

Positioning for a Win – Accounting System Reviews

The Defense Contract Audit Agency (DCAA) has been under fire since mid-2008 when a Government Accountability Office (GAO) report was issued that was extremely critical of the DCAA's independence and general competency. This was closely followed in September by a Senate hearing in which the Agency was berated mercilessly.

The DCAA reacted by becoming decidedly insular and “cracking down” on all sorts of perceived compliance issues. While it worked to improve compliance with Generally Accepted Government Auditing Standards (GAGAS), it also raised the bar for contractor compliance to the point that systems had to be effectively perfect or the DCAA would find them unacceptable for use on Government contracts. In addition, they would recommend that the company's ACO disapprove the system and suspend payments to the contractor. Whether the ACO disapproved the system or not, the DCAA began inserting a statement in subsequent audit reports (including proposal reviews) stating that the contractor's system had been found deficient.

One of the first effects of the DCAA's new policies was a rash of recommendations for disapproval of contractor accounting systems and suspension of payments. The reaction of the ACOs was inconsistent, to say the least. Some contractors received letters disapproving their systems, but no withholding of payments. Others found their payments suspended across the board and cash flow effectively reduced to zero. With the DCAA holding their very survival hostage, some contractors were reduced to begging for a review of corrective actions. Whether payments were affected or not, many contractors found themselves ineligible for awards under the terms of solicitations requiring “evidence of a Government-approved accounting system.” Others had previous approved accounting system letters greater than three years old, at which point they were rendered expired and became useless.

Major Government contractors have largely resolved these issues and regained an “approved” system status. Many of them have resident auditors whose full-time job it is to monitor the contractor's system.

Many small and mid-size contractors find themselves in a “catch-22” position. Their contract volume is not enough to make examination of their systems or proposed corrective actions a priority for the DCAA. Nor is it attractive for the ACO to use its shrinking budgets to pay for a DCAA examination.

Not surprisingly, some small and mid-size firms have begun to look for alternatives to approval by the DCAA. At the same time, some solicitations now include a provision specifically allowing the offeror to submit an opinion on system adequacy from an independent CPA firm.

At Watkins Meegan, we have conducted a number of such system examinations. We use the same audit programs that the DCAA would use for the review and execute the same form – a Standard Form 1408, Pre-Award Survey of Prospective Contractor Accounting System. And, we have been very successful in having our review of the contractors' system accepted by the Government in the pre-award solicitation process. Many clients feel this proactive approach is a strategic business decision designed to set them apart from their competition in the proposal process.