



# Accounting for Government Contracting

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# Agenda

- ▲ **Approved Accounting System**
- ▲ **Direct vs. Indirect Costs**
- ▲ **Government Audits**
- ▲ **Current Matters Update**



# Rhonda Gaydos – Consultant Government Contract Services Group

- ▲ Rhonda Gaydos is a consultant in Aronson & Company's Government Contract Services Group. She specializes in accounting and financial compliance issues impacting government contractors. She has a broad based background in generally accepted accounting principles and cost principles related to government contractors including the FAR and CAS. Rhonda is a licensed CPA in the State of Virginia.



# Approved Accounting System



# What is an Approved Accounting System

**A government contractor's accounting system that:**

- ▶ **Is adequate for accumulating and billing costs on Government contracts.**
- ▶ **Can record, process, summarize and report in a manner consistent with Government contract laws and regulations.**



# Basic Attributes of a Contractor's Accounting System

- ▲ Segregation of direct costs from indirect costs.
- ▲ Identification and accumulation of direct costs by contract.
- ▲ Exclusion of Unallowable Costs from direct & indirect expenses.
- ▲ Allocation method for indirect expenses.
- ▲ Accounting system in operation.
- ▲ Posts contract costs at least monthly to books of account.



# Basic Attributes of a Contractor's Accounting System

- ▲ **Ability to prepare billings of direct costs directly from the system, excluding unallowable costs.**
- ▲ **Adequate and Reliable Data.**
- ▲ **In accordance with GAAP - Have or intend to have an accrual basis accounting system.**
- ▲ **A timekeeping policy.**



# Direct vs. Indirect Costs



# Direct vs. Indirect Costs?

## Direct Costs

- ▶ **Costs that can be specifically identified with a contract.**

## Indirect Costs

- ▶ **Costs that can not be specifically identified with a contract.**

**Cost must be segregated, grouped, and accumulated separately.**



# Types of Direct Costs

**Direct costs specifically identified with a contract:**

- ▶ **Labor**
- ▶ **Travel**
- ▶ **Materials**



# Accounting for Direct Costs

## Accumulate costs by contract

- ▶ Level of detail consistent with that used in its proposal.
- ▶ Record keeping meets contract requirements.



# Types of Indirect Costs

## Fringe benefits:

- ▶ **Expense incurred to benefit company employees:**
  - ▶ Leave
  - ▶ Employer payroll taxes
  - ▶ Employee insurance coverage
  - ▶ 401K match
  - ▶ Tuition reimbursement

# Types of Indirect Costs

## Overhead:

- ▶ **Expenses incurred in support of contacts and the direct labor employees.**
  - Bonuses, Rent, Training

## General & Administrative (G&A):

- ▶ **Expenses incurred for the benefit of the entire company**
  - Bonuses, Rent, Training, for Admin. employees
  - General Liability, Licenses, Accounting, Executive Management



# Direct vs. Indirect Labor

## Direct Labor

- ▶ Labor cost specifically identified to a contract.

## Indirect Labor

- ▶ Labor of employees, who normally charge direct on a contract, incurred for non-direct functions, such as a company meeting or training.
- ▶ Contract Administration
- ▶ Accounting
- ▶ Human Resources
- ▶ Executive Management



# Allocation of Indirect Costs

**Indirect costs are accumulated in groups/pools and allocated based on benefit.**

- ▶ **Fringe – Total Labor**
- ▶ **Overhead – Direct Labor**
- ▶ **G&A – Total Costs**

**Descriptions of the contents of pools and bases should be documented.**



# Timekeeping

- ▲ **Employees must be properly trained and informed on how to fill out their timesheets.**
- ▲ **Every employee must know their Labor Codes and Project Numbers to charge both direct and indirect.**
- ▲ **Record time daily.**
- ▲ **Employees must properly document any changes.**
- ▲ **Timesheets - completed & signed by the employee.**
- ▲ **An approval system must be in place.**
- ▲ **Employers should perform internal checks to ensure the timesheets are being completed properly.**



# Unallowable Costs

**A cost that can not be included as either a direct or indirect cost.**

- ▶ **Expressly unallowable or mutually agreed.**
- ▶ **Must be segregated from direct and indirect costs in records.**
- ▶ **Subject to penalty clause if unallowable costs are included in final indirect cost settlement proposals.**



# Unallowable Costs

## Expressly unallowable costs:

- ▶ **Alcoholic Beverages**
- ▶ **Interest**
- ▶ **Entertainment**
- ▶ **Fines and penalties**
- ▶ **Bad Debts**
- ▶ **Political Contributions**

# Determining Allowability

## Factors to consider:

- ▶ Reasonableness
- ▶ Allocability
- ▶ Specific cost principles

# Reasonableness



## A cost is Reasonable if:

- ▶ In its nature and amount, it does not exceed that which would be incurred by a prudent person in the conduct of competitive business.
- ▶ It is generally recognized as ordinary and necessary for the contractor's business or the contract performance.
- ▶ It is incurred through the use of generally accepted sound business practices for the purpose of fulfilling contractor's responsibilities to the government.

# Allocability

## A cost is Allocable if:

- ▶ It is incurred specifically for the contract.
- ▶ It is assignable or chargeable to one or more cost objectives on the basis of relative benefits received.
- ▶ Cost benefits both the contract and other work, and can be distributed to them in reasonable proportion to the benefits received
- ▶ Cost is necessary to the overall operation of the business, although a direct relationship to any particular cost objective cannot be shown.



# Government Audits



# Pre-award Survey Audit

- ▲ **Performed by Defense Contract Audit Agency, DCAA.**
- ▲ **Performed at either a major or non-major contractor before contract award.**
- ▲ **Requested by the Contracting Officer.**
- ▲ **Determines if the design of the contractor's system acceptable for the award of the prospective Government contract.**



# Post Contract Award Audit

- ▲ **Performed after the contract has been awarded.**
- ▲ **A follow up procedure to a pre-audit survey.**
- ▲ **May be conducted if no pre-award survey was performed.**
- ▲ **Need is determined by level of audit risk.**



# Consequences of having a Noncompliant System

## Withholding of payments by the Government

- ▶ Lose contract award.
- ▶ Reduction in scope of the original award.
- ▶ Frequent audits.
- ▶ Worse case – Barred from doing business with the Federal Government.



# Current Matters Update



# E-Verify

- ▲ **Requires federal contractors and subcontractors to utilize the Dept. of Homeland Security's program to verify the employment eligibility of new hires and employees assigned to federal contracts.**
- ▲ **Federal Government contracts awarded after June 30, 2009.**
  - ▶ **Contract valued \$100,000 or more.**
  - ▶ **Period of performance exceeding 120 days.**
  - ▶ **FAR 52.222-54**



## **E-Verify** (continue)

- ▲ **Enroll in E-Verify within 30 days after contract award.**
- ▲ **Begin using within 90 days of enrollment.**
- ▲ **Verify the employment status of all existing employees within 30 days of assignment to the covered contract.**
- ▲ **Verify new hire within three days from their date of hire.**

# Code of Ethics and Business Conduct



- ▲ **All Contractors that receive a Federal Government contract valued at \$5 million or more with a period of performance exceeding 120 days must:**
  - ▶ Display fraud hotline posters at the worksite.
  - ▶ Develop and distribute a Code of Ethics and Business Conduct to all employees.
  - ▶ Promote compliance with the code of conduct .
  - ▶ Disclose any violations of Federal law relating to Government contracting to the CO & agency IG when there is credible evidence that such a violation has occurred.

# Code of Ethics and Business Conduct

(continue)



- ▲ **Large Businesses must further:**
  - ▶ Provide compliance training to all employees.
  - ▶ Adopt a set of prescribed internal controls.



# Need Additional Information

**For more information about Aronson & Company's  
Government Contract Solutions Group**

**Please contact:**

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