

DynCorp on Hook for Subcontractor's False Claims

Written by Nick Sanders
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Recently we [took umbrage](#) at the phrase “the prime is responsible for managing the subcontractor” – asserting that it had been taken out of context and inflated by DCAA and GAO into a meaning the rule drafters had never intended. Despite our strong reservations with what government folks had done with the language, we were careful to distinguish certain things with which we agreed. We wrote about an official DCAA presentation –

It states: *The prime contractor is primarily responsible for subcontract award, technical and financial performance, monitoring, and payment to the subcontractor for the work accomplished under subcontract terms.* That's quite true and unobjectionable

Indeed, there is nothing unobjectionable about the idea that the prime contractor (or higher tier subcontractor) is responsible for managing its subcontractor. If you know anything about Apogee Consulting, Inc., you should know that we have long been vociferous advocates of subcontractor management.

Let's list those prime contractor duties found above in the DCAA presentation:

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Subcontract award

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Technical performance

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Financial performance

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Monitoring

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Payment for work accomplished

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Compliance with subcontract terms

One sticks out a bit: “monitoring” the subcontractor. What does it mean to monitor the subcontractor? What efforts are sufficient in that regard?

Well, obviously the efforts deployed to monitor a subcontractor depend on the risks. If the contract is firm, fixed-price, then cost risks are minimal, since (except for contract changes) the price to be paid to the subcontractor is fixed and won't change based on costs incurred. That means that cost allowability issues largely disappear after subcontract award (but need to be addressed when negotiating the contract price). If the contract is FFP, then the subcontractor may not need much in the way of an adequate accounting system; and thus the prime may not have to worry overmuch about monitoring what comes out of that system.

But the converse is also true. If the subcontract type is other than FFP – if, for example, it is T&M or cost-type – then the prime contractor (or higher tier subcontractor) must monitor costs being billed. The prime contractor must review each invoice submitted and exercise due diligence to ensure that only appropriate costs – that is to say, reasonable, allowable, and allocable costs – are being billed and reimbursed. The subcontractor needs to have appropriate infrastructure in place so that the prime can rely on its controls; or, failing that, the prime needs to deploy additional controls to make up for its subcontractor's lack. It would not be unheard-of for the prime contractor to have a team of “auditors” – its own employees – review each monthly invoice and approve that invoice for payment, just to make sure unallowable costs didn't inadvertently get reimbursed and then passed on to the government customer through the prime contractor's own invoices.

The effort expended by the prime (or higher tier subcontractor) depends on a risk analysis. The risk analysis needs to be performed and then appropriate action taken. That's what we think “monitoring” means.

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If the prime (or higher tier subcontractor) doesn't fulfill its responsibility for monitoring its subcontractors, then it ends up like DynCorp.

DynCorp was the subject of a False Claims Act suit brought by the Department of Justice. According to the DoJ [press release](#) —

The United States filed a False Claims Act complaint against DynCorp International Inc. (DynCorp) alleging that it knowingly submitted inflated claims in connection with a State Department contract to train Iraqi police forces (CIVPOL contract) ... in its complaint, the United States alleges that DynCorp knowingly allowed one of its main CIVPOL subcontractors to charge excessive and unsubstantiated rates for hotel lodging, translator, security guard and driving services and overhead expenses, and included these charges in the claims it submitted under the CIVPOL contract to the State Department. The complaint also alleges that DynCorp added its own markup to its subcontractor's excessive charges, thereby further inflating the claims it submitted to the government.

What the allegations seem to say is that DynCorp failed at monitoring its subcontractor. It allegedly allowed the subcontractor to submit invoices, and receive reimbursement, for "excessive and unsubstantiated" costs. DynCorp paid the invoices and included them in its own contract costs (as one does) and then "marked-up" the costs (with some kind of indirect cost rate), which we assume included an element of fee as well. Now DynCorp is facing serious allegations and will have to hire some serious attorneys to defend it and (perhaps) negotiate a serious settlement.

This would seem to be a great illustration of the importance of monitoring subcontractors, which is an element of overall subcontractor management. Effective subcontractor management may be expensive, but we believe that ineffective subcontractor management is even more expensive.