting in compliance with applicable laws, regulations, and management decisions, and may include subsystems for specific areas such as indirect and other direct costs, compensation, billing, labor, and general information technology.

DFARS lists 18 criteria for an acceptable accounting system

ACCOUNTING SYSTEM AUDIT FAILURES

1. Contract set up

- Lack of internal control

2. Data Entry

- Lack of descriptions when adjusting something on audit trail

3. Overriding controls not in accordance with policy and procedures

4. Timesheets: controls being overridden

5. Treating like costs dis-alike.

ESTIMATING SYSTEM IMPORTANCE

PURPOSE (from FAR Part 15.407-5 -- Estimating Systems)

An acceptable estimating system benefits both the Government and the contractor by increasing the accuracy and reliability of individual proposals. It also reduces the scope of reviews to be performed on individual proposals, expedites the negotiation process, and increases the reliability of proposals. Significant deficiencies not corrected by the contractor shall be a consideration in subsequent proposal analyses and negotiations.

DFARS lists 17 criteria for an acceptable estimating system

ESTIMATING SYSTEM AUDIT FAILURES

1. Ranges are too large to be statically correct or believable.
2. Explanation of judgement usage.
 - Estimating of hours does not include estimation of impact on indirects with directs.
 - No SME discussion of how they came up with estimate.
3. Backing into rate to win number without justification or use of historical data
4. Deviating from requirements of RFP
 - Noncompliance with FAR table 15-2
5. Not going back and updating original estimate to actuals

PURCHASING SYSTEM IMPORTANCE

Objective from FAR Part 44.301

The objective of a contractor purchasing system review (CPSR) is to evaluate the efficiency and effectiveness with which the contractor spends Government funds and complies with Government policy when subcontracting. The review provides the administrative contracting officer (ACO) a basis for granting, withholding, or withdrawing approval of the contractor's purchasing system.

PURCHASING SYSTEM AUDIT FAILURES



1. Noncompliance with public laws, regulations, and prime contract requirements
2. Lack of competition, too many sole/single source and lack of adequate justifications
3. Failure to adequately perform and/or document price analysis and source selection
4. Failure to adequately conduct and document commercial item determinations;
5. Failure to obtain required certifications at time of award (*i.e.* TINA, CAS, suspension/debarment, limitation on use of appropriated funds)

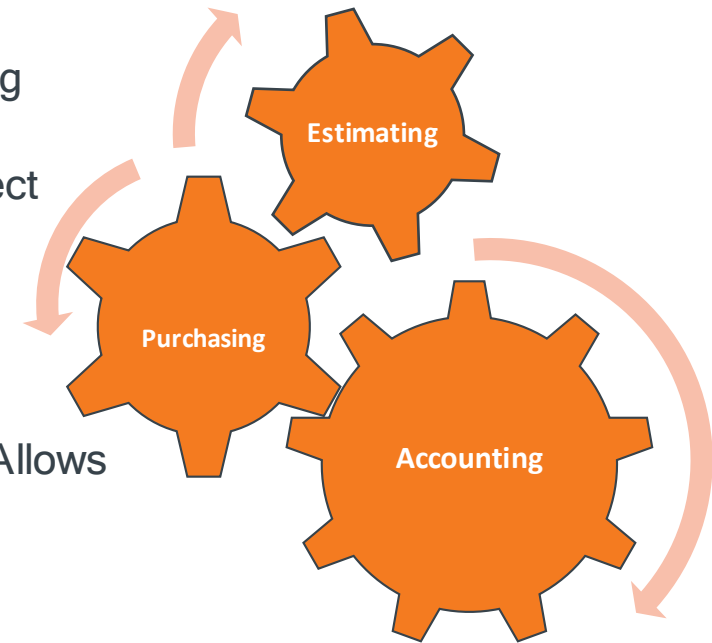


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INTERRELATIONSHIP OF THE
BUSINESS SYSTEMS

Learning and
Development

INTERRELATIONSHIPS OF THE BUSINESS SYSTEMS

- Starts with Estimating and the proposal
 - Price Analysis of subs and vendors should roll into purchasing and should be using data from accounting system to compare
 - Estimate should be using your Accounting System information for direct and indirect rates
- Accounting
 - Award information go in accounting system correctly, controls for subs too.
 - Bid, book, bill: Setting up in accounting system as it was structured in proposal. Allows for easier revenue recognition process.
- Purchasing
 - Awarding subcontracts/POs and using price analysis (updating) from proposal stage
 - Setting up subs and vendors in accounting system
 - Some purchases could require different accounting (related parties)

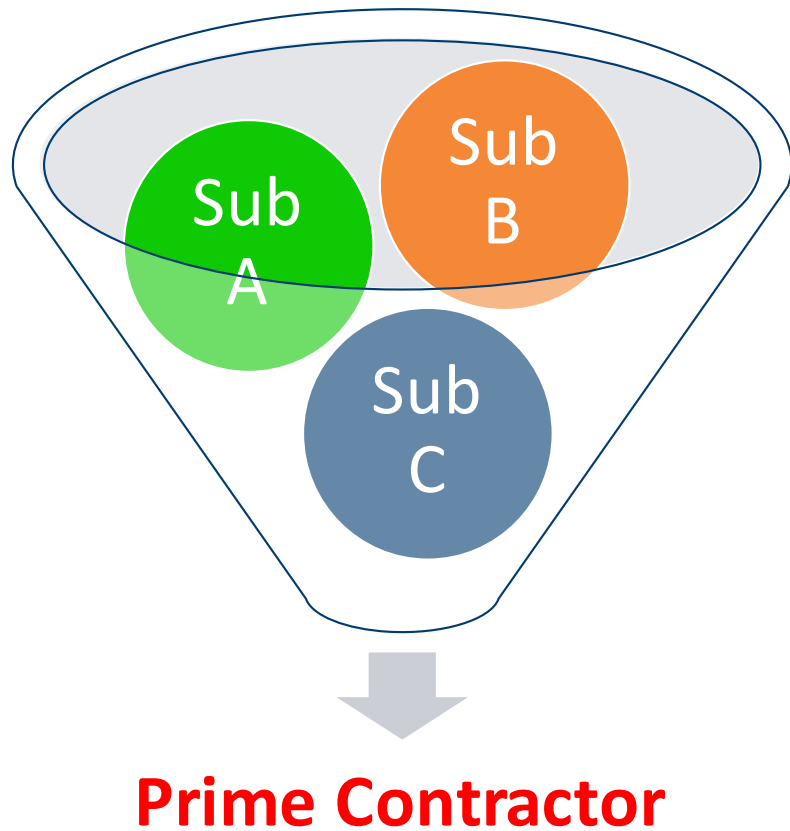




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RESPONSIBILITIES OF THE
PRIME FOR THE
SUBCONTRACTOR'S
BUSINESS SYSTEMS

ACCOUNTING SYSTEM RESPONSIBILITIES

(Prime-Subcontract Relationship) FAR 42.202(e)(2)



- Subcontractor's accounting system is able to handle the type of award.
 - Cost Reimbursable (e.g. Incurred cost submission, indirect allocation, etc.)
 - T&M / Labor-Hour contracts (e.g. timesheets, Labor distribution, etc.)
 - Firm-fixed price
- Billing and invoicing (e.g. billing terms)
- Periodic performance reporting - Level of effort, project status, etc.

ESTIMATING SYSTEM RESPONSIBILITIES

- Flowdown DFARS Clause 252.215-7002, Cost Estimating System Requirements, in all solicitations and subcontracts to be awarded on the basis of certified cost or pricing data (no FAR clause)
- Include in subcontract, that subcontractor will allow Prime (or independent 3rd party) to audit/review the subcontractor's Cost Estimating System elements upon request
 - Estimating Policy and Procedures
 - Basis of Estimate
 - Management reviews of estimates
 - Cost and pricing support documentation



PURCHASING SYSTEM RESPONSIBILITIES

- Prime Contractor “stands in the shoes” of the Government when allowing 1st Tier subcontractor to make direct purchases on Federal contract
- Flowdown DFARS 252.244-7001 Purchasing System Requirements or FAR 52.244-2 Subcontracts
- Include in subcontract, that subcontractor will allow Prime (or independent 3rd party) to audit/review the subcontractor’s Purchasing System elements upon request
 - Non-competitive selection justifications
 - Price analyses
 - Representations and certifications from 2nd tier sub
 - Debarment representations from 2nd tier sub
 - Cost and Pricing certifications, when required





THE 5TH PILLAR OF
BUSINESS SYSTEMS:
CYBERSECURITY

FAR 52.204-21: BASIC SAFEGUARDING- COVERED CONTRACTOR INFORMATION SYSTEMS

- Imposes 15 “basic” security controls on “systems” holding **Federal Contract Information (FCI)** (not the information itself like DFARs);
- “Information not intended for public release, provided by *or generated for* the government under product or service contract”;
- Covers all Federal contractors since (i) it covers *systems* which “may” hold FCI & (ii) the safeguarding is “most basic” protection.

DOD - DFARS 252.204-7012: NETWORK PENETRATION

- **Covered Defense Information (CDI):** Unclassified controlled technical information (UCTI) or Controller Unclassified Information (CUI)
 - (i) marked or identified by USG as provided to contractor, or
 - (ii) *collected, developed, stored, transmitted, processed, or used by contractor* in contract performance;
- Excludes commercial-off-the-shelf (COTS) contracts (+ basic research);
- Contractor information systems must satisfy NIST SP 800-171

DOD - DFARS 252.204-7012: NETWORK PENETRATION

- Cyber incident reporting within 72 hours of discovery directly to DoD Cyber Crime Center (DC3) with DoD reporting code to prime contractor;
 - Acquire DoD approved medium assurance certificate to communicate with DC3 regarding the cyber incident
- Post Cyber Incident audit requirements;
- Flows down to Subs if CDI retains characteristics;
- If external Cloud Service Provided (CSP) to be used, the CSP must meet FedRAMP “moderate” security requirements + cyber incident reporting/audit requirements.



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KEY TAKEAWAYS

TOP 5 KEY TAKEAWAYS

- Remember it's a system not a software package
- Know the criteria of each business system and make sure your Policy and Procedures address them all
- Train your personnel at least annually on each business system
- Use checklists to ensure your business system artifacts are consistent
- Perform internal reviews of your business system annually at a minimum



QUESTIONS?



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RESOURCES

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