

UNANET WHITE PAPER

The Basics of Incurred Cost Audits



Unanet

OVERVIEW

Every year, DCAA performs thousands of audits but the most common is the Incurred Cost Audit and it continues year over year to be a priority for DCAA. This audit verifies that the prices paid for cost reimbursable services are both fair and reasonable. As tax payers we want to know that we are getting what we pay for.

“One of the several benefits of Unanet is the ease of satisfying a DCAA auditor.”

PURPOSE OF THE AUDIT

The Incurred Cost Submission (ICS) is a financial representation of both the direct and indirect cost of the work that was performed for a fiscal period. It is used to make sure that claimed actual cost and billed cost reconcile. The requirement and specifications for the content of the submission are in FAR 52.216-7- Allowable Cost and Payment. The clause addresses two key areas: interim reimbursement of costs and determination of final indirect rates and billing rates. Using a financial accounting system like Unanet helps assure that all types of costs are properly accounted for and are easily reportable.

The overall submission can be difficult as there are both mandatory and supplemental schedules and you must identify items such as your rate structure, direct cost to cost objectives (contracts) and identify both indirect and unallowable costs. Incurred Cost Electronically (ICE) is an Excel spreadsheet found on dcaa.mil that provides you with a standardized, user-friendly, electronic package to assist in preparing an adequate incurred

cost submission. Using the ICE model should result in less time spent preparing the submission as well as supporting the audit. Keep in mind that any missing or unreconcilable schedule could cause the submission to be deemed inadequate so best practice is to use the ICE spreadsheet promulgated by DCAA.

BENEFITS OF ICE:

- Standardized and reasonably user friendly
- It includes all schedules required for an adequate submission per the Allowable Cost and Payment clause (FAR 52-216-7)
- Updates are performed electronically and the linking feature updates all impacted schedules
- ICE creates an inventory of electronic files that can be used in subsequent years to compare costs and facilitate submission preparation
- The submission of an adequate proposal may facilitate a more timely determination of indirect rates and that will expedite contract closing outs

WHO IS REQUIRED TO SUBMIT?

This submission is required annually of all contractors performing contracts with cost reimbursable provisions and which contain the Allowable Cost and Payment clause. CAUTION: This clause includes most, if not all, T&M contracts—not just cost plus contracts. The submission must be made annually within six months following the end of the contractor's fiscal year. Extensions are granted only on an exception basis. The request must be in writing and if the Contracting Officer (ACO for those under DOD cognizance) grants the exception, that must also be in writing. Requests "One of the several benefits of Unanet is the ease of satisfying a DCAA auditor." for extension are very rarely granted. Late submissions without an extension are much more common, particularly for firms with systems that have poor access to the necessary data.

Failure to submit a required ICS may lead to billing withholds or just a plain refusal to pay, and no firm needs that problem. The other danger is that the Contracting Officer can unilaterally set the final indirect rates and the resulting rates will be low enough to ensure the government is not paying for unallowable costs. In other words, COMPLY.

POLICIES AND PROCEDURES

One of the keys to a smooth ICS audit is to have concise, written policies and procedures that document your cost accounting practices and make them available to your auditors. The document(s) should include policies and procedures with respect to Billing, Travel, Bonus, Segregation of Direct and Indirect Costs, Segregation of Allowable and Unallowable Costs, Vendor and Subcontractor payments, and the structure and allocation bases of all indirect pools including both intermediate and final pools. Also make sure that the actual practices match what is outlined in the policies and procedures

and that you can demonstrate compliance to them. Be prepared to answer questions on your costs from who got paid to where, when, and why.

EXAMPLES OF QUESTIONED COSTS:

- Travel costs over prescribed per diem rate for the location
- Employee bonuses
- Executive compensation
- Salaries above agency administrative caps (usually a contract provision)
- Employee morale expense
- Legal fees
- Marketing costs

You can find audit information, ICE formats, the DCAA Report to Congress, and much more at www.dcaa.mil

DCAA AUDIT OBJECTIVES

First and foremost, DCAA wants to ensure that costs are reasonable and that the contractor is following the FAR and that corporate policies follow GAAP. The costs in your accounting system will need to be supported by adequate documentation. Accounting systems like Unanet empower firms to satisfy DCAA's demands for data and support by providing comprehensive reports and all the information required to support preparation of the ICS, insertion of data into the ICE Model, and the audit when and if it occurs.

Make sure that during the audit you provide pertinent documentation to DCAA as they request it. One helpful tip is to make sure you review the audit plan and do upfront research on the DCAA Contract Audit Manual (CAM). Keep in mind that if you don't provide backup,

you can be sure that cost will be questioned. Gathering documentation in advance is helpful to both you and the audit team.

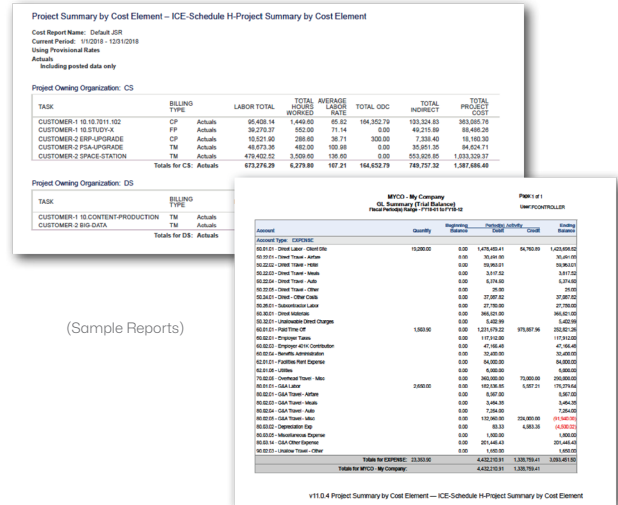
Supplemental documentation such as financial statements, org charts, 10K submissions (for public companies), audit plans, and other pertinent documents may also be requested and can help facilitate the overall flow and results of the audit. A sample documentation checklist is included below:

Document	Complete
GL Detail Statement of Indirect	<input type="radio"/>
Statement of Indirect Expenses	<input type="radio"/>
Trial Balance	<input type="radio"/>
Payroll Reconciliation	<input type="radio"/>
Job Cost Reports	<input type="radio"/>
Revenue by Contract Type	<input type="radio"/>
List of Applicable Contracts	<input type="radio"/>
Tax Returns	<input type="radio"/>
Policies and Procedures	<input type="radio"/>
Last Invoice for Applicable Contracts	<input type="radio"/>
Contract Briefs	<input type="radio"/>

Using a risk-based approach, DCAA closes incurred cost submissions in several ways. It conducts audits on high risk submissions and a sample of low risk submissions. For low risk submissions not audited, the Agency provides valuable assistance to contracting officers by issuing low risk memos. Because DCAA has the authority to establish final indirect rates, contracting officers may be able to avoid negotiations and go straight to closing out contracts using the rates established in these memos.

HOW UNANET HELPS YOU PREPARE YOUR ICE

Make sure that the trial balance is correct and that all unallowable costs have been removed. Use the Unanet step-by-step procedure to populate the schedules. Unanet can get you all of the needed reports and information.



After you have gone through the step-by-step process that Unanet provides, one quick check is to go tab by tab on the schedules and make sure the numbers tie from schedule to schedule.

The ICE form is Excel, so be sure you validate the spreadsheet (formulas, links, etc) after the data insertion is complete to ensure the schedules still tie to each other. The ICE model is complex and the formulas and links are notoriously easy to “break.” Also, make sure you have completed all the mandatory schedules and that the proper signatures have been obtained (sign and date Schedule N).

As you populate the worksheets, make sure you save all of the back-up information so that you can support where the numbers came from at audit time. Keep that backup until the audit is complete. Pull DCAA’s checklist and make sure you are complete.

WHAT HAPPENS WHEN THE AUDIT IS COMPLETE?

Once the audit is complete, billing adjustments “under/over” should be submitted for payment using the final indirect rates. Those final indirect rates are effective for the entire fiscal period covered by the ICS.

Completed contracts should be noted in your accounting system as soon as they are physically complete, noted in the ICS as such, and closeout should begin as soon as the rates are final for the last year of performance.

NEXT STEPS FOR THE FIRM: BECOME COMPLIANT-READY WITH UNANET

The accounting, timekeeping, and expense solution you use has a direct bearing on the success you have in overall compliance today and in the future. It will also set the stage for your company's success when under audit.

Unanet's integrated, real-time, project based ERP system in conjunction with your policies, procedures, practices, and qualified personnel will ensure that you can meet the requirements of the government's regulation and satisfy DCAA's demands for data and information when it's time for an audit.

If you would like to learn more about how Unanet can help you best prepare, please join us at one of our upcoming product demonstrations or an upcoming webinar.



Unanet is a leading provider of ERP solutions purpose-built for Government Contractors, A/E, and Professional Services. More than 3,600 project-driven organizations depend on Unanet to turn their information into actionable insights, drive better decision-making, and nurture business growth.



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