

Proposed Revisions to DFARS Business System Oversight Regime

Written by Nick Sanders
Friday, 08 August 2014 11:31

Governor Robert Ritchie, R-FL : Now, he's going to throw a big word at you – ‘unfunded mandate.’ He's going to say if Washington lets the states do it, it's an unfunded mandate. But what he doesn't like is the federal government losing power. But I call it the ingenuity of the American people.

Moderator : President Bartlet, you have 60 seconds for a question and an answer.

President Josiah ‘Jed’ Bartlet: Well, first of all, let's clear up a couple of things. ‘Unfunded mandate’ is two words, not one big word.

If there is one particular topic we have covered thoroughly on this site, it would have to be the DFARS Business System Administration rules. We railed against it when it was first promulgated as a proposed rule; we railed against it when it became a final DFARS rule. We reported on DCAA and DCMA implementation and interpretation, and we reported on DOD Inspector General criticism of DCAA’s inability to fulfill its oversight responsibilities. You want to see those articles, just type “business system” into the keyword search feature on the front page.

More recently, we [warned](#) readers of a rumored sea change in the DCAA Business System oversight role, wherein DCAA would stop auditing contractors’ business systems altogether. We thought that would be a brilliant idea, writing “Consequently, it's likely that contractors are going to be required to spend more of their limited indirect funds to pay for external CPAs to review their business systems, a review that will be mandated by DOD and paid for through increased prices for goods and services.”

Indeed, that is what the proposed DFARS [rule revisions](#) would entail.

Published July 15, 2014, the proposed DFARS rule revisions would purport to “ensure appropriate contractor accountability for adequate contractor business systems.” It would accomplish that objective by—

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... proposing to amend the DFARS to entrust contractors with the capability to demonstrate compliance with DFARS system criteria for contractors' accounting systems, estimating systems, and material management and accounting systems, based on contractors' self-evaluations and audits by independent Certified Public Accountants (CPAs) of their choosing. Government auditors will perform overviews of the results of contractor self-evaluations and CPA audits.

Let's be clear. DCAA would no longer audit three of the six DFARS business systems. Those three systems are Estimating, Accounting, and Material Management and Accounting (MMAS). Instead, contractor's would be "entrusted" with their own evaluations, augmented by periodic reviews by independent CPA firms.

Let's be even clearer:

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For the three systems noted above, contractors must conduct annual self-assessments and report the results of those self-assessments to the cognizant ACO and to DCAA. The annual self-assessments must be completed within six months of the end of the contractor's fiscal year and must be signed-off by a contractor executive.

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In year one, and once every three years thereafter (unless the cognizant ACO directs a more frequent assessment) the contractor will engage an independent CPA firm to perform an external assessment of the three systems in accordance with GAGAS. As part of the external report, the contractor must provide the cognizant ACO and DCAA with the CPA's audit strategy, risk assessment, and audit plan (program), upon completion. The CPA firm must provide its working papers for government inspection.

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DCAA may review the annual self-certifications or the triennial independent CPA reports, and may provide its findings to the cognizant ACO.

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The contractor's failure to submit either the annual self-certification or the triennial independent

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CPA report will constitute a “significant” deficiency and will lead to payment withholds.

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The new rule does not apply to small businesses.

The proposed rule has drawn intense scrutiny from many sources. The attorneys at Wiley Rein [opined](#)

For contractors, the ability to potentially accelerate approval of their business systems may be attractive. Nonetheless, the proposed rule imposes significant new mandatory requirements on covered contractors to report their annual business system assessments, engage independent CPAs to provide audit plans and perform audits, and produce documentation regarding audits and assessments. Since these contractor and CPA reports are subject to DCAA review, it remains to be seen how long DCAA takes to review the reports and whether DCAA will accept CPA audits or review them so critically that the anticipated efficiencies are lost.

Attorneys at McKenna Long & Aldridge **wrote**—

The purposes of the proposed rule appear to be to relieve DCAA of business system audit responsibilities it has been unable to meet, and to require that contractors disclose to the government internal documentation supporting contractor’s business systems that the government is often unable to obtain in connection with system reviews. It remains to be seen whether DOD will seek to impose the same or similar reporting requirements in connection with the purchasing, earned value management, and property management systems that DCMA currently reviews.

What do we think?

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Well, we think that if contractors' business systems truly are the "first line of defense against fraud, waste, and abuse," as every civil servant seems to think and has so testified, then it is a damning indictment that DCAA lacks sufficient resources to perform timely audits on those business systems. The phrase "inherently governmental function" springs to mind. And now that government oversight, for which the taxpayers have paid and paid and paid, is going to be outsourced. Will DCAA downsize as a result of its suddenly reduced workload? Doubtful. So there will be no reduction in government oversight costs, while the contractors will be required to pay for the oversight that was previously performed by DCAA.

Tell us that won't raise contractors' costs and prices. Tell us the taxpayers won't pay more. Go on. We're waiting.

But more fundamentally, we believe this rule is anti-small business. We believe this rule will harm small businesses. "How is that," you may say, since the proposed rule clearly exempts small businesses. Well, here's how: If DCAA is not going to perform business system reviews and large businesses will perform their own reviews, then what are small businesses going to do? That's right: nothing. So they will not have approved business systems and will be at a competitive disadvantage. They won't be able to win that big contract that moves them from small to large business.

At a time when more and more RFPs required approved business systems, small businesses won't have them. FAR 16.603 requires that a contractor must have an adequate accounting system in order to be awarded a cost-type contract. How are small businesses going to obtain a determination that their system is adequate when DCAA won't be performing audits anymore? Are small businesses supposed to have the same financial resources as large businesses? We don't think so. As a result, we very much suspect small businesses will be unable to win awards of cost-type contracts—including SBIR Phase 2 contracts.

Where are the independent CPA firms going to come from? You know, the ones with GAGAS compliance training and government contract expertise. Sure, they exist. But contractors will not be able to use their external auditor for such work and the other firms will be vying for the remediation work (where the money is), so who will be left to perform the assessment work?

Which firm will agree to the potential liability associated with a system approval that the DCAA subsequently finds to be deficient? Which firm will agree to turn over its working papers for DCAA review? Again, they exist. But there will not be very many of them and they will charge

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contractors dearly for the work. And the contractors will pass those charges back to DOD via indirect rate increases.

Clearly, something needs to be done. But this proposal either goes too far or doesn't go far enough. DOD needs to remove DCAA completely from the picture and simply rely on the work of the independent CPAs. Failing that, DOD needs to completely revamp DCAA so the audit agency can actually perform quality audits that are useful to COs, and issue them timely.

Or perhaps it's time to rethink this unworkable and quite frankly punitive business systems oversight regime. You know, go back to the drawing board and start fresh. We would advocate that approach.

If you feel the same way we do about this proposed rule, you may wish to submit written comments to the DAR Council for consideration. Not that we expect the DAR Council to actually listen to the public input (they didn't listen the last time, when many (including Apogee Consulting, Inc.) told them their original plan was not going to work, because DCAA lacked sufficient resources to execute its role. But still. We have to keep trying to help the bureaucrats even if our efforts will prove futile.

You can submit comments on DFARS Case 2012-D042 before September 15, 2014 as follows:

Regulations.gov: <http://www.regulations.gov> . Submit comments via the Federal eRulemaking portal by inserting "DFARS Case 2012-D042" under the heading "Enter keyword or ID" and selecting "Search." Select the link "Submit a Comment" that corresponds with "DFARS Case 2012-D042." Follow the instructions provided at the "Submit a Comment" screen. Please include your name, company name (if any), and "DFARS Case 2012-D042" on your attached document. Follow the instructions for submitting comments. Show citation box

Email: osd.dfars@mail.mil . Include DFARS Case 2012-D042 in the subject line of the message.

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