Org: IT Alliance for Public Sector
Name: Eminence Griffin
sectionnumber: Sec. 893
Input: For Section 893, Business System Requirements, ITAPS recommends a clarification that if a contractor is determined not to be a covered contract under Section 893 of the FY 2011 NDAA, as amended by Section 893 of the FY 2017 NDAA, the following FAR, DFAR clauses and CAS and MAARs do not apply to that contractor - as they exempted under Section 893. The below FAR, DFAR and MAAR clauses are duplicative of the business system requirements in Section 893. It is our position that Section 893 applies to all business system requirements regardless of where they appear in supporting regulations. Accordingly, we request that following be included in the DFARS Case:

The term “contractor business system” includes –

A. The accounting system, estimating system, purchasing system, earned value management system, material management and accounting system, or property management system of a contractor, or

B. The United States Government business system rule requirements in Section 893 also address those requirements promulgated in -

i. The Federal Acquisition Regulations.
ii. Title 48 of the Code of Federal Regulations.
iii. The Government Auditing Standards.
iv. The Defense Federal Acquisition Regulation Supplement.
v. The Cost Accounting Standards.
vi. The Mandatory Annual Audit Requirements.
vii. The Defense Contract Audit Agency Contract Audit Manual.

A contractor that qualifies as a non-covered contractor is except from business system rule requirements as promulgated throughout the FAR, DFARS, GAS, CAS, CFR, MAARs and DCAA audit manuals and instructions.

Please see Attachment #1 for the ninety-seven (97) unique business system rule requirements promulgated throughout the FAR, DFAR, CAS, MAARs and DCAA Contract Audit Manual.

Attachment #1-List of Business System Rule Requirements listed in the FAR, DFAR and MAAR:

Accounting and Billing Systems:

1. DFARS Subpart 242.75
2. DFARS Subsection 252.242.7006
3. 48 C.F.R. Parts 9901, 9903 and 9904
4. FAR Part 31
5. FAR Subsection 52.216-7
6. FAR Subsection 52.216-10
7. FAR Subsection 52.232-16
8. FAR Subsection 52.232-7
9. DFARS Part 231

Purchasing System:

10. DFARS Subsection 252.244.7001
11. DFARS Subsection 244.305.70

12. FAR Part 44
13. FAR Subsection 52.244-2
14. FAR Subsection 52.244-5
15. FAR Subsection 52.244-6
16. DFARS Part 244

Estimating Systems:
17. DFARS Subsection 215.407-5-70(b)
18. DFARS Subsection 252.212.7002(a)-(g)
19. FAR Subsection 15.403
20. FAR Subsection 15.407-5
21. FAR Subsection 15.408
22. FAR Subsection 31.205-26
23. 48 C.F.R. subsection 9904.401-20
24. 10 USC subsection 2306a

Government Property Management System:
25. DFARS Subsection 245.105
26. DFARS Subsection 252.245.7003
27. FAR Subsection 45.101
28. FAR Subsection 45.107
29. FAR Subsection 52.232-16(d)-(f)
30. FAR Subsection 52.245.1
31. DFARS Subsection 252.242-7004

Material Management and Accounting System:
32. DFARS Subpart 242.72
33. DFARS Subsection 252.242-7004
34. FAR Subsection 31.205-26
35. 48 C.F.R. Subsection 9904.411

Earned Value Management System:
36. DFARS Subpart 234.2
37. DFARS Subsection 252.234.7002
38. FAR Subpart 34.2
39. DoD Instruction No 5000.02
40. American National Standards Institute / Electronics Alliance Standard-748-B, EVMS
41. DoD Earned Value Management Implementation Guide
42. DCAA Contract Audit Manual
43. NDIA Program Management System Committee Earned Value Management Systems Intent Guide.

Administration of Business System Requirements:
44. DFARS Subsection 242.7001, Contractor Business System
45. DFARS Subsection 252.242-7005, Contractor Business System
46. DFARS Subsection 252.215-7002, Cost Estimating Systems Requirements
47. DFARS Subsection 252.234-7002, Earned Value Management
48. DFARS Subsection 242.242-7004, Material Management and Accounting Systems

49. DFARS Subsection 252.242.7006, Accounting System Administration
50. DFARS Subsection 252.244.7001, Contractor Purchasing System Administration
51. DFARS Subsection 252.245-7003, Contractor Property Management System Administration
52. FAR Part 30, Cost Accounting Standards Administration
53. FAR Part 31, Contract Cost Principle and Procedures
54. FAR Part 53.209, Contractor Qualifications
55. FAR Subpart 44.3, Contractors Purchasing Systems Reviews
56. FAR Subpart 15.4, Contract Pricing
57. FAR Subpart 34.2, Earned Value Management System
58. Cost Accounting Standards (CAS) Consistency in Estimating, Accumulating and Reporting Cost
59. CAS Consistency in Allocating Costs Incurred for the Same Purpose
60. CAS Allocation of Home Office Expenses to Segments
61. CAS Capitalization of Tangible Assets
62. CAS Accounting for Unallowable Costs
63. CAS Cost Accounting Period
64. CAS Use of Standard Costs for Direct Material and Direct Labor
65. CAS Accounting for Costs of Compensated Personal Absence
66. CAS Depreciation of Tangible Capital Assets
67. CAS Allocation of Business Unit General and Administrative Expenses to Final Cost Objectives
68. CAS Accounting for Acquisition Costs of Material
69. CAS Composition and Measurement of Pension Costs
70. CAS Adjustment and Allocation of Pension Cost
71. CAS Cost of Money as an Element of the Cost of Facilities Capital
72. CAS Accounting for the Cost of Deferred Compensation
73. CAS Accounting for Insurance Cost
74. CAS Cost of Money as an Element of the Cost of Capital Assets Under Construction
75. CAS Allocation of Direct and Indirect Costs
76. CAS Accounting for Independent Research and Development Costs
77. DFARS Part 230, Cost Accounting Standards
78. DFARS Part 231, Contract Cost Principles and Procedures
79. DFARS Subpart 253.209, Contractor Qualifications
80. DFARS Subpart 244.3, Contractors Purchasing Systems Reviews

DCAA Mandatory Annual Audit Requirements (MAARs)(more details available if needed):

81. MAARs Audit #1, Internal Control Audit Planning
82. MAARs Audit #2, Contract cost analysis and reconciliation to books
83. MAARs Audit #3, Permanent files
84. MAARs Audit #4, Tax returns and financial statements
85. MAARs Audit #5, General ledger, trial balance, income and/or credit adjustments
86. MAARs Audit #6, Labor floor checks and interviews
87. MAARs Audit #7, Changes in charging direct/indirect costs
88. MAARs Audit #8, Comparative analysis – sensitive labor account
89. MAARs Audit #9, Payroll/Labor distribution reconciliation and tracing
90. MAARs Audit #10, Adjusting entries and exception reports
91. MAARs Audit #12, Auditable subcontracts/assist audits
92. MAARs Audit #13, Purchase existence and consumption
93. MAARs Audit #14, Pools/Base reconciliation to books
94. MAARs Audit #15, Indirect cost comparison with prior years and budgets

95. MAARs Audit #16, Indirect account analysis
96. MAARs Audit #18, Indirect allocation bases
97. MAARs Audit #19, Indirect rate computations

Attachment #2 - Mandatory Annual Audit Requirements (MAARs) When it comes to audits of incurred costs, DCAA auditors use Mandatory Annual Audit Requirements (MAARs). MAARs are minimum audit procedures necessary to comply with generally accepted government auditing standards (GAGAS) when performing incurred cost audits.

The MAARs vary greatly in purpose, type of transaction being evaluated, and time frame of accomplishment. MAARs are performed at all major contractors (those with $100 million or more in costs booked to flexibly-priced contracts such as CPFF, CPIF, FPI, and T&M) unless such work would fulfill no useful current or future need or the contractor has no costs claimed in one or more cost elements related to a specific MAAR.

- MAARs 1, 3, and 7 are typically accomplished on a continuous basis as audits are performed and are not necessarily associated with a single contractor fiscal year or exclusively with the incurred cost audit.
- MAARs 2, 4, 9, 14, 15, and 19 are "reconciliation" procedures and are usually performed as preliminary steps in the audit of incurred costs.
- MAARs 10 and 16 are historical transaction testing and performed during the incurred cost audit.
- MAARs 6 and 13 are concurrent procedures and must be performed during the fiscal year being audited.
- Finally MAARs 5, 8, 12, and 18 are typically performed during annual incurred cost audits but may also be performed in advance of the fiscal year being audited.

MAAR #1 - Internal Control Audit Planning and/or Internal Control Questionnaire. The purpose of this requirement is to determine the extent of reliance that can be placed on the internal controls for contract costs and the need for and extent of substantive testing that may be required based on the observed strengths or weaknesses of contractor systems. Essentially, the better a contractors internal control systems, the less auditing will be required. If the auditor can rely on internal control systems to "catch" potentially unallowable costs, he/she can reduce audit testing.

MAAR #2 - Contract Cost Analysis and Reconciliation to Books. This provides the auditor (i) an overview and order-of-magnitude frame of reference for direction of audit effort and other audit planning/performance considerations, and (ii) to verify that the auditable costs claimed or to be claimed on Government contracts tie in to the amounts produced by the accounting system in the contractor's official books and records. Auditors will evaluate summaries of the contractor's total annual contract costs by major cost element (material, subcontracts, intra-company charges, and credits, etc), and verify that the auditable contract costs reconcile to contractor accounting records by cost element.

MAAR #3 - Permanent Files. Permanent files provide an efficient and effective repository of current audit information. Permanent file maintenance should help identify the need for further audit and analysis, and help in determining the accounting methods that influence the nature, level, and extent of further testing required in specific cost accounts, functions, operations, and departments. Permanent files are updated for new or changed contractor organizations, operations, policies, procedures, internal controls, software programs, and accounting methods that influence the nature, level, and accounting treatment of costs being charged to Government contracts.

MAAR #4 - Tax Returns and Financial Statements. The purpose of this step is to highlight possible areas to reduce the extent of audit effort that might otherwise be required. The evaluation of a contractor's financial statements, corporate minutes, tax returns, reports filed with regulatory bodies (e.g. SEC) and

data available on the corporate web site will assist the auditor in planning the audit more effectively. Generally, greater weight is placed on corporate reports to regulatory bodies with reporting requirements.
MAARs #5 - General ledger, trial balance, income and/or credit adjustments. The purpose of this procedure is to help identify any income and credits which the Government may be entitled to obtain or share, and to evaluate the exclusion of any adjustments not reflected by the contractor in Government contract costs. It is not uncommon nor is it contrary to generally accepted accounting principles (GAAS) to book miscellaneous income "below the line" to an income statement section reserved for non-operating income and expenses. However, sometimes the Government is entitled to share in these non-operating transactions (e.g. rebates). Additionally, contractors have been known to hide expenses in these sections in order to reduce their indirect expense rate allocation bases thereby increasing their indirect rates (hint: don't do that).

MAARs #6 - Labor floorchecks or interviews - We've covered this area extensively in our blog. The purpose of this procedure is to test the reliability of employee time records, that employees are actually at work (difficult for "work-at-home" employees), that they are performing in assigned job classifications, and that time is charged to the proper cost objective. This is one of the two MAARs that must be performed in the year the costs are incurred (the other is MAAR #13). After the fact, there is no way to determine that time charges correspond to the work actually being performed.

MAARs #7 - Changes in charging direct/indirect costs. The purpose of this procedure is to verify that changes in charging direct/indirect cost do not have the effect of improperly shifting costs among cost objectives or circumventing costs targets or ceilings of certain contracts or other significant cost categories. The auditor will evaluate changes in procedures and practices for charging direct/indirect cost for consistency with generally accepted accounting principles, the applicable cost principles per contracts, and any applicable CAS requirements.

MAARs #8 - Comparative analysis-sensitive labor accounts. The purpose of this procedure is to identify for further examination any sensitive labor charges (for example, indirect charging by direct labor employees) that vary significantly from the prior period and/or budgetary estimates. Lately, DCAA has been requesting contractors to prepare two or three year comparisons of costs by account. It saves time for the auditor however there is no contractual requirement that contractors do so.
MAAR #9 - Payroll/Labor Distribution Reconciliation and Tracing. The purpose of this MAAR is to test the overall integrity of labor cost records at the general ledger and cost ledger levels, and to reconcile payroll accruals and disbursements to ensure that distribution entries trace to and from the cost accumulation records. Or, to put it another way, how does an hour charged on a timesheet, convert to dollars on a bill to the Government.
MAAR #10 - Adjusting entries and exception reports. The purpose of this MAAR is to identify adjustments and/or exceptions that require further audit analysis and explanation. The audit will evaluate the propriety of adjusting journal entries and exception reports for both direct and indirect costs.
MAAR #11 - Reserved. (At one time, MAAR #10 pertained to labor adjusting journal entries and MAAR #11 pertained to materials adjusting journal entries. These were combined into a single MAAR.
MAAR #12 - Auditable subcontracts/assist audits. The purpose of this procedure is to identify and request assist audits on "auditable" subcontracts. "Auditable" subcontracts are flexibly priced subcontracts awarded under flexibly priced prime contracts. It is the prime contractor's responsibility to perform subcontract audits but its the auditor's responsibility to ensure that those audits are adequately performed.

MAAR #13 - Purchases existence and consumption. The purpose of this MAAR is to test that materials were in fact received (exist or were consumed) and that services were in fact performed. The auditor will make physical observations and/or inquiries on a concurrent basis in addition to documentation verification of contract charges for purchased materials and services.
MAAR #14 - Pools/Base Reconciliation to Books. The purpose of this procedure is to determine that the claimed indirect cost pools and allocation bases under Government contracts reconcile to amounts in the contractor's official books and records. This is why auditors will often request the "trail balance" when determining adequacy of an annual submission.
MAAR #15 - Indirect cost comparison with prior years and budgets. The purpose of this procedure is to identify changes in cost accounting practices, reclassification of costs, and areas with substantial increases or decreases in costs that require further audit analysis and/or explanation. Auditors will often ask contractors to prepare a comparison showing current year and prior year's costs by account. Significant changes either up or down will prompt at least a query.
MAAR #16 - Indirect account analysis. This is likely the area that an auditor will spend the most time during an audit of incurred costs. The auditor needs to obtain sufficient evidence to support an opinion on the allowability, allocability, and reasonableness of the costs. The auditor will concentrate on sensitive accounts, new accounts and accounts with large variances.
MAAR #17 - Reserved. Initially, this MAAR involved IR&D/B&P computations. At one time, there were limits to how much a contractor could claim on Government contracts and this involved formulas and comparisons with prior years. After those limits were eliminated in the FAR cost principles, this MAAR was dropped.
MAAR #18 - Indirect allocation bases. The purpose of this MAAR is to assure that allocation bases are equitable for allocation of indirect costs to intermediate and final cost objectives. The focus here is on whether indirect costs are allocated to cost objectives on a "causal and beneficial" basis.
MAAR #19 - Indirect rate computations. The purpose here is to confirm that the contractor's rate computations are accurate for distributing indirect costs to Government contracts. Most contractors use Excel-based models to submit their annual incurred cost claims. These models are moderately complex and errors commonly occur.
MAAR #20 - Reserved. At one time, this MAAR required auditors to review adjusting journal entries that involve indirect expenses. It has now been merged into MAAR #10 which requires auditors to review all adjusting journal entries.