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Contracting for Audit and
Management Advisory Services
With the Federal Government**

Lester A. Fettig

AICPA

**American Institute of
Certified Public Accountants**

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Federal Financial Management: Contracting for Audit and Management Advisory Services With the Federal Government

Lester A. Fettig

**Issued by the
Federal Government Division
American Institute of
Certified Public Accountants**

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Director's Preface

Federal contracting activity has grown in direct proportion with the federal budget, which now exceeds \$600 billion a year. Over \$100 billion is spent on direct purchases of goods and services from the private sector, and approximately \$100 billion is spent on federal assistance to state and local governments, universities, and other nonprofit organizations.

This increase in federal spending has brought with it an increased emphasis on accountability and a growing need for financial and compliance audits of recipients of federally assisted programs by CPAs. Accounting firms are also providing a variety of management advisory services to the government.

Federal contract records for fiscal 1979 show that over 31,000 separate firms provided professional, technical, and management services to federal agencies. Within this category 338 firms specifically performed financial auditing services. Both figures probably underestimate contractor activity because many such contracts are coded and accounted for in other special categories.

The purpose of this book is to provide the fundamental grounding in federal contracting for audit and management advisory services—from the “how to” specifics of bidding and negotiating, through the performance of federal work. It incorporates the latest public laws, regulations, and best advice on those judgmental issues involved in bidding, negotiating, pricing, and performing federal contracts.

Federal contracting is neither mysterious nor complicated; it is “different” in many respects, but an understanding of basic guidelines is all that is needed to begin to participate. The important point to consider about the federal marketplace is that there is no one “typical” situation.

This publication is the work of Lester A. Fettig, who has years of experience in federal contracting, financial assistance programs budgeting and management, systems acquisition, and legislative and executive branch procedures. Mr. Fettig is a consultant on federal contracting matters. Prior to becoming a consultant he was administrator of the Office of Federal Procurement Policy, in the Office of Management and Budget. He was staff director for the U.S. Senate Governmental Affairs Subcommittee on Federal Spending Practices, Efficiency, and Open Government, where he managed numerous pieces of contract legislation signed into law by three presidents. He began his career as an operations

research analyst with Lockheed-California Company and later served as a member of the professional staff for the Congressional Commission on Government Procurement.

As with any work of this nature, the resulting product is the culmination of the efforts and contributions of many individuals. The author wishes to thank particularly members of the AICPA task force who provided technical assistance: Donald S. Grenough, Sy Herman, Leslie A. Leiper, James J. O'Neill, and especially Terri S. Meidlinger, who managed the project. In addition, thanks go to Marie Bareille for her editorial assistance.

Joseph F. Moraglio, Director
Federal Government Division

With deep respect for Senator Lawton M. Chiles of Florida, an elected leader who brought uncommon thoughtfulness, substance and energy to the field of federal contracting; and in fond memory of Herbert Roback, who showed us all the way.

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1 The Role of Private Firms

The United States federal government is the largest single consumer of goods and services in the world. With a total budget now in excess of \$600 billion a year, direct purchases of goods and services exceed \$100 billion and cover the gamut of products and services available in the private sector. Indirectly, federal assistance outlays—grants and cooperative agreements to third parties—generate a comparable range of demand, with total assistance spending also in excess of \$100 billion annually.

Notable in the array of federal needs is a large and growing demand for audit and management advisory services—the kind of services offered by both large and small CPA and professional services firms.

Theoretically, the government might rely on its own capacity to perform these audit and management advisory services, and, to some degree, it does maintain an in-house capability. However, federal policy principally has been to contract with independent firms to perform these services. This principle of relying on the private sector derives from formal policy contained in Office of Management and Budget Circular A-76. Further information about this circular is included in Appendix 1.

Except for special cases whose extreme public sensitivity makes the government's own involvement more appropriate, it makes good sense for the government to rely on private firms, since both it and the taxpayers benefit from the rigors of free enterprise, and the special skills and qualifications offered by certain private firms can be tapped as needed.

The harnessing of private capabilities to meet public needs is one of the unique features of American government—literally tens of thousands of separate contract actions are executed each year. Not surprisingly, a substantial, constantly fluid body of statutes, regulations, and administrative organizations has grown up around this federal spending process.

Small or uninitiated firms may be apprehensive about the federal marketplace's unique policies, procedures, regulations, and forms. After receiving a federal contract solicitation, one small firm in Chicago returned it with this note: "I would have to hire a staff of lawyers and CPAs myself just to be sure I understood all the terms and conditions that are in here."

That firm did the taxpayers and itself a disservice by not taking a more thoughtful look at the possibilities of bidding on federal work. We all benefit when a larger base of talent and skills is brought to the competitive arena. Federal contracting is neither mysterious nor complicated; it is "different" in many respects, but an understanding of basic guidelines is all that is needed to begin to participate.

The purpose of this book is to provide the fundamental grounding in federal contracting for audit and management advisory services—from the "how to" specifics of bidding and negotiating through the performance of federal work.

Although this guide is intended as a practical introduction for the small and uninitiated firm, it will also be valuable to those firms that already engage in federal work as an ongoing part of their business. It incorporates the latest public laws, regulations, and the best advice on those judgmental issues involved in bidding, negotiating, pricing, and performance on federal contracts.

2 Figures and Trends

Federal contracting activity has grown in direct proportion with the federal budget and will continue to do so. Both can be expected to continue to rise with, at least, the rate of inflation.

Special factors have affected the increase in demand for audit and management advisory services—most notably, the rapid expansion of federal assistance programs during the late 1960s and early 1970s. The increased awareness of and concern about waste, fraud, and abuse in federal programs in recent years has placed growing emphasis on financial and compliance audits.

The Federal Procurement Data Center (FPDC) prepares quarterly reports that are available on request and that provide information about which federal agencies have bought goods and services and in what quantities.

Data available through the Federal Procurement Data Center reports include the following:

- Number and value of contract actions.
- Analyses of contract activity for each federal agency.
- Type of contractors receiving awards.
- Types of contracts awarded.
- Small and minority business contract award preferences.
- Geographic distribution by state.
- Analyses by type of product and service, as well as other specialized information.

The fiscal year 1979 FPDC report shows the magnitude of contract activity by agency. Figure 1 displays total contract actions and dollar values for selected agencies and contract actions and dollar values for the type of service of interest here: professional, technical, management, and financial auditing services.

Figure 1
FEDERAL CONTRACT ACTIONS—
ACTIONS AND DOLLARS BY EXECUTIVE DEPARTMENT AND AGENCY

Executive Department/Agency	Total Awards		Professional, Technical and Management Services		Management Services Financial—Auditing	
	Actions	Dollars (000)	Actions	Dollars (000)	Actions	Dollars (000)
Department of Agriculture	566,208	1,817,158	605	31,109	4	124
Department of Commerce	57,164	201,304	567	58,611	15	530
Department of Defense	11,400,769	70,423,311	16,649	2,902,421	20	12,673
Department of Energy	53,371	5,754,298	197	259,076		
Department of Health, Education and Welfare	560,758	1,669,683	2,030	321,634	162	20,191
Department of Housing and Urban Development	13,648	112,421	185	28,598		
Department of Interior	560,492	1,223,431	1,351	112,355	16	638
Department of Justice	471,295	195,409	220	37,395		
Department of Labor	23,494	305,152	333	42,010	46	4,673
Department of Transportation	261,613	1,013,717	550	238,180	13	79
Department of the Treasury	115,514	294,550	74	7,343	4	323
Community Services Administration	1,490	4,549	22	2,109	1	48
Environmental Protection Agency	53,320	341,352	1,002	133,712	34	1,870
Veterans Administration	1,847,745	1,628,852	363	39,185	4	255
Other	935,052	9,394,028	6,929	920,798	19	1,165
Total	16,921,933	94,379,215	31,077	5,134,536	338	42,569

SOURCE: Annual Report of Federal Contract Awards, Fiscal Year 1979 (October 1, 1978–September 30, 1979); Special Report no. 0338 (Washington, D.C.: Federal Procurement Data Center, Office of Federal Procurement Policy).

Professional services, including audits and management advisory studies, accounted for over \$5 billion alone.

Federal contract records for fiscal year 1979 show that over 31,000 separate firms provided professional, technical, and management services to federal agencies. Within this category 338 firms specifically performed financial auditing services. Both figures probably underestimate contractor activity because many such contracts are coded and accounted for in other special categories.

Demand for audit services does not arise directly from federal agencies alone but also from the grant recipients: state and local governments, universities, and other nonprofit organizations. The latter, an equally large and important market, also centers on a few major federal agencies. Figure 2 shows grant outlays to state and local governments by agency. Note that the Department of Health and Human Services will provide 32 percent of total estimated grant-in-aid outlays in 1981, far more than any other agency.

The audit requirements and sponsoring organizations vary widely among the more than one thousand federal domestic assistance programs. The *Catalog of Federal Domestic Assistance*, compiled by the Office of Management and Budget, contains detailed information about federal programs, including audit requirements. See Appendix 1 for further information about it.

A final draft of a model procurement code for state and local governments has been completed by the American Bar Association's Model Procurement Code Project Group. The model provides the statutory principles and policy guidance for managing and controlling the procurement of supplies, services, and construction for public purposes. A copy of the ABA's Model Procurement Code can be obtained by writing to the address listed in Appendix 1.

Competitive Base

On the supply side, more than one-quarter-million separate firms provide goods or services on federal contracts in any given year. Audit and management advisory services are rendered by an equivalently broad base of both large and small practitioners throughout the country. According to the latest Federal Procurement Data Center reports, 338 separate firms provided financial auditing to federal agencies. The types of firms active in contracting for audit and management advisory services range from the

Figure 2
FEDERAL GRANT-IN-AID OUTLAYS BY AGENCY

Agency	Actual 1979	Estimate	
		1980	1981
Funds appropriated to the president	521	601	2,902
Department of Agriculture	5,313	6,072	6,183
Department of Commerce	2,255	1,021	1,095
Department of Education	5,994	6,919	7,691
Department of Energy	83	367	549
Department of Health and Human Services	26,666	28,909	30,788
Department of Housing and Urban Development	6,405	7,701	8,837
Department of Interior	1,029	1,234	1,321
Department of Justice	505	457	466
Department of Labor	10,390	10,131	11,058
Department of Transportation	10,353	11,301	11,572
Department of the Treasury	7,818	7,413	8,166
Environmental Protection Agency	3,963	4,108	4,187
Community Services Administration	739	1,779	511
Other	825	931	986
Total Outlays	82,858	88,945	96,312

SOURCE: Special Analysis H, Budget of the United States Government, 1981. (Washington, D.C.: Office of Management and Budget, January 1980).

eight largest public accounting firms to smaller, local public accounting firms.

Virtually any firm in the country could qualify for, and effectively perform, the required services. Government solicitations often result in dozens of proposals, and competitive pressure, particularly regarding costs, can be intense. Often, the nature of the requirements will automatically reduce eligible competitors to a select few that have the peculiar skills, experience, staff, and flexibility called for. In still other, more restrictive situations, the special requirements will mean that only several currently experienced firms will have a chance to compete successfully. And finally, in some cases, there will not even be competition in that sole-source awards to one uniquely qualified firm may limit entirely other opportunities to bid.

The important point to consider about the federal marketplace and the competitive base is that there is no one “typical” situation. Competitors may range from frequent to occasional government performers, and the contest may range from a wide-open, “anybody’s ballgame” to a pro forma competition or sole-source award.

Most firms interested in maintaining a steady and substantial federal client base, obviously, will try to develop their qualifications and familiarity to target increasingly the less competitive, more specialized contract requirements. But in any event, the firm should always assess likely competitor qualifications and the nature of the competitive situation—factors discussed in detail in chapter 6. Appreciating the diversity of competitive situations is crucial to a firm’s successful entry into the federal marketplace.

3 The Regulatory Structure

The variety of contracting policies, procedures, regulations, and forms that apply to federal contracts originate from several sources. In descending order of precedence, they are

- Public law, passed by the Congress and signed by the president.
- Executive order, issued unilaterally by the president.
- Government-wide directive issued from the Executive Office of the President, notably the Office of Federal Procurement Policy in the Office of Management and Budget.
- Federal agency regulations.

In virtually all cases, whatever the original source of the contracting provision—public law, executive order, or Office of Management and Budget (OMB) or Office of Federal Procurement Policy (OFPP)—the specific procedures are spelled out in regulations issued by the implementing agency.

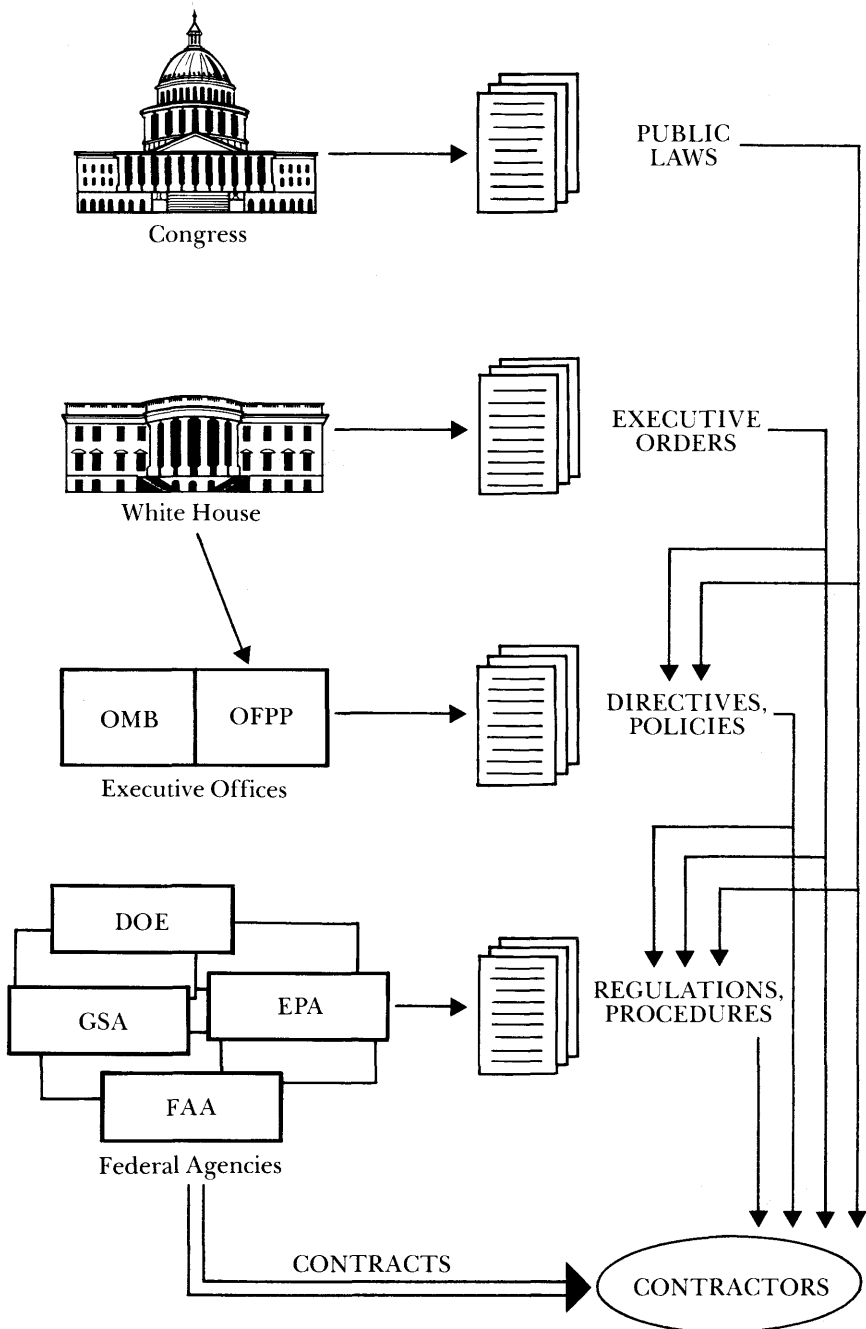
The purpose of this chapter is to lay out the fundamental structure of the statutes and regulations that control federal contracting practice. Figure 3 provides a simple graph of the origin and flow of contracting provisions.

Statutes

The basic method of acquiring goods and services is one of “formal advertising”—with the government issuing a precisely tailored specification and the award going to the low bidder. Clearly, as appropriate as this approach might have been in the late 1940s, it has come to be more and more irrelevant in acquiring a broad range of goods and services—especially professional services—where the qualitative differences between firms and offers are equally if not more important than the final price.

Figure 3

SOURCES OF CONTRACT REQUIREMENTS



There are several key pieces of law devoted to particular contracting issues of specialized subjects, for example—

- The Brooks Act of 1972 (Pub. L. 92-582) takes precedence and governs contracting procedures for the acquisition of architectural and engineering services.
- The Contract Disputes Act of 1978 (Pub. L. 95-563) governs the rights and procedures of parties in the event of disputes in the performance of government contracts.
- The Truth in Negotiations Act (Pub. L. 87-653) sets the statutory requirements for disclosure and access to books and records pertaining to the performance of government contracts.
- The Small Business Act of 1958 (Pub. L. 85-530) and the Small Business Act Amendments of 1978 (Pub. L. 95-507) lay down the federal contract provisions and preferences for small and disadvantaged businesses.
- Public Law 85-804 empowers federal agencies to grant extraordinary relief to failing contractors above and beyond that permitted in the original, basic procurement statutes.

All of the applicable statutes expressed in an agency's regulatory system and related contract provisions are spelled out clearly in the basic contract documentation. The important point, then, is not that a firm needs in-depth expertise on all possible contracting conditions, but rather, that it should have a general appreciation for the scope of possible special conditions and, therefore, an alertness to them as they arise in contract solicitations. In addition, the contracting officials of the agency are under an obligation to respond to any and all questions concerning contract provisions.

Executive Orders and Directives

Contracting conditions also emanate from levels of lesser authority than public law. Executive orders issued by the president carry the next highest precedence; for example, President Carter's executive order 12138, signed May 18, 1979, enjoins federal agencies to set preferential goals for the participation of women-owned businesses in federal contracts—a requirement that is not reflected in agency regulations per se but in agency internal operating reviews and monitoring systems.

The Office of Management and Budget, operating by itself or in concert with its statutory adjunct, the Office of Federal Pro-

curement Policy, may issue contract-related circulars, bulletins, or policy letters that are binding on the federal agencies and are either transcribed or reflected in their operating regulations, for example—

- OMB Circular A-76 governs agency procedures for determining whether work should be done on contract at all or performed by the agency itself. (See Appendix 1 for further information about this circular.)
- OMB Circular A-102 governs standards for federal assistance programs, and its Attachment O sets minimum requirements for the contracting practices that can be used by recipients of federal funds. Attachment P establishes audit requirements for state and local governments that receive federal assistance. (See Appendix 1.)
- OMB Circular A-120 governs agency management practices to control the use of consultants, including personal appointments as well as consultant contracts. (See Appendix 1.)
- OFPP Policy Letter 78-2 sets down the requirement, reflected in agency procurement regulations, that competition for professional services contracts be conducted in a manner that prevents firms from reducing professional salaries in order to gain a cost advantage—a restriction on so-called “wage busting” practices. (See Appendix 1.)

Appendix 1 also contains reference to an OMB publication, *Financial Management of Federal Assistance Programs*, which summarizes a series of OMB circulars dealing with the financial aspects of federal aid programs.

All of these issuances—executive orders, OMB, and OFPP directives—take precedence over any regulations on the same subject.

Agency Regulations

The actual procedures and rules that the firm will be subject to in contracting with an agency are the agency regulations.

The two basic sets of procurement regulations—the Defense Acquisition Regulations (DAR) and the Federal Procurement Regulations (FPR), are the models from which all other agency regulations are derived. (Chapters 6 and 7, herein, discuss the pertinent sections of the DAR and FPR.)

Fortunately, it is not necessary to stay abreast of all regulations and their provisions, since contract documents will contain or

refer to all essential features. A firm should obtain copies of just those regulations for the agencies with which it is seeking to do business and become generally familiar with their contents.

In the very near future, the regulatory situation may improve dramatically with the issuance of a single set of contracting regulations for the entire federal government—the Federal Acquisition Regulations (FAR). Targeted for completion by 1982, the FAR will be the basic source document for federal contracting rules and procedures. All parts of the common regulations have already been written and subjected to public review under an initiative by the Office of Federal Procurement Policy. The FAR will be centrally maintained and updated and will be published in the Code of Federal Regulations.

For the present, however, copies of pertinent regulations can be obtained through the individual agencies. These regulations are updated through the *Federal Register*, which is issued daily and is preferable to the Code of Federal Regulations (CFR), since CFR material is infrequently updated and, in many cases, does not include collateral instructions issued by different offices within the agencies.

Commerce Clearing House publishes a variety of services that include agency regulations, audit guides, and OMB circulars. (See Appendix 1 for information on how to obtain these publications.)

4 Government Entities Involved

A firm doing business with federal clients should have at least a basic appreciation for the government entities involved and an understanding of pressures that come to bear on each, how they perceive the contracting situation and, most importantly, what they can or can not do that might affect the firm's contract business.

This chapter provides an overview of the federal government offices and personnel involved in the contracting arena and offers basic orientation for uninitiated firms, including some insights into the relationships between government organizations.

Executive Office of the President

The highest executive branch focus for contracting matters is the Office of Federal Procurement Policy established by law in 1974 (Pub. L. 93-400) as a part of the Office of Management and Budget in the Executive Office of the President.

The OFPP, originally created with a five-year "sunset" life-span, received a four-year reauthorization in 1979. The office has authority over all contracting matters, in concurrence with the director of OMB, including authority to review and veto agency acquisition regulations. The administrator of the OFPP is appointed by the president and is subject to confirmation by the Senate.

Important to the firm doing business with the federal government is the fact that, legally, the OFPP cannot intervene in particular contract actions. This provision was intended both to prevent the OFPP from becoming a final "contract appeals" forum and to give it self-protection: With over ten million contract actions a year, any kind of direct intervention would be impossible.

Those firms committed to an ongoing business with federal clients should keep abreast of the activities and initiatives of the OFPP through its annual report to, and its frequent testimony before, Congress, its policy directives, and its issuances, which are covered routinely by all specialized contracting newsletters and digests.

Another critical part of the Office of Management and Budget, although not separately established by law, is the financial management branch of the OMB Budget Review Division. This unit is the focus for audit and financial management standards relating to federal assistance programs and special classes of federal contractors—such as universities and nonprofit organizations. Government-wide standards and directives applicable to federal contracts and assistance programs are issued through the OMB system of directives, notably OMB Circular A-102. (See Appendix 1.)

The Federal Agencies

A firm doing business with a federal client should become familiar with the people and personalities involved in contract award and performance, who, depending on the agency, will carry different titles, ranks, and organizational affiliations.

Four key groups have much to say about certain aspects of contract award and performance: program officials, contracting officials, budget officials, and agency general counsels' offices.

The *program officials* are directly responsible for running and administering the activity that the audit or management advisory contract will support. They are the operating personnel who see to it that housing assistance programs or sewer construction grants or military studies and analyses actually serve the purposes for which they were intended. Despite the need to interact with the other groups discussed below, the firm is working for the program officials, who determine what contract work needs to be done, the scope of work, and the adequacy of the firm's performance.

The *contracting officials* are usually assigned to a separate contracts office in the agency to support several programs or, in cases of very large programs, assigned directly to work for the program officials. The contract people are the keepers of the rules and regulations, the skilled mechanics who make the contract machinery run. They are responsible for setting the terms of competition, preparing and distributing the contract solicitations, receiving the proposals, interpreting regulations, and fielding

questions and replies about the contract process. These people sign the checks, administer the contract, and review compliance with terms and conditions.

The designated contracting officer is the single authoritative point for validating all contractual actions, a position of legal supremacy. All changes, modifications, and disputes must flow through that person.

Being the legal conduit for contract matters, however, does not mean the contracting officer can exercise unilateral authority to dictate or change contract conditions. Obviously, the firm also has rights under the contract and the best contracting officers perceive their role as not only protecting the interests of the government but also preserving the rights of the performing firms, as, indeed, they must, since as the legal point of contact between the government and firm, the contracting officer labors under the obligation to facilitate solicitation, award, and performance, assuring that actions proposed and taken fall within acceptable legal and regulatory bounds.

The firm should be aware of the *budget officials*, who are usually separately located in the agency's comptroller and/or planning staffs. These people will rarely act directly on any particular contract matters, but they are the people who, in a broad sense, will determine how much latitude—namely, money—the program officials will have to execute their programs and fund their contracts and when they can receive the funds. The firm may frequently find that contract work hinges not on the unilateral decisions of the program official and contracting support but rather on the budgeting decisions from the comptroller's chain of command. Contract timing, award, slippage, and rearrangement can often be learned by inquiring about the budgetary constraints imposed by this third set of agency officials.

The fourth group that can heavily influence contract activity is the agency's *general counsel's office*—or the equivalent, which is usually a separate legal staff within the agency or division. These lawyers, some of whom will be designated contract specialists, will be called on to offer rulings and interpretations on contract procedures from a purely legal standpoint. It is important to appreciate the role that the contract legal staff can and does play in the event of less-than-routine contract complications.

Depending on the agency, the relationship between the program, contracting, budget, and legal officials may vary somewhat. But in general terms, the following can be expected:

- All will defer to the program officials on questions of work content, matters of judgment over required contractor qualifications, and contract execution.

- Both program and contracting officials will have to defer to the budgeting people the decisions that will limit the total resources available and the timing of contract commitments.
- Throughout the bidding, award, and execution stages, all officials will refer to the contracting officer (and, when needed, the supplementary advice from the legal staff) on matters of contract administration and compliance with rules and regulations.

A firm that wants the most mutually beneficial contract engagement will appreciate these facts and relationships and, in so doing, can become part of the program team to help the program officials cope with the constraints within which they, too, must operate.

Firms doing business with federal agencies should also be aware of the newly established *inspectors general* now required by law to be set up in all major agencies to report directly to the agency head and Congress on matters relating to waste, fraud, and abuse. Although established only in 1979 and without generalized patterns of operations, the inspectors general can be expected to keep contract and grant-related matters prominent on their agenda for investigations and audit.

The Congress

General jurisdiction over federal acquisition matters rests with the House Government Operations Committee and the Senate Committee on Governmental Affairs. Hearings and legislation on contracting will be focused in these committees. For example, as this book was being prepared, various bills were pending before those committees concerning the federal use of consultants.

Any committee with authorization jurisdiction over a particular agency—or an appropriations subcommittee handling that agency's budget—can be expected to play some role when contract procedures affect that particular agency's base of activity. For example, issues relating to contracting for research and development will automatically gain the attention of the committee responsible for the National Aeronautics and Space Administration and the Department of Energy.

In short, a firm doing federal business cannot feel that only one or several committees of Congress may be interested in a particular contract issue or procedure, although the main focus

is on the House Government Operations and Senate Governmental Affairs Committees.

An important contact for a firm doing federal business is the congressional delegation that represents that firm—the two senators and the local member of the House of Representatives, who have an obligation to know and to understand how government activities, including contracting, affect their constituents. Any firm that does business regularly with the federal government should make it a point to communicate with Congress on how government policies affect the firm.

Specifically, there are some things you should and should not expect from your congressmen. *Do* expect them to make inquiries on your behalf to help obtain full and complete explanations for contract actions that are apparently at odds with prevailing procedures. It is quite natural and normal for a member of Congress to act merely as a prominent spokesperson to request explanations or reviews on a particular contract question either from the cognizant agency officials or from the General Accounting Office (GAO).

Do not, however, expect congressmen to get involved with contract competition or award decisions. They should not and will not intervene unless it appears that proper procedures are not being followed or that certain regulations or provisions have been overlooked.

The General Accounting Office

The General Accounting Office, commonly referred to as Congress's "watchdog," is officially part of the legislative branch but does play a role in federal contracting. The GAO is heavily involved in audit and investigation of federal program activities, including contracts, and in recent years has emphasized program effectiveness and quality evaluation reviews beyond the more traditional audit role.

Most important to the contract process and the firm doing business with federal agencies is the fact that the GAO acts as a forum to hear protests related to bidding and award of federal contracts. This bid protest role remains something of a quasi-legal debate, in that GAO rulings are not literally binding on federal agencies. For example, if a contractor protests an award and the GAO finds in favor of that contractor, the agency may or may not reverse itself or recompute the contract. In fact, if the ruling

comes after award and the contract is under way, there is virtually no chance that the decision will be reversed.

Nevertheless, GAO rulings do provide an important forum for bid protests and, equally important, create a body of precedents and interpretations for acceptable contracting procedures that are carefully monitored and adhered to by executive agencies in their contracting activity. Figure 4 displays the GAO organizational chart.

Cost Accounting Standards Board

The Cost Accounting Standards Board (CASB) was established by Pub. L. 91-379 in 1970. Its chartered objective was to achieve uniformity and consistency in cost accounting principles used by defense contractors and subcontractors, and thus it issued standards that may be defined broadly as cost accounting principles. Adherence to these principles in proposing and costing negotiated national defense contracts over certain dollar values is mandated by law. It is important to note, however, that small businesses are wholly exempt from cost accounting standards.

The CASB achieved its objectives by issuing standards that now cover most, if not all, the major areas of cost accounting where significant disparity existed. Effective September 30, 1980, the CASB was dissolved because Congress did not fund it for fiscal 1981. Congress has not yet legislated a transfer of the board's authority or functions to another agency.

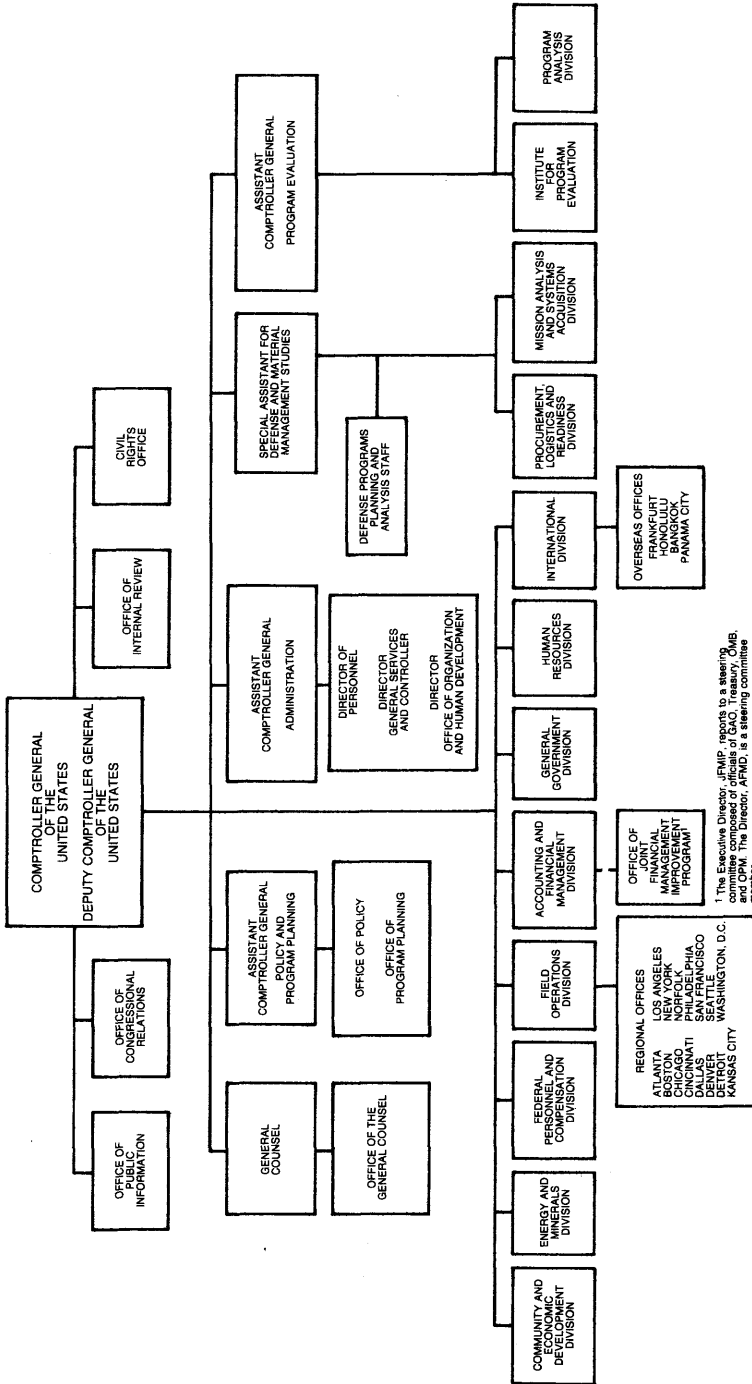
Subsequent to the establishment of the board, its standards, rules, and regulations were, with minor exception, incorporated into the Federal Procurement Regulations (FPR), which resulted in subjection of certain nondefense contracts and subcontracts to cost accounting standards. As a general rule, however, accounting firms, because of the nature of their work, are subject only to standards 401 and 402, which, together with promulgation comments by the CASB coincident to their release and a listing of the other standards, appear in Appendix 2, herein.

Notwithstanding these exemptions, any potential government contractor should have a general familiarity with these standards, since government auditors view some if not all of these standards as a codification of cost principles that have emerged from the litigation of appeals under government contracts.

A case in point is standard 401, the first standard issued by the board, which requires—quite logically—that costs shall be accounted for in the same manner in which they were originally bid.

Figure 4

UNITED STATES GENERAL ACCOUNTING OFFICE



Another example, stated in an oversimplified way, is cost accounting standard 402, which requires consistent treatment of like items of cost. If, for example, an accounting firm treats travel time or local travel costs as a direct cost on a government contract, government auditors will expect that similar costs related to nongovernment work are treated in a like manner, rather than included in indirect costs. On the other hand, that does not prevent travel costs of indirect personnel to be charged indirectly. Other standards that deal with broad, basic principles are regarded similarly by government auditors.

These two standards represent the foundation upon which ensuing standards were built.

5 Understanding The Client

In order to provide professional services, a firm must understand the client as well as the perceptions, pressures, and incentives under which the client labors.

Audit and management advisory services are particularly sensitive when the firm's performance becomes an essential ingredient in the government's ability to execute a program. The firm's performance can have a direct bearing on the government manager's own status and career. Well-done work or deficient performance can reflect alike directly on the program and the program official's effectiveness.

Audit Services

In performing audits, CPAs should adhere to the established standards and guidelines including the generally accepted auditing standards (GAAS) issued by the American Institute of Certified Public Accountants; the GAO *Standards for Audit of Governmental Organizations, Programs, Activities, and Functions* (Revised); OMB Circular A-102, entitled *Uniform Administrative Requirements for Grants-in-aid to State and Local Governments*; and audit guides for specific grant programs issued by the federal agency itself (more than 100 guides have been issued). A firm's performance will be carefully judged for a number of reasons.

First, government programs operate in a "fishbowl" before, during, and after funds are expended for a public purpose. In many cases, more must be done than a mere audit of financial transactions or an expression of an opinion on financial statements. These engagements usually include some compliance auditing

work, such as determining that the terms and conditions of the grant have been met by the recipient. Overlooked facts, discrepancies not fully pursued and settled, inadequate records or documentation, or subjective interpretations not fully disclosed all have the potential for severe embarrassment and later program repercussions.

Second, the government client must be able to depend upon the firm's objectivity. While the government manager and program officials may emphasize or de-emphasize particular aspects of an audit and they may have an opinion on which compliance and program performance features are most important, the firm should not take it upon itself to do anything but an audit in accordance with established standards, guidelines, or contract.

Third, conflicts of interest between the firm and the organization being audited are of extreme concern to the federal government. A firm should anticipate any and all conflicts arising from prior or current work performed for the same organization, interrelated owners or directors of the firm and the audited organization, and any and all financial interdependencies.

Overall, these points and many others could be made for all audit services, whether or not they are performed for a government client. They are, however, special sensitivities for government program officials, and the firm should be aware of them while performing its work.

For more detailed discussion of conducting audits of federal grantees, see an earlier AICPA study on accounting and auditing practices in the federal government, *Federal Grants-in-Aid: Accounting and Auditing Practices*. (See Appendix 1.)

Management Advisory Services

The needs of the federal client should be well served by the very same basic points of superior professional support provided to private clients. Professional services can range from expanded scope audits, which cover program effectiveness and program results, through crucial special studies and analyses that can be the principal sources for a government program official to make key management decisions on the character, content, and direction of his program.

This broad range of management advisory support is by no means routine. It is precisely the specialized nature of many federal management support requirements that make it most

appropriate to go to the private sector to obtain the best available expertise for the job at hand. Naturally, the concerns expressed earlier relating to audit services also apply to management advisory services. Some additional perspectives on the federal client's needs require careful consideration.

A firm contracts to provide its client with specific services. Unpredictable complications can and do arise in major government programs, and they need prompt and flexible resolution. A clear, written understanding of any modification of the scope of the engagement should be obtained to prevent later disputes and misunderstandings.

Second, in management advisory services, the federal client will value the ability of the contracting firm to do original research and thinking; in fact, the client may regard the program requirements as unique even when they are not. The firm should avoid telling the client what he already knows—or what he could routinely find out without the trouble and expense of retaining a professional adviser. Firms should provide the highest level of knowledge and experience in solving the government's problems.

Third, federal program managers will quickly evaluate the firm's personnel. Because the program is the manager's first priority, he will expect the firm to assign competent personnel to the engagement. Professionals named in the original proposals should adhere to their proposed roles, and the firm's leading contract professionals should be given command of any of the firm's internal resources necessary to effective performance of the contract.

Fourth, the federal government manager will need tailored expertise—expert professionals who understand his particular problems. The firm must assess its capabilities regarding each proposal request to determine whether it can truly offer the expertise needed for the job. If the capability does not exist, do not expect to “learn as you go.” Either get the expertise, make arrangements to get it by teaming with other firms on your offer or by retaining special consultants, or do not bid.

Fifth, initiative is extremely important to the federal client. Even large and regular federal contractors with millions in annual business can quickly lose their reputation and standing if they fail to appreciate that a contract may require them to tell the client what is needed. The managers will be looking for a firm that not only brings solutions to the government official's problems but also takes the initiative to point out unforeseen problems. Professional services contracts are not mundane supply contracts. Superior performance depends on the imagination, initiative, and

self-starting and self-managing qualities that a firm can demonstrate.

Sixth, the most successful contracting firm will invest the necessary time and effort to get to know the management environment in which the client is operating. That means talking to people who understand the management proclivities of the client's superiors and the budget issues facing the program, and being alert to congressional hearings, investigations, and reports that deal with program activities. It requires a careful marketing approach to build up a broad and contemporary appreciation for the organizations, issues, and attitudes that affect a client.

Price Versus Qualification

Before introducing the specific mechanics of contracting with the federal government, one more general subject should be discussed: the balance of price against qualifications in professional services, such as audit and MAS.

No other single issue has so dominated debate and discussion over professional service contracting as the contradictory objectives of qualifications and price. Consider the following ambiguous statement on the matter issued by a congressional commission on government procurement in its 1972 report—after two years of study.

The procurement of professional services should be accomplished so far as practicable, by using competitive proposal and negotiation procedures which take into account the technical competence of the proposers, the proposed concept of the end product, and the estimated cost of the project, including fee. The primary factors in the selection process should be the professional competence of those who will do the work, and the relative merits of proposals for the end product, including cost sought by the government. The fee to be charged should not be the dominant factor in contracting for professional services.

A product or service that does not meet required standards is no bargain whatever the price; on the other hand, no one wants to pay more than necessary to receive a professional and competent job.

This leaves—and will always leave—the subject of professional service contracting in the judgmental world where price is a factor in selection—but should not be the dominant one. A firm should be expected to perform a high quality, professional job, and, in

bidding government work, it cannot afford to sacrifice its highest professional standards. A quality professional job requires, among other things, costly supervision and review.

Many government officials may be tempted to select a firm because it offers a bargain basement price. When this happens, however, the government manager may get what he has paid for: bargain basement performance.

Government officials should not be constrained to select the most outstanding qualified firm if that firm also carries the most outstanding high prices, particularly if other, well-qualified firms can and will perform the work in top-notch fashion for considerably less.

The most frustrating part of this price versus qualifications issue is that there is no one answer, no simple rule, no set of magic guidelines that define the precise combination of winning ingredients. Firms must strive to give the government the best of both worlds: the best qualifications for the job at the lowest reasonable price.

Keep in mind always, however, that price should be the secondary consideration. Unless the firm is willing to propose a competent, professional capability to perform the work, no bid, no matter how low, will be appropriate. Do not bid barely qualified, shaky teams of people banking on price to be the deciding factor. Respond with the best talent the firm can offer. With that established, the safest path to follow is fair pricing of the talent and effort needed to perform the professional work. The government must get the services it needs—the firm must be fairly compensated for its services.

6 Contract Bidding And Award

The Award Process

Virtually all government contracting is the result of one of two procurement processes: formal advertising or competitive negotiations.

Formal Advertising

Formal advertising is the basic traditional approach to contracting and culminates in job awards to the low bidders. This approach is seldom used in professional services work where quality and qualifications are such important variables in the selection process.

In the terminology of federal contracts, formal advertising starts with invitations for bids (IFBs), which rigidly lay out all the details of work content: specifications, delivery schedules, and all elements designed to neutralize all differences among competitors except price.

A fixed period is allowed for receipt of bids, followed by a public opening, and award to the low bidder. Preaward surveys may be conducted, however, and may find the apparent winner unable to actually perform the contract, in which case the next lowest bidder may receive the contract. Firms so disqualified are termed “nonresponsible”—unable, technically or financially, to perform the contract—as opposed to disqualified firms that may be termed “nonresponsive”—failing to submit a proposal in conformance with the work standards set down in the solicitation.

Formal advertising is generally inappropriate when a federal agency must evaluate special expertise and judge comparative qualifications. Also, the very nature of audit and management

advisory services frequently precludes advance prescription of precisely what work will be needed. For example, the initial findings of an audit may require additional in-depth reviews of records or financial systems, an eventuality that cannot be foreseen and cannot be accounted for on a fixed-price, low-bid basis.

Competitive Negotiations

“Negotiation” is the broad term used to refer to all other contract methods not of the formal advertising type. The term embraces both competitive negotiations, in which formal competitions based on all factors, including price, determine the outcome, as well as situations where “sole source” negotiations may be conducted with only one firm in order to arrive at a contract.

Competitive negotiation is the main method used to contract for audit and management advisory services. The method is flexible enough to take price into account but, more importantly, permits the federal client to make intelligent choices, given the condition of the modern marketplace: to trade off features of experience, quality, qualifications, and value and take advantage of unique talents and proposals that might be offered and tailored precisely to federal needs.

The opportunity to trade off many factors, to take into account elements of quality as well as cost, does not give competitive negotiations a simple, cookbook style for predicting the winner in any given circumstances. This flexibility is illustrated in the form language used in the following typical contract case.

Award shall be made to that responsible offeror who can best perform the required work in a manner most advantageous to the Government. You are advised that paramount consideration shall be given to the evaluation of technical proposals in the award of the contract, and that proposed cost is secondary to the quality of this procurement.

The negotiation process begins when the federal agency goes to the private sector to seek “offers” (the term used in conjunction with competitive negotiations; the term “bids” is used to refer to formal advertising). For competitive negotiations, the government will issue “requests for proposals”—RFPs (as contrasted with the IFBs used in formal advertising).

On occasion, the government may subject especially large or complex requirements to some preliminary stages of competition before issuing the RFP. Therefore, the firm should also be alert to requests for qualifications (RFQ) statements that are sought to

identify firms who might be interested in eventually offering proposals and whose capabilities can be scanned first by the federal agency.

Once issued, the RFP may be modified at any time prior to the date set for receipt of proposals, or the date may be set back. In such cases, all potential offerors who have requested the RFP will be notified uniformly of any supplementary changes, additions, clarifications, and amendments in it.

Often, especially for large contracts, a preproposal bidders' conference will be held by the agency to give interested firms an opportunity to ask questions and further clarify the requirements of the RFP. Some RFPs may actually require attendance at such a bidders' conference to make sure that all firms clearly understand the agency's preferences and intent.

The RFP will also give the firm information on how the award will be determined or the relative importance of various factors that will be used to judge competing proposals. Firms should always pay special attention to the evaluation factors described in the RFP and request as complete a description as possible in order to be responsive to the client's needs. Agencies must at least give some indication of the relative importance of evaluation factors and, in some cases, may actually give the precise numerical weights and scoring method that will be used.

After the agency receives the proposals, it may simply choose the winning contractor—or decide to enter into further written and oral discussions with several offerors to further clarify their submissions. If discussions are held, they must be held with all competitors judged to be within a competitive range—nominally showing the ability to perform, if selected, within reasonable measure of other offerors.

Types of Contracts

The federal government uses a wide variety of specially tailored contracts, all of which, however, can be categorized as either fixed-price or flexibly priced contracts.

With fixed-price contracts, the contract price and scope of work is basically set at the time of award, and it is assumed that the work will be performed for that price. Flexibly priced contracts take two basic forms: cost or labor hour. Under the cost type, the contractor bills the government for actual costs incurred plus a fixed fee (profit). Under labor hour contracts, billings are

presented in terms of actual hours worked, extended by rates set forth in the contract. The rates, like normal billing rates, include base salary costs, indirect expenses, and profit.

There is a significant distinction between fixed-price and flexibly priced contracts. Under a fixed-price contract, the contractor is expected to complete performance of the work called for irrespective of the accuracy of his initial estimate of the cost or effort involved. Under flexibly priced contracts, however, the dollar magnitude of the effort is considered to be an estimate only, and the contractor is under no obligation to incur costs or to expend man-hours beyond those set forth in the contract without an appropriate increase in the contract value.

Audit and management advisory services will typically be procured under some form of flexibly priced contract, primarily because neither the agency nor the performing firm will be able to estimate accurately the full effort required by the work. If the contract involves a number of severable assignments the exact scope of which is undeterminable at the time of award, or there is otherwise no specific work content committed in advance, the contract may provide for control of effort by issuance of individual tasks. In this approach, the government project officer and the contractor reach agreement on the required extent of effort prior to the beginning of work on individual assignments.

While other types of contracts, such as fixed-price-incentive, cost-plus-incentive-fee, and cost-plus-award-fee, are used by government agencies, they are seldom, if ever, used in contracting for audit or management advisory services.

If the total cost contemplated by the government is less than \$10,000, the agency may elect to award the work by use of a purchase order rather than a contract. Purchase orders are awarded on a much less formal basis and do not require the extent of preaward review as do contracts.

Cost type contracts are preferred for audit and management advisory services. Because variations in anticipated work can and do occur, this type of contract reduces risks for both the government and the firm. The contractor knows that unforeseen demands will be compensated fairly, and the government has the assurance of paying only for that work and scrutinizing costs through the firm's internal accounting system.

Fixed-price contracts, on the other hand, offer the compensatory advantage of the firm's not having to reveal all cost and pricing data to determine reimbursements; the fixed price is set in advance. In some cases, the work is of such short, precise increments that this advantage may become important. Also,

under fixed-price terms, the contractor has the opportunity to earn a higher net fee if he is able to execute larger economies in contract performance than originally anticipated. However, a fixed-price contract may not be worth the risk. A more detailed discussion of the various types of contracts is included in an earlier AICPA study on accounting and auditing practices in the federal government, *Federal Financial Management: Accounting and Auditing Practices*. (See Appendix 1.)

Assessing the Firm's Capabilities

The most important techniques of bidding on federal work begin with the firm's careful, preliminary assessment of its particular capabilities in order to target specific segments of the federal marketplace. In this manner, the firm can concentrate its resources on the requests for proposals it believes offer a higher probability of success.

One of the most attractive aspects of contracting with the federal government is the wide range of opportunities it offers for the firm to grow into new and varied fields of capability. Literally no other client regularly demands such a variety of audit and management advisory services. Thus, the firm should identify not only the capabilities it already possesses—from performing financial and compliance audits through more expanded scope audits and specialized management advisory capability—but also the capabilities and expertise it seeks to build for the future.

Two considerations are important for new or small firms entering the federal marketplace:

1. Adding to the firm new professionals who can service existing clients but who also possess talents that can be used in responding to federal needs.
2. Arranging teaming with other firms to add complementary capabilities, which can be done either through a set of standing agreements between firms or on an ad hoc basis in response to a particular RFP.

Both techniques—new employees and teaming arrangements—are frequently used to build capabilities specifically solicited by the federal government, and they represent the essence of why the government looks to the private sector for needed services, namely, the opportunity to precisely match its needs against the talents available in private firms.

Small, Minority-owned, and Women-owned Business Preference Programs

Some firms may qualify for special consideration under one or more preference programs: small-business, minority-owned, and women-owned businesses.

By law, an agency can set aside a particular contract for only small businesses, which will be prominently noted when the IFB or RFP is issued. To do this, however, the agency must have made the preliminary determination that adequate competition is still expected to ensue even if the solicitation is so restricted.

Although not frequently done, especially for professional services, an agency may also make a partial set-aside—reserving a portion of a particular contract for award to, and performance by, a small-business firm.

In the areas of audit and management advisory services, a firm qualifies as a small business for purposes of federal contract preferences if its “average annual receipts for its preceding three fiscal years do not exceed \$2 million.” In other words, if the firm’s gross receipts have been averaging around \$2 million per year or less, that firm qualifies. Recent indications are that the revenue criterion may be changed to one that is keyed to the number of personnel, but whether this change will in fact be instituted is still uncertain.

The Small Business Administration (SBA) can also provide a very important service to a small firm, especially to those entering the federal marketplace for the first time.

In the event that a firm is the apparent winner, but, upon preaward surveys, is judged by the agency to be “nonresponsible”—not able to perform the work—the SBA, upon application by the firm, can vouch for performance by issuing a “certificate of competency.” Then the firm must be awarded the contract, because the SBA has now insured performance.

Generally, firms should become familiar with the complete range of services and opportunities offered by the Small Business Administration that go beyond direct federal contract involvement, including a variety of loan programs, counseling services, and other business assistance. SBA offices are listed in Appendix 3, herein.

The climate and environment for small businesses has been and will continue to be good, especially since the recently passed Small Business Act Amendments of 1978 (Pub. L. 95-507) now call for a formal goal-setting agreement between the federal contracting agencies and the Small Business Administration.

Special contract preferences are also available to firms owned by disadvantaged persons, which are now defined by law to be those that are at least 50 percent owned and managed by Blacks, Hispanics, and Native Americans (American Indians, Eskimos, Native Hawaiians, Aleuts and Asian Pacific Americans). The law also provides for the SBA's administrative designation of other minorities, now expanded to include Hassidic Jews. Women are not automatically designated as a disadvantaged group.

The minority business programs were only recently placed on a new, settled footing with the passage of Pub. L. 95-507. Before that time, the SBA's so-called 8(a) program sought to channel federal contracts to minority firms without clear definitions for eligibility and without effective legal grounding. The new law, however, in conjunction with a completely new set of SBA operating procedures, is expected to bring the 8(a) program to better levels of performance.

Under the program, the SBA contracts with the federal agency and, in effect, subcontracts with one of the qualified 8(a) firms that are on its list of eligible contractors. Minority firms must first apply to the SBA for 8(a) standing and, if certified, may then be eligible for directly set-aside awards from federal agencies.

Another important set of new preferences relates to minority business subcontracting. Recipients of federal contracts must now develop minority subcontracting plans and may actually receive additional contract payment for exceeding subcontracting goals. These added incentives will continue to make large federal contractors another important marketing point for small and minority businesses that may provide audit and management advisory services to the prime contractors.

Complete information and regulations on the minority program can be found in OFPP Policy Letter 80-2. (See Appendix 1.)

In May 1979, President Carter issued an executive order to enhance the posture of women-owned businesses, including provisions for all federal agencies to set goals and expand the number of federal contracts going to such firms. OFPP Policy Letter 80-4 sets forth amendments to be made to the FPR, DAR, and NASA PR relating to subcontracting with women's businesses under federal contracts. (See Appendix 1.)

Although this program does not enjoy the same legal status and rigorous procedures under the small- and minority-business programs, it does, nevertheless, make federal agencies particularly anxious to receive proposals from all qualified firms who can provide audit and management advisory services. Since goals and monitoring are part of the agency activity, competitive advantage

can be obtained by women-owned firms in cases where essentially equal qualifications and other factors are present.

With the existing preference programs available, teaming arrangements can maximize both the firms' opportunities and the government's objectives by incorporating the talents of small and minority-, and women-owned businesses, none of which may individually possess the complete set of skills required to perform government contracts satisfactorily.

Targeting the Federal Market

If the firm has done a thorough, realistic analysis of its existing and desired capabilities, then the task of targeting the federal market is fairly straightforward. As shown in chapter 2, several agencies dominate the demand for audit and management advisory services. Whichever agency or agencies and types of work the firm selects for focus, the objectives are to (1) narrow the field of interest to economize on resources spent in reviewing and responding to RFPs and (2) begin to build that foundation of familiarity with a particular agency and subject matter that will, in the long run, increase chances for successful proposals.

Having focused on only select RFPs from particular agencies and types of work, some time and consideration should be directed to understanding the needs of that particular marketplace prior to the receipt of the RFP. Larger firms with additional resources may consider paying office visits to the program officials in the agencies, even if there is no RFP of interest pending or in the offing.

In the case of audits for financial assistance efforts, some knowledge of the subject organizations that receive federal assistance monies and that have been or will be subject to compliance audits is frequently useful. In this connection, firms should try to develop a practical understanding of the subject matter and the particular problems and perspectives of potential clients. In these cases it may be useful to capitalize on current firm work related to nonprofit clients that are supported in part by grants, since such work becomes a base of knowledge for other types of audits financed in a similar manner with federal grants or assistance programs.

The firm may consider participating in—or at least monitoring—the activities of a variety of professional associations that regularly engage in either the subject matter of the programs or the general issues of contracting and auditing. If the specialized subject matter to be targeted deals with, for example, educational,

military, health, or housing programs, the firm should consider the advantages of obtaining some exposure to the professional societies that will offer concise and current data regarding important issues in those areas.

Other professional societies have charters to keep abreast more generally of the subject matter of federal contracting such as the National Contract Management Association (NCMA), National Assistance Management Association (NAMA), National Association of State Purchasing Officers (NASPO), National Institute of Governmental Purchasing (NIGP), and the Association of Government Accountants (AGA).

Monitoring the activities of, or belonging to, some of these associations offers the firm a relatively inexpensive way to keep abreast of current developments that will affect contracting for audit and management advisory services.

The firm may also consider monitoring the key issues and debates that occur during the annual authorization and appropriation process for the firm's targeted agencies and subject matter. The firm's capabilities will be enhanced by familiarity with the issues and debates and the protagonists and their views when it comes time to deal with the agencies under support contracts. For management advisory services, this kind of understanding becomes almost essential. The client will have to labor under and become a factor in these congressional perspectives; the firm should share an equivalent appreciation.

For small-business, minority-owned, and women-owned firms, visits to the SBA regional and headquarters offices can build personal familiarity with available assistance within the agency, procedures for obtaining assistance, and contract opportunities. Review the list of contact points presented in Appendix 3 for the location that can serve your firm.

Each major agency and department has an SBA representative; visits to that representative will underscore the firm's interest in supporting the agency. Of course, the small-business, minority-owned, and women-owned firms should train their efforts on RFP responses regarding contracts required to be awarded entirely or in part to such a firm.

Request for Proposals

The most common, widely used method to monitor agency needs and new RFPs is the *Commerce Business Daily (CBD)*, a daily publication of the Commerce Department. (See Appendix 1.)

The *CBD* is a valuable reference that lists not only new solicitations but also contracts awarded and to whom. Notices in the *CBD* are organized by the subject of the contract work. Of particular interest for audit and management advisory services are the following categories:

- Experimental, developmental, test, and research work.
- Expert and consultant services.

The *Commerce Business Daily* will contain a brief synopsis of the type of services being purchased. This notice does *not* constitute a solicitation but does give instructions for how a firm can obtain an RFP or RFQ and indicates the office and name of the official to be contacted. Firms should make prompt arrangements to obtain a copy of the solicitation itself because

- The *CBD* synopsis may often be cryptic, incomplete, or misleading, and only the solicitation document contains an accurate description of the type of work being sought.
- Time deadlines are often short; by the time the agency submits the synopsis, the *CBD* publishes it, and the firm finally receives and reviews it, the response period will have shortened leaving some deadlines as little as a week away.
- Some agencies maintain only a limited stock of copies of the solicitations, which are sent to interested firms on a first-come, first-served basis.

A second technique for monitoring government RFPs is to have the firm placed on the bidders' mailing lists maintained by some federal agencies. Separate and apart from the *CBD*, some agencies will maintain an automatic mailing of solicitations to firms that have an interest in, or that regularly bid on, certain types of work. A list of contact points for bidders' mailing lists is shown in Appendix 4.

RFP Background

An RFP is issued at a relatively late stage in the process of an agency's formulating its requirements and beginning to seek competitive sources. Much work precedes issuance of a solicitation: for example, budget officials will have defined the allowable limits of contract support; program officials will have often spent many months in prescribing the scope of work to be sought; contracting officials will have made efforts to determine the competitive

approach to be used, the type of contract, and which socioeconomic programs and special-interest clauses will be applied.

Obviously, many of the decisions reflected in the RFP derive in some part from the expectations and experience of agency officials who have already dealt with particular firms for audit and management advisory services. The terms and conditions, whether stated inadvertently or not, can influence which firms might eventually enjoy certain advantages or disadvantages in formulating a response to the RFP. Generally, more detailed and precise RFP requirements indicate that there is a greater likelihood that, even inadvertently, one firm or another may find itself at a competitive advantage or disadvantage.

Thus, again, a firm should become as familiar as possible with the client's needs and working environment. The firms most successful in providing regular support for federal agencies develop this working knowledge in order to anticipate upcoming needs and fairly well gauge forthcoming requirements.

There are other things a firm can and should do to accurately analyze a particular RFP and the competitive situation that will determine a bid or no bid decision.

A firm can contact the same federal contracting agency for information on similar contracts already let and completed. The firm can review the public record of firms that have completed earlier, similar contracts, the prices quoted, and the rates for various skill categories accepted by the government.

A firm can also ask whether the RFP in question represents new work or whether it represents a periodic recompetition of ongoing work. If it is ongoing work, find out which firm is the current contractor and use this to gauge whether your firm can be reasonably expected to provide better support, more reasonable prices, or both. Try to assess whether the current contractor has been providing satisfactory service, and try to learn the reputation the firm has acquired among the agency officials. This, too, will provide important information on the likelihood of the firm's ability to compete successfully on the RFP. Further, discussion with agency officials may reveal essential needs that can be addressed specifically in the response.

Another point to be considered is whether the RFP has resulted from an unsolicited proposal from another firm. In some cases, a firm will make such an unsolicited offer if it feels it has discerned a serious agency requirement. In these circumstances, the agency's perception of the need, scope of work, and the type of qualifications being sought has already been colored by the original submission from the firm offering their services, and such a firm may have the advantage in submitting a response to the RFP.

Effective Proposals

A prerequisite for successful proposals is to provide ample time for their preparation. After obtaining the RFP, plan to assess the kinds of information described in the preceding section, and make an *early* commitment either to pursue or reject the RFP. Significant resources can be consumed in making the decision whether to bid, as well as the actual preparation of bids and proposals; therefore, a disciplined decision process is necessary.

Another important perspective that is generally more difficult for firms new to government contracting to understand is not to try to sell the government on the type of work that the firm wants to do but to show why the firm can best do the job *the government* wants done. Federal managers are quite able to appreciate what their program needs are and, in many specific areas, what will best meet those needs.

In this vein, not only the program officials but the contracting officials who are responsible for the integrity of the selection process will expect the firm to conform precisely to the terms and conditions of the solicitation. Take every provision of the RFP strictly and literally. Deviations, unless specifically requested, can be cause for disqualification because the proposal was “nonresponsive” to the conditions set down in the solicitation. This admonition applies even to such mundane conditions, as the maximum number of pages and page size of the response. This caveat, however, does not preclude submission of an alternative proposal in addition to one that is responsive to the RFP.

A firm may have the conviction that, given the opportunity, it could perform the work differently, more effectively and more economically, if some of the solicitation constraints or conditions were removed or altered. If the firm chooses to pursue this as an issue, it is usually best to make a formal, written inquiry to the agency, either independently or as part of the bidders’ conference sponsored by the agency. Question only the particular RFP provisions of concern to you. RFPs are amended frequently to correct mistakes, to add further clarifications, or to change conditions, especially proposal due dates; however, changing an RFP to alter constraints or conditions described by a single firm usually will not be done by an agency.

Typically, a proposal will be requested in two parts: the technical proposal and the cost proposal. While the requirements of the technical proposal will vary from contract to contract and from agency to agency, a broad pattern has emerged. Generally, the RFP will require discussion of the following items within the technical proposal:

1. Understanding of the problems and technical approach to be taken.
2. Qualifications and experience of the offeror's personnel.

The portion of the technical proposal dealing with exposition of the problem and discussion of the technical approach will frequently prove frustrating in that they both are self-evident in the statement-of-work portion of the RFP and in audit guides provided with the RFP (although not all RFPs provide such guides). The requirement for the offeror to present an understanding of the problem is a practice common to many types of procurement, not only audit and management services; it is intended to ensure that the government and the contractor have a mutual understanding of the work to be performed. While this requirement may appear innocuous, inappropriate, or, at best, marginally applicable to many proposals for audit and management advisory services, it should not be treated lightly. The government's review of technical proposals prior to award includes a determination of whether the proposal contains all of the items stipulated in the RFP. Indeed, in this specific area, many RFPs warn that a statement by the contractor that he will perform the effort set forth in the scope-of-work portion of the RFP will not suffice and will be regarded as nonresponsive.

When this portion of the technical proposal appears to be inadequately detailed in the RFP or its addenda, it may be appropriate to query the procuring agency. Generally, the RFP will contain the name of the contract specialist assigned to the RFP and a telephone number. Open discussion may reveal the principal focus of the problem and/or the technical approach.

The portion of the technical proposal dealing with qualifications and experience of the offeror's personnel may require or, in the absence of a specific requirement, be properly addressed by, reference to the experience of individual staff members or to the experience of the firm as a whole. Where the experience of the firm as a whole is not impressive in the type of efforts being proposed, it may be appropriate to build the technical proposal around the prior experience of a particular staff member. This approach is the logical extension of a technique discussed earlier; hiring new professionals who possess talents that can be used in responding to federal needs.

Regarding the cost proposal, much has already been said in chapter 5 on the issue of price versus qualification. Preparing the cost proposal and pricing the firm's services will be among the most difficult decisions.

Recognize that contracting with the federal government is often a highly competitive market, and frequently the firm will not be

able to win the award if it prices the work on the basis of full billing rates. The pricing decision is basically a marketing decision. The firm must determine the lowest rates for which it is willing to perform a high-quality, professional job and still achieve the financial objectives of the firm. Firms, of course, are motivated differently in this regard, depending on a variety of different circumstances such as the time of year the work is to be performed, availability of staff, other client commitments, the nature and amount of fixed expenses, experience to be acquired, effect on the firm's reputation, and its long-range objectives.

The type of contract (firm fixed-price, cost-plus-fixed-fee, time-and-materials, and so forth) envisioned in the RFP will influence how the firm sets its price, which may be different from the way firms bill other clients. For example, billing rates of various staff may be set forth, with estimated hours for each level, and the total price based on the sum of all staff billing proposed for the job. In other cases, billing rates supported by costs determined in accordance with federal procurement regulations and included on Government Standard Form 60 are required, which necessitates the development of estimated direct labor costs, indirect overhead cost rates, general and administrative rates, and profit rates. This type of cost display may not coincide with the firm's method of maintaining its accounting records, and some adjustment may be required as described herein in chapter 7 in the section titled "Internal Accounting Systems." In still other cases, the RFP may simply request a firm price to do the work, with minimum supporting detail regarding how such amount was determined. In any event, the firm's cost and price proposal is subject to review by government auditors, and therefore a working knowledge of appropriate government cost regulations as described in section 15 of the federal procurement regulations is required. (See Appendix 5 for pertinent excerpts of this section.) In this chapter, in the section entitled "Internal Accounting Systems," there is a list of more commonly unallowable costs applicable to this type of work.

Since the manner of determining proposed prices for government contracts may differ substantially from that used for other kinds of clients, the firm should closely review its methodology to determine amounts proposed to the government to be certain that such prices ensure the firm's objectives and that the methodology is consistent with the RFP and related government procurement regulations.

The firm's internal organizations can also enhance the ability to respond to RFPs and create effective proposals. Personnel and operating units should be regularly designated for participation

in the RFP process. Proposals should not be treated on an ad hoc basis. Plan in advance to designate proposal managers. Lay out the precise duties of various professional and administrative units and prepare the advice and input they will be expected to provide for government contract efforts. Try to focus authority and responsibility in a single person—a proposal manager—for each effort that merits the firm’s attention. Try to stabilize the personnel who will be involved regularly in work for particular agencies on a particular subject. Once again, the firm should concentrate on building a regular familiarity with the prospective federal clients.

The mechanics of effective proposal preparation is both an art and a science. Keep in mind that the proposal is, in the final analysis, a sales document designed to argue actively and persuasively the merits of the firm’s capabilities. Many specialized publications on the subject are available. The purpose of this book is not to provide in-depth instructions on proposal writing, but a few basic points are in order, with specific and intricate elaborations among the references listed in Appendix I, herein.

In writing the technical proposal, strive for simplicity and plainness. Complicated sentence structure, strings of buzz words, and gratuitous verbiage make unfavorable impressions on federal officials who go through the routine of proposal review dozens of times a year. Those officials will, however, be relieved by and impressed with a firm’s ability to make its point concisely and effectively and thereby demonstrate that it can provide the services the government is seeking. Similarly, elaborate illustrations, art work, bindings, and other frills will not compensate for an austere, tightly written, responsible proposal.

Relatively simple procedures can achieve this end as long as sufficient time is allotted for thorough preparation, editing, and rewriting. Firms will find that the first few proposals are quite difficult and time-consuming, but that experience yields significant improvement, since portions of earlier proposals can be incorporated with minor modification into later proposals.

Negotiations

Proposals and government evaluation will typically be divided into two parts: the technical proposal and the business or cost proposal. Each RFP will provide precise instructions for format and desired content of the two parts, each of which will generally stand on its own and be evaluated separately by different teams of government personnel.

In competitive negotiation situations, the RFP will give the firm some indication of the factors to be used in evaluation and the relative weightings assigned to each. In many cases, the agency may stipulate only general weightings; in others, such as the following example (figure 5), precise point scorings will be given.

Figure 5

TECHNICAL EVALUATION CRITERIA (Total 100 points)

Criteria	Numerical Weights
Proposed cost, offeror’s proposed hourly rates for each labor category.	45
Bidder’s management organization, showing technically qualified personnel at managerial and supervisory levels.	20
Qualification of individuals actually proposed to perform the audit.	20
Bidder’s past record in performing audits of this nature.	10
Bidder’s physical location relative to the audit site.	<u>5</u>
Total	<u><u>100</u></u>

Following submission and evaluation of proposals, the agency may choose to (1) simply select the winner and enter into final contract negotiations with that firm or, more commonly, (2) conduct additional written and oral discussions with all firms judged to be in the competitive range.

On the basis of their original proposals, some firms may be clearly judged as outside the competitive range and will not be asked to participate in discussions. This can happen, for example, if the technical proposal is seriously below par—even if the cost proposal appears to be the low bid.

All firms in the competitive range must receive equal treatment in these written and oral discussions, which are designed primarily to clarify uncertain points in the proposals and lead to the submission of a best and final offer to the government. For the most part, government policy is to discourage multiple rounds of best and final offers because it can lead to several undesirable results, such as technical leveling or transfusion of proposals. Ideas, approaches, and specific content in one proposal can be implied or inadvertently signaled from discussions with govern-

ment personnel who are familiar with all submissions. This undermines the integrity of the competitive process and can make government officials susceptible to charges that they have steered the award to one firm or another.

The government reserves the right to discontinue negotiations with one firm and open negotiations with the next most advantageous offeror if the negotiation process fails to accomplish what the government desires.

One other judgmental issue deserves mention. Some firms, in anticipation of an iterative negotiating process, make a relatively soft original proposal, with a view toward lowering the price or adding features during final negotiations. This is not always a good practice. Later discussions and negotiations to reach a “best and final offer” may, in fact, never take place if the firm is judged outside the competitive range or if the government simply proceeds to make an award on the strength of the original proposal submission. Therefore, this practice should be viewed as somewhat risky but not completely without merit when government negotiators later look for further adjustments.

In competitive negotiations for audit and management advisory services, even losing can be a valuable experience for the firm. After award, each firm that offered a proposal is entitled to a debriefing from the agency. The firm can inquire about the reason for the award and the relative evaluation standings of the proposal that won and the firm’s own proposal. This debriefing offers insight into the firm’s competitive weaknesses and strengths and whether they relate to personnel qualifications or to pricing. It will also reveal the perceived capabilities of the firm, that is, the attitudes and preferences of the agency clients. In general, the firm can gain accurate information needed to bid more successfully on future RFPs by examining its standing in the losing effort.

Protests

As is discussed in chapter 4, the General Accounting Office will hear bid protests. If the firm feels that any aspect of the competition—from the terms of the solicitations to the mechanics of submission and evaluation—were either constructed unfairly or conducted unfairly, the firm can file a written protest with the GAO either before or after the contract award. As a general rule, a firm should carefully consider whether it wants to take this action, since, in most cases, it will not be in the firm’s best interest to do so.

If the firm is concerned about unfair conditions or procedural violations, the best course is to inform the federal agency, and in so doing, avoid taking a harsh, adversary posture. A firm's professional posture, both in offering proposals and in performing audit and management advisory services, should be maintained since, in professional services work, the reputation that a firm gains as a cooperative, responsive contractor can weigh heavily in agency judgments. Performing audit and management advisory services requires an intimate, cooperative working relationship, one in which the firm shares the perspective and problems of the client.

As a practical matter, a protest to the General Accounting Office holds rather slim prospects for relief in any event. GAO rulings are not legally binding on the contract agency. Agencies rarely if ever terminate the contract and recompetitively award it as a result of protests filed after a contract is awarded even if the agency is found to have committed a violation.

A firm that feels a bid protest is in order should file with the GAO as early as possible in the contract process even before proposals are due for submission if the firm notes unfair competitive provisions in the RFP, for example. In this event, the GAO ruling process might be conducted in time to reach a decision before the agency has selected a firm and awarded the contract.

Beyond the GAO, the courts are not generally a good forum to pursue bid protests. They will typically require that the contractor have first exhausted all administrative remedies, including written requests to the contracting officials and GAO review. And, even when such appeals have been made and exhausted, the courts have typically been reluctant to intervene in any cases but those showing blatant bad faith on the part of the government or fraudulent behavior.

7 Supporting the Client

As an entity providing audit or management advisory services to the federal government, the firm is an integral part of a team providing needed public services and thus, as such, the firm should try to accommodate the everyday problems of the federal agency and the requirements of its contract.

Performance

The early stages of the contract, when attitudes are formed, are the most important in establishing good working relationships. Contract performance determines the firm's reputation and its future as a successful and regular contractor for the particular agency.

According to most evaluation standards, past performance ratings are not called out or applied, either explicitly or implicitly. However, the U.S. Air Force, in 1979, recognized that in many cases past performance was, in fact, an important source selection factor, and was so recognized if not so rated. As a result, the Air Force Systems Command has initiated a trial program whereby a contractor's past performance can be explicitly rated, either as a major source selection factor or as a generalized consideration.

Applying past performance standards leads to several complexities, such as some firms' having no past track records or cases of poor performance whose cause is unclear or attributable not to the firm but to the actions of the federal agency. Moreover, some argue that poor performance on one contract may have little or no relevance to future performance, or, in fact, that a contractor may be expected to improve as a result of past difficulties.

Whatever the merits of these arguments and whether or not the Air Force and other agencies decide to include past performance as an explicit source selection criterion, the main point remains: The caliber of a firm's contract support can and will have a major impact on future contract competitions and the firm's ability to sustain and expand its federal business base. Poor performance can even lead to contract cancellation with potentially severe financial exposures (see the section below titled "Terminations").

It is true that the government's own rules and regulations and its emphasis on open competition generally allow it less flexibility than a private client to select somewhat arbitrarily preferred sources for audit and management advisory services. But the firm should bear in mind the same principles that make contract performance among the most crucial considerations in obtaining and keeping private or public clients. Unlike formal advertising—sealed bids with awards to the low bidder—the government does retain considerably more discretion in competitive negotiated awards for professional services. Just as with private clients, the same people will be evaluating the firm's future proposals.

Other Deliverables

Contracts for audit or management advisory services generally culminate in delivery of reports on these services to the government. Such contracts customarily require delivery of other reports that are primarily administrative, dealing with such matters as the success or status of the effort or the extent of completion expressed in either (or both) financial terms or man hours (or some equivalent measure). While agency program representatives are primarily interested in the reports on audit or management advisory services, contract representatives view the administrative reports as equally important. Hence, such requirements warrant careful attention.

Other Clauses

The rules of federal contracting also contain many requirements not related directly to the contract work but rather to the achievement of critical social and economic goals for the country.

Among the important socioeconomic requirements in federal contracts are the following:

1. *Equal employment opportunity* prohibiting discrimination by federal contractors in their personnel practices.
2. *Fair labor standards* requiring contractor compliance with wage and hour standards in production of goods.
3. *Veterans hiring preferences* requiring contractors to list suitable job openings with state agencies to assist veterans.
4. *Labor surplus area preferences* allowing contractors to give preference for contracts set aside for areas of high unemployment, as measured quarterly by the Labor Department.

These and other socioeconomic requirements, including the small business subcontracting provision mentioned earlier in chapter 6, should not represent any major deterrent for firms seeking to provide audit and management advisory services.

Government contracts generally contain a preprinted set of general provisions, some of which are not germane to contracts for audit or management advisory services. Examples include those clauses dealing with patent rights, reporting or royalties, and the Buy American Act. Certain other clauses have only marginal applicability; others, however, have a direct relationship to the responsibilities and rights of the contractor, including clauses dealing with the following.

- The Truth in Negotiations Act (Pub. L. 87-653) permits the government to adjust the contract price if data contained in the offeror's proposal are subsequently found to be inaccurate or incomplete and the data were relied upon in developing the contract price.
- The limitation-of-cost clause places a ceiling on the government's commitment of funds but also limits the contractor's requirement to incur cost. This clause appears in cost-type contracts only, and the ceiling set by the contract can be increased, notwithstanding this clause, by an appropriate contract modification.
- The key personnel clause is designed to guarantee the participation of those key personnel offered in the proposal in contract performance.
- A consultants clause puts limits on the use of consultants on the contract and the rates paid to them.
- An allowable cost fixed-fee-and-payment clause is also re-

stricted to cost type contracts and, in addition to stipulating manner, form, and frequency of billing, incorporates by reference the provisions of an appropriate regulation (generally the Federal Procurement Regulations), which indicate principles applicable to determination of allowable costs and discuss in detail certain specific items of cost.

- A changes clause gives the contracting officer the unilateral right to make changes within the general scope of the contract but also provides for appropriate modifications in the contract price.

Prospective contractors should, if unfamiliar with the terms and conditions of government contracts, review the basic contract document that accompanies the RFP. A clear understanding of the contract at the outset will facilitate later day-to-day performance of it.

Payment for Services

For most audit and management advisory services performed under cost type contracts, the firm can expect to be reimbursed regularly and periodically for costs incurred, generally monthly, although some payments may be tied to specific contract milestones and deliverables. A portion of the fee earned will also be paid periodically, although it is common for the agency to retain a portion of the fee, with or without incentives, for payment only upon successful completion of the contract.

The firm can do several things to enhance the cash flow. First, it should discuss specific payment provisions when negotiating the final contract. In some cases, for good cause, the government will agree to adjusted payment schedules on a semimonthly basis or will adjust the schedule of deliverables versus payments.

Second, the firm should recognize that the contracting officer generally has broader flexibility to provide for accelerated payment schedules for small businesses.

Third, the government saves the taxpayers tens of millions of dollars each year by accepting and conforming to prompt payment discount offers by the contracting firm, although these are more common in contracts for equipment and supplies.

Internal Accounting Systems

The internal accounting system employed by the firm may require varying degrees of adaptation to ensure provision of the appropriate data required for government determination of contract

costs and reimbursements. The degree of adaptation will depend on the requirements set forth in the RFP, the type of contract specified therein, and the scope of preaward review of cost proposals.

Government agencies traditionally develop contract prices as a lump sum (firm fixed-price), rate per hour (labor hour or time-and-material contracts), or estimated cost plus profit allowance (cost plus fixed fee) in terms of cost (to the contractor) and profit. In service contracts, cost is, in turn, generally presented in terms of its constituent elements, which, by and large, are direct salaries and indirect expenses. Many accounting firms do not record costs in this fashion. Smaller firms, although extremely conscious of billable time (direct salaries), do not generally make a distinction between direct and indirect salaries on their own internal statements. Similarly, the accounting for other billable costs (for example, travel expenses) is frequently obscured. Rather than develop billable rates (prices) by use of the government's method (direct salaries plus indirect expenses plus profit), accounting firms generally employ a multiple of the average base hourly rates of the various staff classifications (for example, three times the average rate for seniors).

If the procurement contemplates a labor hour or time-and-material contract and does not require the submission of cost data, no adaption of the internal accounting system will be required. In such cases, the RFP will require a pricing summary such as the example that follows.

Figure 6

Category	Estimated		
	Rate	Hours	Amount
Partner	\$ _____	450	\$ _____
Supervisor and/or manager	\$ _____	1,350	\$ _____
Senior and/or in-charge accountant	\$ _____	3,600	\$ _____
Junior and/or assistant accountant or staff assistant	\$ _____	3,600	\$ _____
Estimated Travel			\$27,000.00
Total			\$ _____

Alternately, if the procurement contemplates the same type of contract but requires submission of cost data, the offeror must express his costs in terms of direct salaries, indirect expenses, and

profit. Since billings and reimbursement will be accomplished through a fixed rate per hour rather than recorded costs, it is not necessary to revamp the internal accounting system to produce such data. The cost elements proposed should, however, be rooted in, or at least reconcilable with, current operating statements. The direct salary rates can be developed quite readily, and, since they are intended to represent the actual salaries to be incurred during the period of performance contemplated by the RFP, they can be estimated by reference to wage rates that are current at the time the proposal is prepared and adjusted for known or anticipated increments that will be in effect during the period of performance.

Unless the accounting firm differentiates between direct and indirect expenses on its internal statements, the development of indirect expenses applicable to the proposal, or, perhaps more accurately, the development of an indirect expense rate, is somewhat more complex.

Under government contracts for services, indirect expenses are customarily expressed in terms of a percentage of direct salaries, since such contracts are labor intensive. To develop such a percentage (indirect expense rate), the data contained in current operating statements must first be allocated between direct and indirect expenses. As mentioned earlier, commingling of direct and indirect expenses occurs most commonly in salaries and such other potentially billable costs as travel.

For purposes of developing cost data to support proposed prices, estimates can be used to segregate direct from indirect costs. If the firm maintains records of billable time expressed in terms of a percentage of total time, this percentage can be applied to total salaries to develop an imputed amount of direct salaries. If such data are kept by staff classification, and total salaries by classification are either recorded or readily available, all the better. If data related to billable time are not accumulated, the estimation can be based on an appropriate sampling. Caution should be exercised, however, to level the effects of seasonal swings in billable time ratios.

A similar approach that uses either readily available actual costs or estimates can be used to allocate costs other than salaries between direct (billable) and indirect categories.

This exercise will result in a restatement of a current operating statement between direct and indirect costs, which may take the general form illustrated in figure 7.

Since these data are taken from a current operating statement, they must, of course, be adjusted to reflect levels of costs and expenses that are expected to prevail during the period of performance contemplated by the contract.

Figure 7

Direct costs	
Salaries	
Travel	
Other	\$ _____
Total direct costs	\$ _____
Indirect expenses	
Indirect salaries	
Fringe benefits	
Travel	
Other	_____
Total indirect expenses	\$ _____

It should be noted that certain costs, although regarded as indirect by the accounting firm, may not necessarily be considered acceptable by the government. The costs of an in-house computer, for example, may not be considered allocable to government work if (1) the computer is not used on the government work and (2) it is used primarily for client accounting.

If the procurement contemplates a cost-plus-fixed-fee contract, it will be necessary to adapt the internal accounting system to provide not only for formal segregation of direct and indirect costs but also for accumulation of costs under this contract, since reimbursement will be made on the basis of actual costs.

Contract cost principles fairly well follow generally accepted accounting principles and practices, and the normal costs of doing business are typically allowed. There are, however, several notable exceptions of which the firm should be aware. The following costs need to be segregated because they are generally *not* allowable under government work:

- Advertising.
- Bad debts.
- Compensation to owners of closely held corporations beyond reasonable amounts for actual services rendered.
- Entertainment expenses.
- Interest and other financial carrying costs.
- Unreasonable rental costs between related organizations from rent or sale/leaseback arrangements.
- Contributions and donations.

In general, however, contract cost principles do follow generally accepted practice and reasonableness as determinable by comparable costs that a prudent person in competitive business would otherwise incur.

Contract Modifications

Few subjects are more important than contract modifications for the firm providing audit and management advisory services. The very nature of the work, and the reason these contracts cannot be handled on a formal advertising basis, is that flexibility and change are to be expected as findings are made, new avenues are presented, and government needs are modified. As discussed throughout this book, the firm becomes part of a problem-solving team whose new discoveries and new information can lead to additional or redirected work effort.

Obviously, changes in the original scope of work can present hazards to both the firm and the government clients. Pitfalls include misunderstandings from loosely shared agreements and disagreements over allowable payments.

In virtually all cases, the firm and the government should record any significant modifications in work scope. Additional work performed without the formal direction of the program officials and approval of the contracting officials can later be designated unauthorized and, therefore, not reimbursable.

The distinction made between the program or technical officials and the contracting officials is especially important in this regard. As described in chapter 4, herein, the contracting officials are the expert mechanics who maintain the contractual relationship. Unless they are involved in, and formally register, contract modifications, program officials and the firm can find themselves at odds later on over what work, precisely, was authorized and subject to reimbursement beyond the original contract.

Contract modifications also present the government with sensitive problems. For audit and management advisory services, it is usually clear when modifications are needed to prosecute the original scope of work. Audited organizations may be found to have seriously deficient recordkeeping in a particular area, or in-depth analysis may be required beyond that anticipated. In management advisory services, a crucial management information system design may have to accommodate changes in agency operating procedures or facilities.

For the government manager, most such modifications are typical and essential. Some, however, can be of such a substantial

nature—varying so widely from the original scope of work—that the government may need to consider whether the new work should be subject to a separate RFP and selection process. Considerable criticism has been levied at contracts that in the end balloon to several times the original estimated value or expand to cover a scope of work clearly not that originally prescribed in the RFP. In such cases, both the agency and the firm become susceptible to charges of improperly turning a competitive award into a de facto sole-source award through the contract modification route.

Neither the firm nor the government agency is well served by such inordinate contract modifications. True, a firm with a small contract may enjoy a severalfold increase in effort, but this can disrupt the firm's ability to plan, control, and commit necessary resources. The government, too, should not be placed in the posture of conducting considerably more contract work than was originally budgeted and planned for.

For all these reasons, both the firm and the government client should design flexibility into the original scope of work to accommodate contingencies. Whenever possible, options for added increments of effort should be incorporated in the original contract negotiation.

When additional contract modifications are needed, follow the simple cardinal rule: Do not initiate unilateral changes; do not accept informal changes—get it down in writing from the contracting officer.

Contract Claims and Disputes

In the event severe disagreement arises between the contractor and the government over performance of the contract, there are a series of remedies and appeals that either party can pursue for fair adjudication.

As part of the overall, ongoing reform process to streamline and simplify the federal acquisition process, landmark legislation was passed in 1978 to provide a uniform and well-paced set of procedures. The Contract Disputes Act of 1978 (Pub.L. 95-563) lays down the parties' rights and the procedures to be followed in the event of contract disputes and is implemented through regulations issued by the Office of Federal Procurement Policy in OFPP Policy Letter 80-3. (See Appendix 1.)

In simple terms, the firm can appeal what it considers unfair reimbursement—claims against the government—through several different forums: the agency contracting officer, the agency board of contract appeals, and the Court of Claims.

The starting point in all cases is the agency contracting officer. The firm must submit its claim in writing and, notably, must continue to perform diligently under the original terms of the contract while any appeals are pending. For claims totaling less than \$50,000, the contracting officer must issue a written decision within sixty days. For claims over \$50,000, the firm must legally certify the validity of its claim and all supporting data, and the contracting officer must, within sixty days, notify the firm of the date that a final decision will be forthcoming.

In the event of undue delay on the part of the contracting officer, the firm may ask the agency's board of contract appeals to set a time limit. Should the contracting officer fail to meet this time deadline, that action is considered a denial of the claim, and the firm may proceed to other appeal forums. No matter what the contracting officer's written determination, any facts presented are reviewable in the later appeals.

After the contracting officer issues a written determination—or fails to do so within the period prescribed by the agency board—the firm may follow one of two appeal courses: the agency board of contract appeals or directly to the U.S. Court of Claims.

In the event that the firm elects to pursue the appeal within the agency board, the claim must be filed within ninety days of the contracting officer's decision. These boards are required by law to conduct the reviews in a semijudicial forum informally, expeditiously, and as inexpensively as possible. The boards are granted, however, full powers to administer oaths to witnesses, issue subpoenas for persons or books and records, and authorize depositions and discovery proceedings.

To bring a claim before the board of contract appeals, the firm may elect an accelerated small claims procedure if the amount in dispute is less than \$10,000. If the firm so chooses, the board must then render a written decision within 120 days, whenever possible; but the decision is then final and not further reviewable by the courts.

Similarly, if the amount in question is less than \$50,000, the firm can also elect an accelerated procedure targeted for resolution within 180 days. Again, however, the board's decision is then considered final, unless the firm is prepared to allege outright fraud in either case.

Whether or not the firm decides to appeal to the agency board, an appeal can be brought before the U.S. Court of Claims. If the firm seeks this higher appeal after a board ruling, it must do so within 120 days after the board's decision. In this case, any board findings on matters of law are reviewable again by the courts. However, the courts will take board findings of fact as final unless

the firm is prepared to demonstrate that they are clearly “fraudulent, arbitrary, capricious or so grossly erroneous as to necessarily imply bad faith, or if such decision is not supported by substantial evidence.”

In other words, if the firm elects to go to the agency board of contract appeals first, it cannot expect to get a completely new trial in the courts. Matters of fact from the board’s proceedings will be accepted basically by the court.

If the firm elects to bypass the agency board and go directly to court, it must decide to do so and file within twelve months of the contracting officer’s decision. In this case, obviously, the case will proceed *de novo*.

The law stipulates that if a firm finds its claim upheld, the government must pay not only the claim but interest accruing from the date of the original filing with the contracting officer.

Bear in mind that the agency may also appeal a decision of the board of contract appeals if it feels the finding in favor of the firm is inequitable. To do so, however, requires the prior approval of the attorney general.

What all these provisions mean to a firm is that, first, there are fair and methodical procedures available to pursue claims in a number of forums, and second, especially for small businesses and small claims, there is every opportunity to dispense with these claims promptly.

Nevertheless, the firm should exercise discretion in deciding to formally file and pursue claims against the government. In many cases, the decision to do so will be materially clear, based on the circumstances and the financial sums involved. In most cases, however, the firm should take into account the time- and resource-consuming appeals process, as well as the adversary posture the firm and the client will have to adopt. The firm should look on the legally available claims procedures as truly a last resort, not as a typical or frequently used norm within the federal acquisition process.

If the firm does find itself in the position of pursuing a claim beyond the contracting officer, the key choice is whether to move sequentially through the agency board of contract appeals or to go directly to the Court of Claims. The merits of either approach are debatable. No blanket advice can or should be given since the particular content and circumstances of each claim will dictate the course and whether, for example, the firm would prefer *de novo* proceedings in a court or would be satisfied to have agency board findings of fact fundamentally accepted at a later time.

In any event, it is important to point out that the agency boards of contract appeals are *not* literally agency organizations. Firms

should not feel that they will receive anything less than a full and impartial hearing on their claims just because the board is affiliated with the contracting agency. In fact, the Contract Disputes Act also upgrades the stature and authorities of the boards; the act makes them clearly independent, as evidenced by the fact that the government agency is also now given the right to appeal decisions of its own board to the courts.

As a general matter, the firm, in considering which route to take, might want to look ahead to the possible outcomes. If the claim is of such material or financial importance that an adverse board decision would nevertheless warrant pursuing the claim to court, perhaps the firm would want to consider going there directly. Other factors related to timing, preparation of documents and supporting materials, and continued performance under the contract also have to be weighed, of course.

Terminations

The contract can be concluded by other means than simply completing the required scope of work and receiving final payment. The government also reserves the right to terminate the contract at any point for one of two basic reasons.

1. *Termination for default* can be initiated if the government judges that the contractor has failed to perform satisfactorily according to contract terms. The implications of termination for default are much greater for fixed-price contracts than for cost type contracts. Normally, best efforts are required in cost type contracts, and the contractor must be negligent before default termination is imposed. Failure to perform the terms of a fixed-price contract carries with it more serious risks than the other. Although historically this has been a relatively rare event, which is usually triggered only after repeated notifications and failure to compensate for late deliverables or other contract terms, the consequences of defaulted termination are enormous. A termination for default entitles the government to recoup from the contractor any extra costs that it might incur from the failure to perform, including costs related to finding an alternative source to perform the remaining work and for differences in prices paid in excess of prices included in the defaulted contract.
2. *Termination for convenience of the government* can be instituted for a variety of reasons that have nothing to do with the

contractor's performance but that stem from changes in the agency's budget, program status, or policy changes. In these cases, also rare, the contractor is entitled to full reimbursement for all costs incurred on completed work and incurred in anticipation of the remainder unless a loss on the contract is anticipated.

Concluding Perspectives

Regardless of the encouragement offered herein, an uninitiated firm may feel somewhat uncomfortable with the rigors of the federal marketplace.

The scope of subject matter, admittedly, is broad. But, having read through the contract and negotiation descriptions and digested the advice, firms should be aware that contracting with the federal government for audit and management advisory services is not difficult. The fundamentals are fairly straightforward, and much of the advice on the "how to" of contracting clearly differs little from sound business practice with private clients.

Taken altogether, the federal acquisition process is important to all of us: It represents one of the truly unique features of American government and the American economy. In no other country is there a system as well developed to harness private talents to meet public needs.

Firms performing federal contracts can expect to see continued modernization of the acquisition process. Antiquated and conflicting statutes are being rewritten; the regulatory mass is being converted and rewritten into the single Federal Acquisition Regulation (FAR) system; and the Office of Federal Procurement Policy has had its statutory charter renewed to continue reform initiatives from the Executive Office of the President.

Throughout these ongoing improvements, the future of the federal contract system will continue to depend, for its health and public acceptability, on the ethics and attitudes that private firms and federal contract officials bring to their work. Federal contract managers and firms alike should serve the public need with enthusiasm and join in constantly seeking to bring still further improvement to that service.

Appendixes

Relevant Publications

Topic	Reference	Acquisition Instructions
Regulatory Materials	<ul style="list-style-type: none"> • <i>Federal Register</i> (Washington, D.C.: Office of the Federal Register, National Archives and Records Service, General Services Administration). <p>The <i>Federal Register</i>, a daily publication, provides a uniform system for making available to the public regulations and legal notices issued by federal agencies. These include presidential proclamations, executive orders, and federal agency documents having general applicability and legal effect, documents required to be published by acts of Congress, and other federal agency documents of public interest.</p>	<p>Superintendent of Documents U.S. Government Printing Office Washington, D.C. 20402</p> <p>Price: \$75.00 per year \$1.00 single copy</p>
	<ul style="list-style-type: none"> • <i>Code of Federal Regulations</i> (Washington, D.C.: Office of the Federal Register, National Archives and Records Service, General Services Administration). <p>The <i>Code of Federal Regulations (CFR)</i> is an annually revised codification of the final rules published in the daily <i>Federal Register</i>.</p>	<p>Superintendent of Documents U.S. Government Printing Office Washington, D.C. 20402</p> <p>Price: \$450 per year (Price of individual copies varies)</p>
	<ul style="list-style-type: none"> • <i>Federal Acquisition Regulation (FAR)</i> (Proposed) (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget). <p>The FAR will be a single, uniform acquisition regulation for use by all federal executive agencies in the acquisition of supplies and services with appropriated funds. The FAR is designed to consolidate and replace the Defense Acquisition Regulation (DAR), the Federal Procurement Regulations (FPR) and the National Aeronautics and</p>	<p>Assistant Administrator for Regulations Office of Federal Procurement Policy 726 Jackson Place, N.W., Room 9025 Washington, D.C. 20503</p>

Space Administration Procurement Regulations (NASA PR). The final FAR will be issued in the *Code of Federal Regulations* as Chapter 1 of Title 41, Public Contracts and Property Management.

- *Federal Procurement Regulations* (FPR) (Washington, D.C.: Office of Federal Management Policy, General Services Administration).

The FPR is the basic acquisition regulation for most non-Department of Defense agencies. The FPR is updated annually and published in Title 32 of the *Code of Federal Regulations*.

- *Defense Acquisition Regulations* (DAR) (Washington, D.C.: DAR Council, Department of Defense).

The DAR is the acquisition regulation for the Department of Defense and is updated and published in Title 41 of the *Code of Federal Regulations*.

- *NASA Procurement Regulations* (NASA PR) (Washington, D.C.: Director of Procurement, National Aeronautics and Space Administration).

The NASA PR is the acquisition regulation for the National Aeronautics and Space Administration and is updated and published in Title 41 of the *Code of Federal Regulations*.

- OMB Circular A-76, Revised, *Policies for Acquiring Commercial or Industrial Products and Services Needed by the Government* (Washington, D.C.: Office of Management and Budget, March 29, 1979).

This circular establishes the policies and procedures used to determine whether commercial or industrial goods and services needed by the government should be done by contract with private sources or in-house using government facilities and personnel.

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Relevant Publications (continued)

Topic	Reference	Acquisition Instructions
Regulatory Materials (continued)	<p>• OMB Circular A-102, <i>Uniform Administrative Requirements for Grants-in-Aid to State and Local Governments</i>, September 12, 1977; Attachment O, Revised, <i>Standards Governing State and Local Grantee Procurement</i>, August 15, 1979; Attachment P, Revised, <i>Audit Requirements</i>, September 3, 1980 (Washington, D.C.: Office of Management and Budget).</p> <p>OMB Circular A-102 establishes uniform financial and administrative requirements for grants to state and local governments. Attachment O provides standards for use by grantees in establishing procedures for the procurement of goods and services with federal grant funds. Attachment P establishes audit requirements for state and local governments and Indian tribal governments that receive federal assistance. The requirements are established to insure that audits are made on an organization-wide basis, rather than on a grant-by-grant basis.</p>	<p>Office of Administration Publications Unit Room G-236 New Executive Office Building Washington, D.C. 20503</p>
	<p>• OMB Circular A-120, <i>Guidelines for the Use of Consulting Services</i>, (Washington, D.C.: Office of Management and Budget, April 14, 1980).</p> <p>This circular establishes policy and guidelines to be followed by executive branch agencies in determining and controlling the appropriate use of consulting services obtained from individuals and organizations.</p>	<p>Office of Administration Publications Unit Room G-236 New Executive Office Building Washington, D.C. 20503</p>
	<p>• OFPP Policy Letter 78-2, <i>Preventing "Wage Busting" for Professionals: Procedures for Evaluating Contractor Proposals for Service Contracts</i> (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget, March 29, 1978).</p> <p>This policy directive sets forth the requirement (and related evaluation factors and criteria) that all service employees, including professional employees, employed by contractors providing services to the U.S. government be fairly and properly compensated.</p>	<p>Office of Federal Procurement Policy Office of Management and Budget New Executive Office Building Washington, D.C. 20503</p>

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• OFPP Policy Letter 80-2, *Subcontracting Under Federal Contracts* (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget, June 1, 1980).

This policy directive sets forth amendments to be made to the FPR, DAR, and NASA PR in implementation of Section 211 (subcontracting under federal contracts) of Pub. L. 95-507, amendments to the Small Business Act, and the Small Business Investment Act of 1958.

• OFPP Policy Letter 80-3, *Final Contract Disputes Regulatory Coverage and Contract Disputes Clause* (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget, June 1, 1980).

This policy directive sets forth amendments to be made to the FPR, DAR, and NASA PR relating to contract disputes regulatory coverage and the contract dispute clause, as required by Pub. L. 95-563, The Contract Disputes Act of 1978.

• OFPP Policy Letter 80-4, *Subcontracting With Women's Business Enterprises Under Federal Contracts* (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget, June 1, 1980).

This policy directive sets forth amendments to be made to the FPR, DAR, and NASA PR relating to subcontracting with women's business enterprises under federal contracts.

• *The Congressional Record* (Washington, D.C.: Superintendent of Documents, Government Printing Office).

The *Congressional Record* is the public proceedings for each House of Congress and is published for each day that one or both Houses are in session. It includes recorded votes, debates on the floors of the House and Senate, committee meetings, and hearings, speeches, and articles inserted by members of Congress.

Legislative Materials

Relevant Publications (continued)

Topic	Reference	Acquisition Instructions
Legislative Materials (continued)	<ul style="list-style-type: none"> • Congressional Documents: Bills, committee reports, and public laws are available by writing to the House and Senate Documents Rooms. Committee documents, including legislative calendars, hearings, and committee reports are available by writing to the pertinent committee. 	<ul style="list-style-type: none"> House Documents Room United States Capitol Washington, D.C. 20515 Senate Documents Room United States Capitol Washington, D.C. 20510 House Committee name U.S. House of Representatives Washington, D.C. 20515 Senate Committee name U.S. Senate Washington, D.C. 20510
Government Information Centers	<ul style="list-style-type: none"> • Federal Acquisition Institute (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget). The Federal Acquisition Institute (FAI) maintains a library of acquisition literature, including books, research papers, conference proceedings, textbooks, journal articles and congressional documents. Anyone may use the library. FAI also publishes a quarterly newsletter which summarizes FAI activities and accomplishments and selected acquisition readings. • Federal Procurement Data Center (Washington, D.C.: Department of Defense, Washington Headquarters Service). Pursuant to the requirements of Pub. L. 93-400, the Federal Procurement Data Center (FPDC) was established in 1978 to operate a Federal Procurement Data System (FPDS) "for collecting, developing, and disseminating procurement data which takes into account the needs of the Congress, the executive branch, and the private sector." Departments and agencies report to the FPDC uniform acquisition 	<ul style="list-style-type: none"> Federal Acquisition Institute Office of Federal Procurement Policy Office of Management and Budget 1815 North Lynn Street Rosslyn, Virginia 22209 Federal Procurement Data Center 1815 North Lynn Street Suite 320 Rosslyn, Virginia 22209

information used for geographical and market analyses and as indicators of congressional and presidential initiatives in a number of socioeconomic areas such as small business, minority business enterprises, and other disadvantaged businesses. Basic procurement data is published for each quarter of the fiscal year in the *Quarterly Report of Federal Contract Awards* and accumulated in the *Annual Report of Federal Contract Awards*.

Relevant
Government
Publications

- *Catalog of Federal Domestic Assistance* (Washington, D.C.: Office of Management and Budget).

The catalog provides users with access to virtually all federal department and agency programs. Program information is cross-referenced by agency, functional classification, subject, eligible applicants, popular name, authorizing legislation, and federal circular requirements. Other sections of the catalog provide users with information on the administrative requirements of federal circulars, definitions of the types of assistance under which programs are administered, proposal writing and grant application procedures, and additional sources of information on federal programs and services. The catalog is published annually, generally in May, and updated in September and December.

- *Commerce Business Daily* (Washington, D.C.: U.S. Department of Commerce).

The *Commerce Business Daily (CBD)* provides a daily list of U.S. government procurement invitations, contract awards, subcontracting leads, sales of surplus property, and foreign business opportunities.

- *Financial Management of Federal Assistance Programs* (Washington, D.C.: Office of Management and Budget, February 1980).

This booklet provides a brief overview of the OMB circulars that establish uniform policies and rules to be observed by all executive branch agencies with regard to the financial aspects of federal aid programs.

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Relevant Publications (continued)

Topic	Reference	Acquisition Instructions
<p>Relevant Government Publications (continued)</p>	<p>• <i>A Guide to Resources and Sources of Information for Acquisition Research</i> (Fort Lee, Virginia: Army Procurement Research Office, Department of Defense, January 1980).</p> <p>The guide is a comprehensive listing of organizations that provide acquisition research and sources of information available on acquisition topics. The array of information sources includes historical and background materials, data bases, bibliographies and indexes, reporters and periodicals, legal references, statistical data, government sources and associations, and advisory organizations. The guide is an excellent source of information for anyone interested in acquisition topics.</p>	<p>Superintendent of Documents U.S. Government Printing Office Washington, D.C. 20402</p> <p>Price: \$1.75 Stock No. 041-001-00193-0</p>
<p>• <i>Report of the Commission on Government Procurement</i> (Washington, D.C.: Commission on Government Procurement, December 1972).</p> <p>The Commission on Government Procurement was created by Pub. L. 91-129 in November 1969 to study and recommend to Congress methods to promote the economy, efficiency, and effectiveness of procurement by the executive branch of the federal government. During two and one-half years of study, the Commission on Government Procurement formulated 149 specific recommendations for improving executive branch procurement. These recommendations are presented in this report, which consists of ten parts in four volumes, a volume devoted to an index, bibliography, a list of acronyms, and a summary report.</p>	<p>Superintendent of Documents U.S. Government Printing Office Washington, D.C. 20402</p> <p>Price: Volume 1—\$2.60 Stock No.—5255-00002 Volume 2— 2.60 Stock No.—5255-00003 Volume 3— 2.60 Stock No.—5255-00004 Volume 4— 2.85 Stock No.—5255-00006 Index, etc.—2.10 Stock No.—5255-00007 Summary— 1.25 Stock No.—5255-00005</p>	
<p>• <i>Report to the Congress: Proposal for a Uniform Procurement System</i> (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget, October 1980).</p> <p>This proposal was submitted to Congress in accordance with the requirements set forth in Pub. L. 96-83. The proposed uniform</p>	<p>Superintendent of Documents U.S. Government Printing Office Washington, D.C. 20402</p> <p>Price: \$5.50 Stock No. 041-001-00216-2</p>	

procurement system (UPS) is designed to "simplify procurement regulations and upgrade the qualifications of federal procurement personnel through personnel training and accountability." The system has five principal elements: a hierarchy of directives, the fundamental or generic procurement process, management and management support components, data systems, and personnel programs. In addition to these elements, the system will encompass the policies addressed in the 149 recommendations of the Commission on Government Procurement.

- *Report to the Congress on the Commission on Government Procurement Recommendations* (Washington, D.C.: Office of Federal Procurement Policy, Office of Management and Budget, October, 1980).

This report summarizes the status of the 149 recommendations made by the Commission on Government Procurement.

- *Federal Contracts Report* (Washington, D.C.: Bureau of National Affairs, Inc.).

This weekly report provides information on a wide range of topics relating to government contracts and grants. It includes summaries of current contracting issues, pertinent news items, court and administrative decisions and rulings, proposed or enacted legislation, and texts of related speeches and statements.

- *The Government Contractor* (Washington, D.C.: Federal Publications, Inc.).

This biweekly periodical reports and analyzes significant government contracts rulings and regulations issued by the courts, boards, comptroller general, procuring agencies, and Congress.

- *Government Contracts Reporter* (Chicago, Illinois: Commerce Clearing House, Inc.).

This reporter is a nine-volume loose-leaf reporting service on federal acquisition topics. The volumes contain annotated explanatory

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Relevant Publications (continued)

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<p>Reporters Periodicals, and Other Relevant Publications (continued)</p>	<p>comments, texts of regulations and statutes, new developments, and related indexes and finding lists. Weekly reports are provided, which include summaries of new developments in federal acquisition and updated pages to be inserted into the volumes. Full texts of acquisition regulations, in addition to the DAR and FPR, include those from the following departments and agencies: Army, Defense Logistics Agency, Air Force, Energy, Transportation, Navy, General Services Administration, and the National Aeronautics and Space Administration.</p> <ul style="list-style-type: none"> • <i>Guidelines for CPA Participation in Government Audit Engagements to Evaluate Economy, Efficiency, and Program Results</i>, Management Advisory Services, Guideline Series no. 6 (New York: American Institute of Certified Public Accountants, 1977). <p>This guide examines the various MAS skills that may be needed when undertaking a government audit in accordance with GAO standards. It explains steps involved in responding to a request for proposal (RFP) and presents techniques, checklists, and illustrations for developing programs.</p> <ul style="list-style-type: none"> • <i>Guidelines for Preparation of Requests for Audit Proposals, Discussion Draft</i> (San Francisco: Western Intergovernmental Audit Forum, October 1980). <p>These guidelines have been prepared to establish a reasonable degree of consistency in the form and content of requests for proposals (RFPs) issued by local governments and audit proposals prepared in response to these requests.</p> <ul style="list-style-type: none"> • <i>Model Procurement Code for State and Local Governments</i> (Washington, D.C.: American Bar Association, Model Procurement Code Project, February, 1979). <p>The American Bar Association <i>Model Procurement Code for State and Local Governments</i> provides "(1) the statutory principles and policy</p>	<p>American Institute of Certified Public Accountants Order Department 1211 Avenue of the Americas New York, New York 10036 Price: \$5.50</p>
	<ul style="list-style-type: none"> • <i>Executive Director</i> Western Intergovernmental Audit Forum Suite 900 1275 Market Street San Francisco, California 94103 	<p>American Bar Association Model Procurement Code Project Suite 200, South Tower 1800 M Street, N.W. Washington, D.C. 20036</p>

guidance for managing and controlling the procurement of supplies, services, and construction for public purposes; (2) administrative and judicial remedies for the resolution of controversies relating to public contracts; and (3) a set of ethical standards governing public and private participants in the procurement process." The code is a culmination of extensive study by state and local purchasing officers, organizations interested in procurement, and members of the legal profession, directed by the ABA Coordinating Committee on a Model Procurement Code. Several state and local governments have adopted the code, and others are considering its provisions.

• Tierney, Cornelius E.; Hoffman, Robert D.; *Federal Financial Management: Accounting and Auditing Practices* (New York: American Institute of Certified Public Accountants, 1976).

This book explains in detail how the government budgets, plans, accounts for, and audits federal funds. It outlines the techniques and procedures followed in federal financial management and auditing and describes how agency financial functions are organized. It also discusses the subject of accounting and auditing of government contracts and grants.

• Tierney, Cornelius E.; *Federal Grants-In-Aid: Accounting and Auditing Practices* (New York: American Institute of Certified Public Accountants, 1977).

This book brings together in a single reference the general accounting and auditing criteria that most governmental grantors require. The author describes the federal grant process in detail and discusses requirements for the management of grant programs, internal accounting, and accounting and auditing.

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Cost Accounting Standards

The following cost accounting standards have been issued:

- 400—Definitions
- 401—Consistency in Estimating, Accumulating and Reporting Costs
- 402—Consistency in Allocating Costs Incurred for the Same Purpose
- 403—Allocation of Home Office Expenses to Segments
- 404—Capitalization of Tangible Assets
- 405—Accounting for Unallowable Costs
- 406—Cost Accounting Period
- 407—Use of Standard Costs for Direct Material and Direct Labor
- 408—Accounting for Costs of Compensated Personal Absence
- 409—Depreciation of Tangible Capital Assets
- 410—Allocation of Business Unit General and Administrative Expense to Final Cost Objectives
- 411—Accounting for Acquisition Cost of Material
- 412—Cost Accounting Standards for Composition and Measurement of Pension Costs
- 413—Adjustment and Allocation of Pension Cost
- 414—Cost of Money as an Element of the Cost of Facilities Capital
- 415—Accounting for the Cost of Deferred Compensation
- 416—Accounting for Insurance Costs
- 417—Cost of Money as an Element of the Cost of Capital Assets Under Construction
- 418—Allocation of Direct and Indirect Costs
- 420—Accounting for Independent-Research-and-Development Costs and Bid-and-Proposal Costs

The following extracts are reproduced from the Code of Federal Regulations, title 4—“Accounts,” chapter III—“Cost Accounting Standards Board,” parts 401 and 402.

Part 401—Cost Accounting Standard—Consistency in Estimating, Accumulating and Reporting Costs

§ 401.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board’s regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

§ 401.20 Purpose.

The purpose of this Cost Accounting Standard is to insure that each contractor's practices used in estimating costs for a proposal are consistent with cost accounting practices used by him in accumulating and reporting costs. Consistency in the application of cost accounting practices is necessary to enhance the likelihood that comparable transactions are treated alike. With respect to individual contracts, the consistent application of cost accounting practices will facilitate the preparation of reliable cost estimates used in pricing a proposal and their comparison with the costs of performance of the resulting contract. Such comparisons provide one important basis for financial control over costs during contract performance and aid in establishing accountability for costs in the manner agreed to by both parties at the time of contracting. The comparisons also provide an improved basis for evaluating estimating capabilities.

§ 401.30 Definitions.

(a) The following definitions of terms which are prominent in this standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in subparagraph (b) of this paragraph.

(1) *Accumulating Costs.* The collecting of cost data in an organized manner, such as through a system of accounts.

(2) *Actual cost.* An amount determined on the basis of cost incurred as distinguished from forecasted cost. Includes standard cost properly adjusted for applicable variance.

(3) *Estimating Costs.* The process of forecasting a future result in terms of cost, based upon information available at the time.

(4) *Indirect cost pool.* A grouping of incurred costs identified with two or more objectives but not identified specifically with any final cost objective.

(5) *Pricing.* The process of establishing the amount or amounts to be paid in return for goods or services.

(6) *Proposal.* Any offer or other submission used as a basis for pricing a contract, contract modification or termination settlement or for securing payments thereunder.

(7) *Reporting Costs.* Provision of cost information to others.

The reporting of costs involves selecting relevant cost data and presenting it in an intelligible manner for use by the recipient.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this standard: None.

§ 401.40 Fundamental requirement.

(a) A contractor's practices used in estimating costs in pricing a proposal shall be consistent with his cost accounting practices used in accumulating and reporting costs.

(b) A contractor's cost accounting practices used in accumulating and reporting actual costs for a contract shall be consistent with his practices used in estimating costs in pricing the related proposal.

(c) The grouping of homogeneous costs in estimates prepared for proposal purposes shall not per se be deemed an inconsistent application of cost accounting practices under paragraphs (a) and (b) of this section when such costs are accumulated and reported in greater detail on an actual cost basis during contract performance.

§ 401.50 Techniques for application.

(a) The standard allows grouping of homogeneous costs in order to cover those cases where it is not practicable to estimate contract costs by individual cost element or function. However, costs estimated for proposal purposes shall be presented in such a manner and in such detail that any significant cost can be compared with the actual cost accumulated and reported therefor. In any event the cost accounting practices used in estimating costs in pricing a proposal and in accumulating and reporting costs on the resulting contract shall be consistent with respect to: (1) The classification of elements or functions of cost as direct or indirect; (2) the indirect cost pools to which each element or function of cost is charged or proposed to be charged; and (3) the methods of allocating indirect costs to the contract.

(b) Adherence to the requirement of § 401.40(a) of this standard shall be determined as of the date of award of the contract, unless the contractor has submitted cost or pricing data pursuant to Public Law 87-653, in which case adherence to the requirement of § 401.40(a) shall be determined as of the date of final agreement on price, as shown on the signed certificate of current cost or pricing data. Notwithstanding § 401.40(b), changes in established cost accounting practices during contract performance may be made when authorized by standards, rules, and regulations issued by the Cost Accounting Standards Board.

§ 401.60 Illustrations.

(a) The following examples are illustrative of applications of cost accounting practices which are deemed to be consistent.

Practices used in estimating costs for proposals

1. Contractor estimates an average direct labor rate for manufacturing direct labor by labor category or function.
2. Contractor estimates an average cost for minor standard hardware items, including nuts, bolts, washers, etc.
3. Contractor uses an estimated rate for manufacturing overhead to be applied to an estimated direct labor base. He identifies the items included in his estimate of manufacturing overhead and provides supporting data for the estimated direct labor base.

Practices used in accumulating and reporting costs of contract performance

1. Contractor records manufacturing direct labor based on actual cost for each individual and collects such costs by labor category or function.

2. Contractor records actual cost for minor standard hardware items based upon invoices or material transfer slips.
3. Contractor accounts for manufacturing overhead by individual items of cost which are accumulated in a cost pool allocated to final cost objectives on a direct labor base.

(b) The following examples are illustrative of application of cost accounting practices which are deemed not to be consistent.

Practices used for estimating costs for proposals

4. Contractor estimates a total dollar amount for engineering labor which includes disparate and significant elements or functions of engineering labor. Contractor does not provide supporting data reconciling this amount to the estimates for the same engineering labor cost functions for which he will separately account in contract performance.
5. Contractor estimates engineering labor by cost function, i.e., drafting, production engineering, etc.
6. Contractor estimates a single dollar amount for machining cost to cover labor, material and overhead.

Practices used in accumulating and reporting costs of contract performance

4. Contractor accounts for engineering labor by cost function, i.e., drafting, designing, production engineering, etc.
5. Contractor accumulates total engineering labor in one undifferentiated account.
6. Contractor records separately the actual cost of machining labor and material as direct costs, and factory overhead as indirect costs.

§ 401.70 Exemptions.

None for this standard.

§ 401.80 Effective date.

July 1, 1972.

Appendix—Interpretation No. 1

Part 401, Cost Accounting Standard, Consistency in Estimating, Accumulating and Reporting Costs, requires in § 401.40 that a contractor's "practices used in estimating costs in pricing a proposal shall be consistent with his cost accounting practices used in accumulating and reporting costs."

In estimating the cost of direct material requirements for a contract, it is a common practice to first estimate the cost of the actual quantities to be incorporated in end items. Provisions are then made for additional direct material costs to cover expected material losses such as those which occur, for example, when items are scrapped, fail to meet specifications, are lost, consumed in the manufacturing process, or destroyed in testing and qualification processes. The cost of some or all

of such additional direct material requirements is often estimated by the application of one or more percentage factors to the total cost of basic direct material requirements or to some other base.

Questions have arisen as to whether the accumulation of direct material costs in an undifferentiated account where a contractor estimates a significant part of such costs by means of percentage factors is in compliance with Part 401. The most serious questions pertain to such percentage factors which are not supported by the contractor with accounting, statistical, or other relevant data from past experience, nor by a program to accumulate actual costs for comparison with such percentage estimates. In the opinion of the Board the accumulation of direct costs in an undifferentiated account in this circumstance is a cost accounting practice which is not consistent with the practice of estimating a significant part of costs by means of percentage factors. This situation is virtually identical with that described in Illustration 401.60(b)(5), which deals with labor.

Part 401 does not, however, prescribe the amount of detail required in accumulating and reporting costs. The Board recognizes that the amount of detail required may vary considerably depending on the percentage factors used, the data presented in justification or lack thereof, and the significance of each situation. Accordingly, the Board is of the view that it is neither appropriate nor practical for the Board to prescribe a single set of accounting practices which would be consistent in all situations with the practices of estimating direct material costs by percentage factors. The Board considers, therefore, that the amount of accounting and statistical detail to be required and maintained in accounting for this portion of direct material costs has been and continues to be a matter to be decided by Government procurement authorities on the basis of the individual facts and circumstances.

Part 402—Cost Accounting Standard—Consistency in Allocating Costs Incurred for the Same Purpose

§ 402.10 General applicability.

General applicability of this cost accounting standard is established by § 331.30 of the Board's regulations on applicability, exemption, and waiver of the requirement to include the cost accounting standards contract clause in negotiated defense prime contracts and subcontracts (§ 331.30 of this chapter).

§ 402.20 Purpose.

The purpose of this standard is to require that each type of cost is allocated only once and on only one basis to any contract or other cost objective. The criteria for determining the allocation of costs to a product, contract, or other cost objective should be the same for all similar objectives. Adherence to these cost accounting concepts is necessary to guard against the overcharging of some cost objectives and to prevent double counting. Double counting occurs most commonly

when cost items are allocated directly to a cost objective without eliminating like cost items from indirect cost pools which are allocated to that cost objective.

§ 402.30 Definitions.

(a) The following definitions of terms which are prominent in this standard are reprinted from Part 400 of this chapter for convenience. Other terms which are used in this standard and are defined in Part 400 of this chapter have the meanings ascribed to them in that part unless the text demands a different definition or the definition is modified in paragraph (b) of this section.

(1) *Allocate*. To assign an item of cost, or a group of items of cost, to one or more cost objectives. This term includes both direct assignment of cost and the reassignment of a share from an indirect cost pool.

(2) *Cost objective*. A function, organizational subdivision contract or other work unit for which cost data are desired and for which provision is made to accumulate and measure the cost to processes, products, jobs, capitalized projects, etc.

(3) *Direct Cost*. Any cost which is identified specifically with a particular final cost objective. Direct costs are not limited to items which are incorporated in the end product as material or labor. Costs identified specifically with a contract are direct costs of that contract. All costs identified specifically with other final cost objectives of the contractor are direct costs of those cost objectives.

(4) *Final Cost Objective*. A cost objective which has allocated to it both direct and indirect costs, and, in the contractor's accumulation system, is one of the final accumulation points.

(5) *Indirect Cost*. Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.

(6) *Indirect cost pool*. A grouping of incurred costs identified with two or more cost objectives but not identified specifically with any final cost objective.

(b) The following modifications of definitions set forth in Part 400 of this chapter are applicable to this standard: None.

§ 402.40 Fundamental Requirement.

All costs incurred for the same purpose, in like circumstances, are either direct costs only or indirect costs only with respect to final cost objectives. No final cost objective shall have allocated to it as an indirect cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included as a direct cost of that or any other final cost objective. Further, no final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective.

§ 402.50 Techniques for application.

(a) The Fundamental Requirement is stated in terms of cost incurred and is equally applicable to estimates of costs to be incurred as used in contract proposals.

(b) The Disclosure Statement to be submitted by the contractor will require that he set forth his cost accounting practices with regard to the distinction between direct and indirect costs. In addition, for those types of cost which are sometimes accounted for as direct and sometimes accounted for as indirect, the contractor will set forth in his Disclosure Statement the specific criteria and circumstances for making such distinctions. In essence, the Disclosure Statement submitted by the contractor, by distinguishing between direct and indirect costs, and by describing the criteria and circumstances for allocating those items which are sometimes direct and sometimes indirect, will be determinative as to whether or not costs are incurred for the same purpose. Disclosure Statement as used herein refers to the statement required to be submitted by contractors as a condition of contracting as set forth in Part 351 of this chapter.

(c) In the event that a contractor has not submitted a Disclosure Statement the determination of whether specific costs are directly allocable to contracts shall be based upon the contractor's cost accounting practices used at the time of contract proposal.

(d) Whenever costs which serve the same purpose cannot equitably be indirectly allocated to one or more final cost objectives in accordance with the contractor's disclosed accounting practices, the contractor may either: (1) Use a method for reassigning all such costs which would provide an equitable distribution to all final cost objectives, or (2) directly assign all such costs to final cost objectives with which they are specifically identified. In the event the contractor decides to make a change for either purpose the Disclosure Statement shall be amended to reflect the revised accounting practices involved.

(e) Any direct cost of minor dollar amount may be treated as an indirect cost for reasons of practicality where the accounting treatment for such cost is consistently applied to all final cost objectives, provided that such treatment produces results which are substantially the same as the results which would have been obtained if such cost had been treated as a direct cost.

§ 402.60 Illustrations.

(a) Illustrations of costs which are incurred for the same purpose:

(1) Contractor normally allocates all travel as an indirect cost and previously disclosed this accounting practice to the Government. For purposes of a new proposal, contractor intends to allocate the travel costs of personnel whose time is accounted for as direct labor directly to the contract. Since travel costs of personnel whose time is accounted for as direct labor working on other contracts are costs which are

incurred for the same purpose, these costs may no longer be included within indirect cost pools for purposes of allocation to any covered Government contract. Contractor's Disclosure Statement must be amended for the proposed changes in accounting practices.

(2) Contractor normally allocates planning costs indirectly and allocates this cost to all contracts on the basis of direct labor. A proposal for a new contract requires a disproportionate amount of planning costs. The contractor prefers to continue to allocate planning costs indirectly. In order to equitably allocate the total planning costs, the contractor may use a method for allocating all such costs which would provide an equitable distribution to all final cost objectives. For example, he may use the number of planning documents processed rather than his former allocation base of direct labor. Contractor's Disclosure Statement must be amended for the proposed changes in accounting practices.

(b) Illustrations of costs which are not incurred for the same purpose:

(1) Contractor normally allocates special tooling costs directly to contracts. The costs of general purpose tooling are normally included in the indirect cost pool which is allocated to contracts. Both of these accounting practices were previously disclosed to the Government. Since both types of costs involved were not incurred for the same purpose in accordance with the criteria set forth in the contractor's Disclosure Statement, the allocation of general purpose tooling costs from the indirect cost pool to the contract, in addition to the directly allocated special tooling costs is not considered a violation of the standard.

(2) Contractor proposes to perform a contract which will require three firemen on 24-hour duty at a fixed-post to provide protection against damage to highly inflammable materials used on the contract. Contractor presently has a fire fighting force of 10 employees for general protection of the plant. Contractor's costs for these latter firemen are treated as indirect costs and allocated to all contracts; however, he wants to allocate the three fixed-post firemen directly to the particular contract requiring them and also allocate a portion of the cost of the general firefighting force to the same contract. He may do so but only on condition that his disclosed practices indicate that the costs of the separate classes of firemen serve different purposes and that it is his practice to allocate the general firefighting force indirectly and to allocate fixed-post firemen directly.

§ 402.70 Exemption.

None for this standard.

§ 402.80 Effective date.

July 1, 1972.

Appendix—Interpretation No. 1

Part 402, Cost Accounting Standard, Consistency in Allocating Costs Incurred for the Same Purpose, provides, in Section 402.40, that *** no final cost objective shall have allocated to it as a direct cost any

cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective.”

This interpretation deals with the way Part 402 applies to the treatment of costs incurred in preparing, submitting, and supporting proposals. In essence, it is addressed to whether or not, under the Standard, all such costs are incurred for the same purpose, in like circumstances.

Under Part 402, costs incurred in preparing, submitting, and supporting proposals pursuant to a specific requirement of an existing contract are considered to have been incurred in different circumstances from the circumstances under which costs are incurred in preparing proposals which do not result from such specific requirement. The circumstances are different because the costs of preparing proposals specifically required by the provisions of an existing contract relate only to that contract while other proposal costs relate to all work of the contractor.

This interpretation does not preclude the allocation, as indirect costs, of costs incurred in preparing all proposals. The cost accounting practices used by the contractor, however, must be followed consistently and the method used to reallocate such costs, of course, must provide an equitable distribution to all final cost objectives.

Small Business Administration Field Offices

Region	City	State	Zip Code	Address	Telephone
I	Boston	Mass. ¹	02110	60 Battery March Street, 10th Floor	(617) 223-2100
	Boston	Mass. ²	02114	150 Causeway St., 10th Floor	(617) 223-2100
	Holyoke	Mass. ³	01050	302 High Street, 4th Floor	(413) 536-8770
	Augusta	Maine ²	04330	40 Western Avenue, Room 512	(207) 622-6171
	Concord	N. H. ²	03301	55 Pleasant Street, Room 211	(603) 224-4041
	Montpelier	Vt. ²	05602	87 State Street, Room 204, P.O. Box 605	(802) 229-0538
	Providence	R. I. ²	02903	57 Eddy Street, 7th Floor	(401) 528-4580
	Hartford	Conn. ²	06103	One Financial Plaza	(203) 244-3600
	New York	N. Y. ¹	10007	26 Federal Plaza, Room 29-118	(212) 264-7772
	New York	N. Y. ²	10007	26 Federal Plaza, Room 3100	(212) 264-4355
	Melville	N. Y. ³	11747	401 Broad Hollow Road, Suite 322	(516) 752-1626
Syracuse	N. Y. ²	13260	100 South Clinton Street, Room 1071	(315) 423-5383	
Buffalo	N. Y. ⁴	14202	111 West Huron St., Room 1311	(716) 846-4301	
Elmira	N. Y. ⁴	14901	180 State Street, Room 412	(607) 733-4686	
Albany	N. Y. ³	12210	99 Washington Ave., Room 301-Mezzanine	(518) 472-6300	
Rochester	N. Y. ³	14614	100 State Street, Room 601	(716) 263-6700	
Newark	N. J. ²	07102	970 Broad St., Room 1635	(201) 645-2434	
Camden	N. J. ³	08104	1800 East Davis Street	(609) 757-5183	
Hato Rey	P. R. ²	00918	Chardon and Bolivia Streets, P.O. Box 1915	(809) 753-4572	
St. Thomas	V. I. ³	00801	Veterans Drive, Room 283	(809) 774-8530	
Philadelphia (Bala Cynwyd)	Pa. ¹	19004	231 St. Asaphs Rd., Suite 646-West Lobby	(215) 597-3311	
Philadelphia (Bala Cynwyd)	Pa. ²	19004	231 St. Asaphs Rd., Suite 400-East Lobby	(215) 597-3311	

III	Harrisburg	Pa. ⁴	17101	100 Chestnut Street, 3rd Floor	(717) 782-3840
	Wilkes-Barre	Pa. ⁴	18702	20 North Pennsylvania Avenue	(717) 826-6497
	Pittsburgh	Pa. ²	15222	1000 Liberty Ave., Room 1401	(412) 644-2780
	Wilmington	Del. ⁴	19801	844 King Street, Room 5207	(302) 573-6294
	Baltimore	Md. ²	21204	8600 LaSalle Road, Room 630	(301) 962-4392
	Clarksburg	W. Va. ²	26301	109 North 3rd St., Room 301	(304) 623-5631
	Charleston	W. Va. ⁴	25301	Charleston National Plaza, Suite 628	(304) 343-6181
	Richmond	Va. ²	23240	400 North 8th St., Room 3015, P.O. Box 10126	(804) 782-2617
	Washington	D. C. ²	20417	1030 15th St., N.W., Suite 250	(202) 655-4000
	IV	Atlanta	Ga. ¹	30309	1375 Peachtree St., N.E., 5th Floor
Atlanta		Ga. ²	30309	1720 Peachtree Street, N.W., 6th Floor	(404) 881-4325
Birmingham		Ala. ²	35205	908 South 20th St., Room 202	(205) 254-1344
Charlotte		N. C. ²	28202	230 S. Tryon Street, Suite 700	(704) 371-6111
Greenville		N. C. ³	27834	215 South Evans Street, Room 206	(919) 752-3798
Columbia		S. C. ²	29201	1835 Assembly Street, 3rd Floor	(803) 765-5376
Jackson		Miss. ²	39201	100 West Capitol Street, Suite 322	(601) 969-4371
Biloxi		Miss. ⁴	39530	111 Fred Haise Blvd., 2nd Floor	(601) 435-3676
Jacksonville		Fla. ²	32202	400 West Bay St., Room 261, P.O. Box 35067	(904) 791-3782
Miami		Fla. ²	33134	2222 Ponce De Leon Boulevard, 5th Floor	(305) 350-5521
(Coral Gables)					
Tampa		Fla. ³	33602	700 Twiggs Street, Suite 607	(813) 228-2594
West Palm Beach		Fla. ³	33402	701 Clematis St., Room 229	(305) 659-7533
Nashville		Tenn. ²	37219	404 James Robertson Parkway, Suite 1012	(615) 251-5881
Knoxville		Tenn. ⁴	37902	502 South Gay St., Room 307	(615) 637-9300
Memphis		Tenn. ³	38103	167 North Main St., Room 211	(901) 521-3588
Louisville		Ky. ²	40201	600 Federal Pl., Room 188, P.O. Box 3517	(502) 582-5971
Chicago		Ill. ¹	60604	219 South Dearborn St., Room 838	(312) 353-0355
Chicago		Ill. ²	60604	219 South Dearborn St., Room 437	(312) 353-4528
Springfield	Ill. ⁴	62701	One North, Old State Capital Plaza	(217) 525-4416	
Indianapolis	Ind. ²	46204	575 North Pennsylvania St., Room 552	(317) 269-7272	
Cleveland	Ohio ²	44199	1240 East 9th St., Room 317	(216) 522-4180	
Columbus	Ohio ²	43215	85 Marconi Boulevard	(614) 469-6860	
Cincinnati	Ohio ⁴	45202	550 Main St., Room 5028	(513) 684-2814	
Detroit	Mich. ²	48226	477 Michigan Ave.	(313) 226-6075	
Marquette	Mich. ⁴	49855	540 W. Kaye Avenue	(906) 225-1108	
V					

SBA Field Offices (continued)

Region	City	State	Zip Code	Address	Telephone
V	Madison	Wis. ²	53703	212 East Washington Ave., Room 213	(608) 264-5261
	Milwaukee	Wis. ⁴	53202	517 East Wisconsin Avenue, Room 246	(414) 291-3941
	Eau Claire	Wis. ³	54701	500 South Barstow St., Room B9AA	(715) 834-9012
	Minneapolis	Minn. ²	55402	12 South 6th St.	(612) 725-2362
	Dallas	Tex. ¹	75235	1720 Regal Row, Room 230	(214) 767-7643
	Dallas	Tex. ²	75242	1100 Commerce St., Room 3C36	(214) 767-0605
	Marshall	Tex. ³	75670	100 South Washington Street, Room G-12	(214) 935-5257
	Houston	Tex. ²	77002	500 Dallas Street	(713) 226-4341
	Lubbock	Tex. ²	79401	1205 Texas Avenue, Room 712	(806) 762-7466
	El Paso	Tex. ⁴	79902	4100 Rio Bravo, Suite 300	(915) 543-7586
VI	Lower Rio Grande Valley (Harlingen)	Tex. ²	78550	222 East Van Buren Street, P.O. Box 2567	(512) 423-4534
	San Antonio	Tex. ²	78206	727 East Durango Street, Room A-513	(512) 229-6250
	Austin	Tex. ²	78701	300 East 8th Street	(512) 397-5288
	Corpus Christi	Tex. ⁴	78408	3105 Leopard Street, P.O. Box 9253	(512) 888-3331
	Little Rock	Ark. ²	72201	611 Gaines Street, Suite 900	(501) 378-5871
	New Orleans	La. ²	70113	1001 Howard Avenue, 17th Floor	(504) 589-6685
	Shreveport	La. ³	71101	500 Fannin Street, Room 5B06	(318) 226-5196
	Oklahoma City	Okla. ²	73102	200 N.W. 5th Street, Suite 670	(405) 231-4301
	Tulsa	Okla. ³	74119	616 South Boston Street	(918) 581-7462
	Albuquerque	N. M. ²	87110	500 Marble Avenue, N.E., Room 320	(505) 766-3430
VII	Kansas City	Mo. ¹	64106	911 Walnut St., 23rd Floor	(816) 374-5288
	Kansas City	Mo. ²	64106	1150 Grande Ave., 5th Floor	(816) 374-3416
	St. Louis	Mo. ²	63101	One Mercantile Center, Suite 2500	(314) 425-4191
	Des Moines	Iowa ²	50309	210 Walnut St., Room 749	(515) 284-4422
	Omaha	Neb. ²	68102	19th & Farnum St., 2nd Floor	(402) 221-4691
Wichita	Kans. ²	67202	110 East Waterman Street	(316) 267-6571	
VIII	Denver	Colo. ¹	80202	1405 Curtis Street, 22nd Floor	(303) 837-5763
	Denver	Colo. ²	80202	721 19th Street	(303) 837-2607
	Salt Lake City	Utah ²	84138	125 South State St., Room 2237	(314) 425-5800
	Casper	Wyo. ²	82602	100 East B Street, Room 4001, P.O. Box 2839	(307) 265-5266
	Helena	Mont. ²	59601	301 South Park Avenue, Room 528, Drawer 10054	(406) 449-5381

Fargo	N. D. ²	58108	657 2nd Ave., North, Room 218, P.O. Box 3086	(701) 237-5771
Stoux Falls	S. D. ²	57102	101 South Main Ave., Suite 101	(605) 336-2980
Rapid City	S. D. ⁴	57701	515 9th St., Room 246	(605) 343-5074
San Francisco	Calif. ¹	94102	450 Golden Gate Ave., P.O. Box 36044	(415) 556-7487
San Francisco	Calif. ²	94105	211 Main Street, 4th Floor	(415) 556-7490
Oakland	Calif. ³	94612	1515 Clay Street	(415) 273-7790
San Diego	Calif. ²	92188	880 Front Street, Room 4-S-29	(714) 293-5440
Fresno	Calif. ⁴	93712	1229 "N" St., P.O. Box 828	(209) 487-5189
Sacramento	Calif. ³	95825	2800 Cottage Way, Room 2535	(916) 484-4726
Los Angeles	Calif. ²	90071	350 S. Figueroa St., 6th Floor	(213) 688-2956
Phoenix	Ariz. ²	85012	3030 North Central Avenue, Suite 1201	(602) 261-3611
Tucson	Ariz. ³	85715	301 West Congress Street, Room 3V	(602) 625-1063
Las Vegas	Nev. ²	89101	301 E. Stewart, P.O. Box 7525, Downtown Station	(702) 385-6611
Reno	Nev. ³	89505	50 South Virginia St., Room 308, P.O. Box 3216	(702) 784-5268
Honolulu	Hawaii ²	96850	300 Ala Moana, Room 2213, P.O. Box 50207	*(808) 546-8950
Agana	Guam ⁴	96910	Pacific Daily News Bldg., Room 508	*(671) 477-8420
Seattle	Wash. ¹	98104	710 2nd Ave., 5th Floor	(206) 442-5676
Seattle	Wash. ²	98174	915 Second Ave., Room 1744	(206) 442-5534
Spokane	Wash. ²	99210	West 920 Riverside Avenue, Room 651, P.O. Box 2167	(509) 456-5310
Boise	Idaho ²	83701	1005 Main St., 2nd Floor	(208) 384-1096
Portland	Oregon ²	97204	1220 S.W. Third Avenue, Room 676	(503) 221-2682
Anchorage	Alaska ²	99501	1016 West 6th Ave., Suite 200	*(907) 271-4022
Fairbanks	Alaska ⁴	99701	101 12th Avenue, Box 14	*(907) 452-1951

* Operator assistance may be needed in some areas.

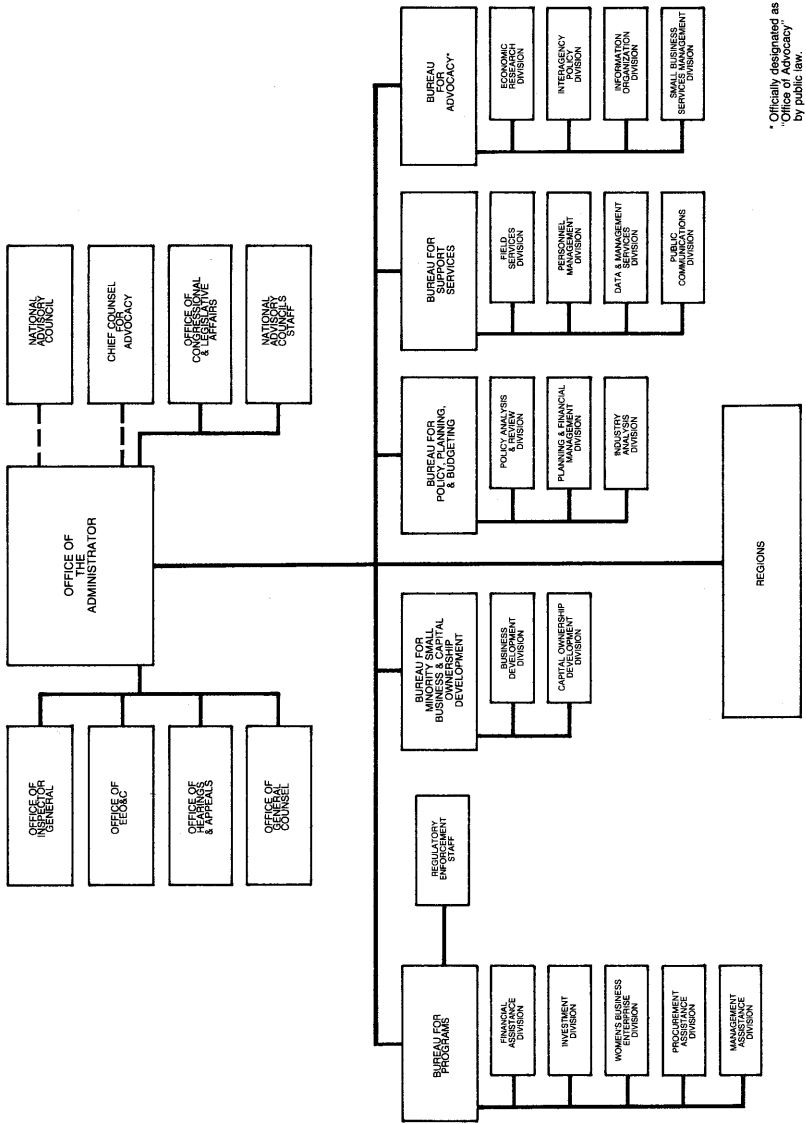
1. Regional office.

2. District office.

3. Post of duty.

4. Branch office.

SMALL BUSINESS ADMINISTRATION



* Officially designated as "Office of Advocacy" by public law.

APPENDIX 4

Contact Points for Agency Bidder's Lists

Federal agencies purchase goods and services on a centralized or decentralized basis. Decentralized purchases are made primarily through an agency's procurement field offices; centralized purchases are generally made through the procurement division of an agency's Washington office.

Almost every federal agency maintains a bidders' mailing list of potential suppliers for various goods and services. Following is a list of contact points from which you can obtain detailed information about an agency's various bidders' mailing lists.

U.S. Department of Agriculture
Office of Operations and Finance
Procurement Division (Policy Unit)
Room 1575
South Building
14th & Independence Avenue, S.W.
Washington, D.C. 20250

U.S. Department of Commerce
Procurement Policy Division
Room 6511
14th & Constitution Avenue, N.W.
Washington, D.C. 20230

Community Services Administration
Procurement Division
Room 418
1200 19th Street, N.W.
Washington, D.C. 20506

U.S. Department of Defense
Directorate for Small Business and Economic Utilization Policy
Deputy Under-Secretary of Defense for Research and Engineering
(Acquisition Policy)
Room 2A340
The Pentagon
Washington, D.C. 20301

U.S. Department of Energy
Office of Procurement Operation
PR 331—Stop 1J009
Forrestal Building
1000 Independence Avenue, S.W.
Washington, D.C. 20314

Environmental Protection Agency
Director, Procurement and Contracts
Management Division (PM—214)
401 M Street, S.W.
Washington, D.C. 20460

Federal Trade Commission
Office of Procurement and Contracts
6th & Pennsylvania Avenue, N.W.
Washington, D.C. 20580

U.S. Department of Health and Human Services
Office of Grants and Procurement
Office of Assistant Secretary for Management and Budget
Room 513D
Hubert H. Humphrey Building
200 Independence Avenue, S.W.
Washington, D.C. 20201

U.S. Department of Housing and Urban Development
Office of Procurement and Contracts
Room B-133
451 7th Street, S.W.
Washington, D.C. 20410

U.S. Department of the Interior
Division of Procurement and Grants
Office of Administration and Management Policy
18th & C Streets, N.W.
Washington, D.C. 20240

U.S. Department of Justice
Procurement Management Group
Justice Management Division
10th & Constitution Avenue, N.W.
Washington, D.C. 20530

U.S. Department of Labor
Office of Assistant Secretary for Administration and Management
Office of Comptroller
Office of Grants and Procurement Policy
200 Constitution Avenue, N.W.
Washington, D.C. 20210

National Aeronautics and Space Administration
Director Small and Disadvantaged Business Utilization
600 Independence Avenue, S.W.
Washington, D.C 20546

Small Business Administration
Purchasing and Contracting Office
1441 L Street, N.W.
Washington, D.C. 20416

U.S. Department of Transportation
Office of Installations and Logistics
400 7th Street, S.W.
Washington, D.C. 20590

U.S. Department of the Treasury
Office of Procurement
Room 900
1331 G Street, N.W.
Washington, D.C. 20220

Veterans Administration
Director, Supply Service
810 Vermont Avenue, N.W.
Washington, D.C. 20420

Pertinent Excerpts From The Federal Procurement Regulations

These excerpts are from the CCH series, Government Contract Reporter (Chicago: CCH). Section 15, in its entirety, can be found in the Government Contract Reporter at paragraphs 66,706 through 66,759.60.

Part 1-15—Contract Cost Principles and Procedures

§ 1-15.000 Scope of part.

This part contains general cost principles and procedures for the negotiation and administration of fixed-price, cost-reimbursement, and other types of contracts, the pricing of contracts and contract modifications whenever cost analysis is performed (see § 1-3.807-2), and the determination, negotiation, or allowance of costs when such action is required by a contract clause.

Subpart 1-15.1—Applicability

§ 1-15.101 Scope of subpart.

This subpart describes the applicability of succeeding subparts of this part to the various types of contracts in connection with which cost principles and procedures are used, and the need for advance understandings.

§ 1-15.102. Negotiated supply, service, experimental, developmental, and research contracts, and contract changes with concerns other than educational institutions.

This category includes all contracts and contract modifications for supplies, services, or experimental, developmental, or research work negotiated on the basis of cost with concerns other than educational institutions (see § 1-15.103) and State and local governments (see § 1-15.108). It does not include facilities contracts (see § 1-15.105) or construction and architect-engineer contracts (see § 1-15.104). Except with respect to the cost principles and procedures in §§ 1-15.201-4,

Definition of allocability; 1-15.205-3, Bidding costs; 1-15.205-6, Compensation for personal services; 1-15.205-26, Patent costs; and 1-15.205-35, Research and development costs, the use of which are optional, the remaining cost principles and procedures set forth in Subpart 1-15.2 are prescribed for mandatory use and shall be (a) used in the pricing of negotiated supply, service, experimental, developmental, and research contracts and contract modifications with concerns other than educational institutions whenever cost analysis is to be performed pursuant to § 1-3.807-2, and (b) incorporated (by reference, if desired) in such contracts as the basis:

(1) For determination of reimbursable costs under cost-reimbursement type contracts (§ 1-3.405), including cost-reimbursement type subcontracts thereunder, and the cost-reimbursement portion of time-and-materials contracts (§ 1-3.406-1) except in such contracts where material is priced on a basis other than at cost in accordance with § 1-3.406-1(d);

(2) For the negotiation of overhead rates (Subpart 1-3.7);

(3) For claiming, negotiating, or determining costs under terminated fixed-price and cost-reimbursement type contracts (§§ 1-8.203 and 1-8.213);

(4) For the price revision of fixed-price incentive contracts (§ 1-3.404-4);

(5) For price redetermination of prospective and retroactive price redetermination contracts (§§ 1-3.404-5 and 1-3.404-7); and

(6) For pricing changes and other contract modifications (§ 1-7.102-20).

§ 1-15.103 Contracts with educational institutions.

(a) This category includes all contracts and contract modifications for experimental, developmental, or research work with educational institutions. The cost principles and procedures set forth in Subpart 1-15.3 shall be incorporated (by reference, if desired) in cost-reimbursement research contracts with educational institutions as the basis:

(1) For determination of reimbursable costs under cost-reimbursement type contracts, including cost-reimbursement type subcontracts thereunder;

(2) For the negotiation of overhead rates (Subpart 1-3.7); and

(3) For the determination of costs of terminated cost-reimbursement type contracts where the contractor elects to "voucher out" his costs (Subpart 1-8.4) and for settlement of such contracts by determination (§ 1-8.209-7).

(b) In addition, Subpart 1-15.3 is to be used in determining the allowable costs of research and development performed by educational institutions under grants, and as a guide in the evaluation of costs in connection with the negotiation of fixed-price type contracts and termination settlements.

§ 1-15.104 Construction and architect-engineer contracts.

This category includes all contracts for construction and contracts for architect-engineer services related to such construction, as defined in § 1-15.401. Subject to the exceptions stated in § 1-15.102, the cost

principles and procedures set forth in Subpart 1-15.4 are prescribed for mandatory use and shall be (a) used in the pricing of negotiated construction and architect-engineer contracts and contract modifications whenever cost analysis is to be performed pursuant to § 1-3.807-2, and (b) incorporated (by reference, if desired) in cost-reimbursement and fixed-price type construction and architect-engineer contracts as the basis:

(1) For the determination of reimbursable costs under cost-reimbursement type contracts, including cost-reimbursement type contracts thereunder (§ 1-3.405);

(2) For the negotiation of overhead rates (Subpart 1-3.7);

(3) For claiming, negotiating, or determining costs under terminated fixed-price and cost-reimbursement type contracts (§§ 1-8.203 and 1-8.213);

(4) For the price revision of fixed-price incentive contracts (§ 1.3.404-4); and

(5) For pricing changes and other contract modifications (§ 1-7.102-20).

§ 1-15.105 Facilities contracts.

Subpart 1-15.5 contains principles and procedures for the evaluation and determination of costs under facilities contracts, as defined in § 1-15.501, and subcontracts thereunder. Subject to the exceptions stated in § 1-15.102, such principles and procedures are prescribed for mandatory use and shall be incorporated (by reference, if desired) in facilities contracts as the basis—

(a) For determination of reimbursable costs under facilities contracts, including cost-reimbursement type subcontracts thereunder;

(b) For the negotiation of overhead rates (see Subpart 1-3.7); and

(c) For the determination of costs of terminated cost-reimbursement type contracts during the period invoices or vouchers are submitted in accordance with § 1-8.402, and for settlement of such contracts by determination (see § 1-8.209-7).

§ 1-15.106 Fixed-price type contracts.

This Part 1-15 shall be used in the pricing of fixed-price type contracts and contract modifications whenever cost analysis is performed. It also will be used whenever a fixed-price type contract clause requires the determination or negotiation of costs. However, application of these cost principles to fixed-price type contracts shall not be construed as a requirement to negotiate agreements on individual elements of cost in arriving at agreement on the total price. The final price accepted by the parties reflects agreement only on the total price. Further, notwithstanding the mandatory use of these cost principles (except as stated in § 1-15.102), the objective will continue to be to negotiate prices that are fair and reasonable, cost and other factors considered.

§ 1-15.107 Advance understandings on particular cost items.

(a) The extent of allowability of the selected items of cost covered in this part has been stated to apply broadly to many accounting systems

in varying contract situations. Thus, as to any given contract, the reasonableness and allocability of certain items of cost may be difficult to determine, particularly in connection with firms or separate divisions thereof which may not be subject to effective competitive restraints. In order to avoid possible subsequent disallowance or dispute based on unreasonableness or nonallocability, it is desirable that contractors seek advance agreement with the Government as to the treatment to be accorded those special or unusual costs. Such agreements may also be initiated by the Government. Advance agreements may be negotiated either before or during a contract but should be negotiated before incurrence of the cost covered by the agreement. Any such agreement must be in writing, shall be executed by both contracting parties, and should be incorporated in the applicable cost-reimbursement type contracts and/or made a part of the applicable negotiated fixed-price type contract file.

(b) The contracting officer is not authorized by this paragraph to agree to a treatment of costs inconsistent with this part. For example, an advance agreement may not provide that, notwithstanding § 1-15.205-17, interest shall be allowable.

(c) An advance agreement entered into in accordance with this section shall contain a suitable statement of its intended applicability and duration. The absence of an advance agreement on any element of cost will not, in itself, affect the reasonableness or allocability of that element.

(d) Advance agreements may be negotiated to affect only a single contract, a group of contracts, or may be broad enough to affect all the contracts of a procuring activity, an agency, or several agencies with a particular contractor. An advance agreement which affects only one contract, or class of contracts from a single procurement office, shall be negotiated by a procurement office contracting officer, his authorized representative, or another contracting officer when delegated this authority by the procurement office contracting officer (for example, to a contracting officer in the procurement office familiar with the particular contractor's costing system, or the agency cognizant contracting officer for that contractor, or the DOD cognizant contracting officer for Cost Accounting Standards Board matters). When the negotiation authority is delegated, the proposed agreement shall be coordinated with the procurement office contracting officer prior to execution.

(e)(1) Advance agreements other than those negotiated in accordance with (d), above, shall be negotiated by an agency cognizant contracting officer for a contractor or subcontractor. The agency cognizant contracting officer for a civilian executive agency shall be the contracting officer designated for a contractor or subcontractor by that agency. Each agency will maintain a current list of cognizant contracting officer designations. The results of the negotiation will be binding upon the agency which assigned the cognizant contracting officer.

(2) In the event the selected items of cost under consideration for advance understanding have broad application to the procurement activities of more than one executive agency, the negotiation responsibility can be assigned by majority vote among the agencies concerned

to (i) a cognizant contracting officer from one of the voting agencies, or (ii) the designated (if any) cognizant contracting officer for Cost Accounting Standards Board matters (see § 1-3.1208) with the consent of that contracting officer's agency. Factors considered in selecting an interagency cognizant contracting officer should include distribution by agency of unliquidated dollar balance of contracts being administered, existence of a designated cognizant contracting officer for CASB matters, location of contract audit support and any other particular factors which may be relevant to the particular case. A list of such designations will be published from time to time in DOD Defense Procurement Circulars and in FPR Bulletins. The results of the negotiation will be binding upon all agencies participating in the vote selection of a cognizant contracting officer with interagency negotiation responsibility.

(f) Prior to undertaking negotiation of an advance agreement, the procurement or cognizant contracting officer shall (i) determine whether there are other procurement offices within his agency, or in other agencies, that have a significant unliquidated dollar balance in contracts with the same contractor, (ii) inform any such activity or agency of the cost item(s) or other matters under consideration for negotiation, and (iii) as appropriate, invite such activity or agency and the cognizant audit activity to participate in pre-negotiation discussions and/or in the subsequent negotiations. At the completion of the negotiation, the cognizant contracting officer who has the negotiation responsibility shall prepare and distribute to other interested agencies and activities (including the cognizant audit activity) copies of the fully executed agreement together with a memorandum setting forth the principal elements of the negotiation and containing, as a minimum, the information specified in § 1-3.811, to the extent applicable.

(g) Examples of cost on which advance agreements may be particularly important are:

(1) Compensation for personal services, including but not limited to allowances for off-site pay, incentive pay, location allowances, hardship pay, and cost of living differential;

(2) Use charges for fully depreciated assets;

(3) Deferred maintenance costs;

(4) Precontract costs;

(5) Independent research and development costs;

(6) Royalties and other costs for use of patents;

(7) Selling and distribution costs;

(8) Relocation costs, as related to special or mass personnel movements;

(9) Idle facilities and idle capacity;

(10) Automatic data processing equipment;

(11) Bid and proposal costs;

(12) Severance pay to employees on support service contracts;

(13) Plant reconversion;

(14) Professional services (legal, accounting, engineering, etc.); and

(15) General and administrative costs (including corporate, division, or branch allocations) and similar expenses, attributable to the general

management, supervision, and conduct of the contractor's business as a whole. These costs are of particular significance in construction, job-site, architect-engineer, facilities, and Government-owned contractor operated (GOCO) plant contracts (see §§ 1-15.203(f), 1-15.403-7, and 1-15.502-4).

§ 1-15.108 Grants and contracts with State and local governments.

Subpart 1-15.7 of this Part 1-15 provides principles and standards for determining costs applicable to grants and contracts with State and local governments. They are designed to provide the basis for a uniform approach to the problem of determining costs and to promote efficiency and better relationships between grantees and the government. These cost principles apply to all programs that involve grants and contracts with State and local governments. They do not apply to grants and contracts with:

(a) Publicly financed educational institutions subject to Subpart 1-15.3 of this Part 1-15; or

(b) Publicly owned hospitals and other providers of medical care subject to requirements promulgated by the sponsoring Government agencies.

§ 1-15.109 Definitions.

As used in this part, except with respect to those contracts exempted under §§ 1-3.1203 (a)(1), (a)(2), or (h)(1), the words and phrases shall have the meanings prescribed by the Cost Accounting Standards Board. For convenience, CASB definitions are set forth in § 1-3.1220.

Subpart 1-15.2—Contracts With Commercial Organizations

§ 1-15.201 Basic considerations.

§ 1-15.201-1 Composition of total cost.

The total cost of a contract is the sum of the allowable direct and indirect costs allocable to the contract, incurred or to be incurred, less any allocable credits. In ascertaining what constitutes costs, any generally accepted method of determining or estimating costs that is equitable under the circumstances may be used, including standard costs properly adjusted for applicable variances.

§ 1-15.201-2 Factors affecting allowability of costs.

Factors to be considered in determining the allowability of individual items of cost include (a) reasonableness, (b) allocability, (c) standards promulgated by the Cost Accounting Standards Board, if applicable, otherwise, generally accepted accounting principles and practices appropriate to the particular circumstances, and (d) any limitations or exclusions set forth in this Subpart 1-15.2 or otherwise included in the contract as to types or amounts of cost items. When a contractor has disclosed his cost accounting practices in accordance with Cost Accounting Standards Board rules, regulations, and standards and any such

practices are inconsistent with any of the provisions of this Subpart 1-15.2, costs resulting from such inconsistent practices shall not be allowed in excess of the amount that would have resulted from the use of practices consistent with this Subpart 1-15.2.

§ 1-15.201-3 Definition of reasonableness.

A cost is reasonable if, in its nature or amount, it does not exceed that which would be incurred by an ordinarily prudent person in the conduct of competitive business. The question of the reasonableness of specific costs must be scrutinized with particular care in connection with firms or separate divisions thereof which may not be subject to effective competitive restraints. What is reasonable depends upon a variety of considerations and circumstances involving both the nature and amount of the cost in question. In determining the reasonableness of a given cost, consideration shall be given to:

(a) Whether the cost is of a type generally recognized as ordinary and necessary for the conduct of the contractor's business or the performance of the contract;

(b) The restraints or requirements imposed by such factors as generally accepted sound business practices, arm's length bargaining, Federal and State laws and regulations, and contract terms and specifications;

(c) The action that a prudent business man would take in the circumstances, considering his responsibilities to the owners of the business, his employees, his customers, the Government, and the public at large; and

(d) Significant deviations from the established practices of the contractor which may unjustifiably increase the contract costs.

§ 1-15.201-4 Definition of allocability.

A cost is allocable if it is assignable or chargeable to one or more cost objectives (see § 1-3.1220 for definition) in accordance with the relative benefits received or other equitable relationship. Subject to the foregoing, a cost is allocable to a Government contract if it:

(a) Is incurred specifically for the contract;

(b) Benefits both the contract and other work, or both Government work and other work, and can be distributed to them in reasonable proportion to the benefits received; or

(c) Is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.

§ 1-15.201-5 Credits.

The applicable portion of any income, rebate, allowance, and other credit relating to any allowable cost, received by or accruing to the contractor, shall be credited to the Government either as a cost reduction or by cash refund, as appropriate. However, payment of interest on contractors' claims pursuant to § 1-1.322 is exempt from the requirements of this section.

§ 1-15.202 Direct costs.

(a) A direct cost is any cost which can be identified specifically with a particular final cost objective. (See § 1-3.1220 for definitions.) No final cost objective shall have allocated to it as a direct cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included in any indirect cost pool to be allocated to that or any other final cost objective. Costs identified specifically with the contract are direct costs of the contract and are to be charged directly thereto. Costs identified specifically with other final cost objectives of the contractor are direct costs of those cost objectives and are not to be charged to the contract directly or indirectly.

(b) Any direct cost of minor dollar amount may be treated as an indirect cost for reasons of practicality where the accounting treatment for such cost is consistently applied to all final cost objectives, *Provided*, That such treatment produces results which are substantially the same as the results which would have been obtained if such costs had been treated as a direct cost.

§ 1-15.203 Indirect costs.

(a) An indirect cost (see § 1-3.1220 for definition) is one which, because of its incurrence for common or joint objectives, is not readily subject to treatment as a direct cost. Any direct cost of minor dollar amount may be treated as an indirect cost for reasons of practicality under the circumstances set forth in § 1-15.202(b). After direct costs have been determined and charged directly to the contract or other work as appropriate, indirect costs are those remaining to be allocated to the several cost objectives. No final cost objective shall have allocated to it as an indirect cost any cost, if other costs incurred for the same purpose, in like circumstances, have been included as a direct cost of that or any other final cost objective.

(b) Indirect costs shall be accumulated by logical cost groupings with due consideration of the reasons for incurring the costs. Each grouping should be determined so as to permit distribution of the grouping on the basis of the benefits accruing to the several cost objectives. Commonly, manufacturing overhead, selling expenses, and general and administrative expenses are separately grouped. Similarly, the particular case may require subdivisions of these groupings, e.g., building occupancy costs might be separable from those of personnel administration within the manufacturing overhead group. The number and composition of the groupings should be governed by practical considerations and should be such as not to complicate unduly the allocation where substantially the same results are achieved through less precise methods.

(c) Each grouping shall be distributed to the appropriate cost objectives. This necessitates the selection of a distribution base common to all cost objectives to which the grouping is to be allocated. The base should be selected so as to permit allocation of the grouping on the basis of the benefits accruing to the several cost objectives. This principle for selection is not to be applied so rigidly as to complicate unduly the allocation

where substantially the same results are achieved through less precise methods. Once an appropriate base for the distribution of indirect costs has been accepted, such base shall not be fragmented by the removal of individual elements. Consequently, all items properly includable in an indirect cost base should bear a pro rata share of indirect costs irrespective of their acceptance as Government contract costs. For example, when a cost of sales base is deemed appropriate for the distribution of general and administrative (G&A) costs, all items chargeable to cost of sales, whether allowable or unallowable, shall be included in the base and bear their pro rata share of G&A costs.

(d) The method of allocation of indirect costs must be based on the particular circumstances involved. The method shall be in accordance with standards promulgated by the Cost Accounting Standards Board, if applicable to the contract. Otherwise, the method shall be in accordance with generally accepted accounting principles. When Cost Accounting Standards Board standards are not applicable to the contract, the contractor's established practices, if in accordance with generally acceptable accounting principles, shall generally be acceptable. However, the method used by the contractor may require examination when:

(1) Any substantial difference occurs between the cost patterns of work under the contract and other work of the contractor;

(2) Any significant change occurs in the nature of the business, the extent of subcontracting, fixed asset improvement programs, the inventories, the volume of sales and production, manufacturing processes, the contractor's products, or other relevant circumstances; or

(3) Indirect cost groupings developed for a contractor's primary location are applied to offsite locations. Separate cost groupings for costs allocable to offsite locations may be necessary to permit equitable distribution of costs on the basis of the benefits accruing to the several cost objectives.

(e) A base period for allocation of indirect costs is the period during which such costs are incurred and accumulated for distribution to work performed in that period. Normally, the base period will be the contractor's fiscal year; however, use of a shorter period may be appropriate in case of (1) contracts whose performance involves only a minor portion of the fiscal year, or (2) where it is general practice in the industry to use a shorter period. In any event the base period or periods shall be so selected as to avoid inequities in the allocation of costs. When the contract is performed over an extended period of time, as many such base periods will be used as will be required to represent the period of contract performance.

(f) Special care should be exercised in applying the principles in paragraphs (b), (c), and (d) of this section when Government-owned contractor operated (GOCO) plants are involved. The distribution of corporate, division, or branch office general and administration expenses to such plants when they operate with little or no dependence on corporate administrative activities, may require more precise cost groupings, detailed accounts screening, and carefully developed distribution bases.

§ 1-15.204 Application of principles and procedures.

(a) Costs shall be allowed to the extent that they are reasonable (see § 1-15.201-3), allocable (see § 1-15.201-4), and determined to be allowable in view of the other factors set forth in §§ 1-15.201-2 and 1-15.205. These criteria apply to all of the selected items of cost which follow, notwithstanding that particular guidance is provided in connection with certain specific items for emphasis or clarity.

(b) Costs incurred as reimbursements or payments to a subcontractor under a cost-reimbursement, fixed-price incentive, or price redeterminable type subcontract of any tier above the first firm fixed-price or fixed-price escalation subcontract are allowable to the extent that allowance is consistent with the subpart of this Part 1-15 which is appropriate to the subcontract involved. Thus, if the subcontract is for supplies, such costs are allowable to the extent that the subcontractor's costs would be allowable if this Subpart 1-15.2 were incorporated in the subcontract; if the subcontract is for construction, such costs are allowable to the extent that the subcontractor's costs would be allowable if Subpart 1-15.4 of this Part 1-15 were incorporated in the subcontract. Similarly, costs incurred as payments under firm fixed-price or fixed-price escalation subcontracts or modifications thereto, when cost analysis was performed pursuant to § 1-3.807-10(b), shall be allowable only to the extent that the price was negotiated in accordance with the principles in § 1-15.106.

(c) Selected items of cost are treated in § 1-15.205. However, § 1-15.205 does not cover every element of cost and every situation that might arise in a particular case. Failure to treat any item of cost in § 1-15.205 is not intended to imply that it is either allowable or unallowable. With respect to all items, whether or not specifically covered, determination of allowability shall be based on the principles and standards set forth in this subpart and, where appropriate, the treatment of similar or related selected items.

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