Is Your G&A Base Right for You?

Presented By:

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<thead>
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<th>Agenda</th>
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<tr>
<td><strong>Who</strong></td>
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WHAT
(is in the G&A pool and the G&A base?)
Cost Accounting Standard 410

Allocation of business unit general & administrative expenses to final cost objectives

Three objectives:

• Criteria for allocating G&A expenses to final cost objectives
• Guidelines for types of expenses in G&A pool
• Requires G&A expenses to be allocated on a Cost Input base representing the total activity of the company
But I’m NOT CAS COVERED!

CAS 410 does not only apply to CAS-covered contractors

FAR 31.203 Indirect Expenses states “CAS provisions for this section apply”

(a) For contracts subject to full CAS coverage, allocation of indirect costs shall be based on the applicable provisions. For all other contracts, the applicable CAS provisions in paragraphs (b) through (h) of this section apply.
Definition of G&A Expenses

G&A expenses must be incurred for managing and administering the whole business unit.

Definition can be found in:

- Federal Acquisition Regulation (FAR)
- Defense Contract Audit Manual (DCAM)
- Cost Accounting Standards (CAS)
- DCAA’s Information for Contractors
  - DCAA.mil or GovCon360.com
A Practical Guide to G&A Expenses

Executive management (CEO, CFO, COO, EIEIO) and associate costs
Finance, accounting and treasury functions – may also include payroll, timekeeping, etc.
Corporate administrative functions – may also include Contract Administration, IT, HR
Business licenses, State income taxes, legal fees, audit fees, Directors’ expenses and fees
The G&A Pool According to CAS 410

Management expenses more directly measured by another base should not be in the G&A pool

program management
procurement
subcontract administration

Immaterial expenses which are not G&A may be included in the G&A pool
The G&A Pool According to CAS 410

The G&A pool may be combined with other expenses allocated to final cost objectives if ...

– the base for the combined pool is appropriate for allocating both the G&A expense pool and the other expenses, and

– the individual and total expenses of the G&A expense pool can be identified separately from the other expenses.
The G&A Pool According to CAS 410

“Selling costs” may be accounted for in the G&A pool or in a separate pool, but...

- A separate pool is required if another base is more equitable
- Commissions are always subject to additional scrutiny
The G&A Pool According to CAS 410

Home Office costs may or may not be G&A...

Three types of Home Office expense

Direct
Centrallized
Residual
The G&A Base According to CAS 410

The base used to allocate the G&A pool must include all significant elements which represent the total activity of the business unit.

Acceptable bases are...

- **TOTAL** cost input
- **VALUE ADDED** cost input
- **SINGLE ELEMENT** cost input

Modified bases are not permitted.
The G&A Base According to FAR

**FAR 31.203(d)** - When a cost input base is used for the allocation of G&A costs, the contractor shall include all items that would properly be part of the cost input base, whether *allowable* or *unallowable*, and these items shall bear their pro rata share of G&A costs.

Unallowable indirect costs (fringe and overhead) must be removed from their respective pool, but remain in the G&A base.
The TOTAL Cost Input Base

The Total Cost Input base is made up of “total direct and indirect costs, except G&A”

The exceptions are:

- Statutory costs are never allowable (Fed Inc Tax, bad debt, interest, etc.)
- Unallowable G&A (exec comp, G&A travel over per diem limits, etc.)

Unallowable G&A (and all statutory unallowable costs) are removed from the G&A pool

A total cost input base is generally acceptable...
The VALUE ADDED Cost Input Base

The value-added cost input base is defined as total cost input less material and subcontract costs.

To be used where inclusion of material and subcontract costs would significantly distort the allocation of the G&A pool:

- Costs deducted to determine the value-added base should be limited to direct material and subcontracts.
- Subcontracts that supplement the workforce and are interchangeable with regular employees do not fit the definition of “services to be performed by other than the contractor” and should not be excluded from the base.
The SINGLE ELEMENT Cost Input Base

The criteria for use of a single-element base are very specific

A Single Element base may be used when a contractor can demonstrate that...

- it best represents the total activity of a business unit, and
- It produces equitable results

Example – direct labor dollars may be used when they are significant and other measures of activity are less significant related to total activity.
Which Base is Best?

Selection of the best base involves judgments on whether inclusion of certain costs causes "distortions" in allocations. (DCAM)

In Ford Aerospace and Communications Corporation, Aeronutronic Division, Case No. 23833, the ASBCA ruled there is no preferred allocation base to distribute G&A expenses other than the one which best represents total activity.
WHERE
(do you find the rules about G&A?)
FAR on the G&A Pool and Base

FAR 2.101 – Definitions (G&A Expense)
FAR 31.001 – Definitions (Cost Input)
FAR 31.203 – Indirect Costs (Allocations)
FAR 31.205-18 – Independent Research and Development and Bid and Proposal Costs (Concomitant allocation with G&A)
FAR 52.216-7 – Allowable Cost and Payment (Requirement for schedule of G&A Expenses in ICS)
CAS on the G&A Pool and Base

48 CFR 9904-410 (CAS 410)
- 410 - 30 – Definitions (cost input, G&A expense, segment)
- 410 - 40 – Fundamental Requirements (grouping, base selection, immaterial costs)
- 410 - 50 – Techniques for Application (inclusions, exclusions, selection of base)
DCAM on the G&A Pool and Base

Defense Contract Audit Manual, Chapter 8 (CAS), Subchapter 410 (CAS 410) - Allocation of Business Unit General and Administrative Expenses to Final Cost Objectives

– Discussion of base selection
– Instructions to auditors on examination of bases for possible distortion of allocations
DCAA “Information for Contractors”

Chapter 6, Incurred Cost Proposals, Section 10, G&A Expenses –

– Short list of generally accepted G&A costs
– Specification of the acceptable allocation bases (TCI, VA or SE, regardless of CAS applicability)
WHO
(uses the different G&A bases?)
The Total Cost Input Base

According to Deltek’s 2010 CLARITY study...

- Among companies with less than $20M in revenues, more than 5 out of 6 firms used the TCI base
- Among companies with more than @25M in revenues, about 2 out of 3 firms used the TCI base

In general, firms that perform most of their own contracts and subcontract out relatively little work tend to use the Total Cost Input base
The Value Added Cost Input Base

According to that same study...

– Among companies with less than $20M in revenues, fewer than 1 out of 6 firms (≈16%) used the VA base

– Among companies over $20M in revenues, ≈1 in 3 firms (≈33%) used VA base

In general, firms that serve as the prime for teams and subcontract out relatively more of their work tend to use the Value Added base
The Single Element Cost Input Base

Despite more than 250 participants in Deltek’s 2010 CLARITY study, not one firm reported using the Single Element Base

– Use of the SE base requires almost completely homogeneous work
– Typical SE firms have little or NO subcontracting or materials (usually pure consulting firms)
WHY
(use one base over another?)
Peer Pressure

Total Cost Input is conventional (especially among small firms)

– There is strength in numbers
– Familiarity to DCAA virtually assures acceptance
– “The highest blade of grass is the first to be cut by the scythe” *(Japanese proverb)*
– “OK, now you got my attention!” *(Dad, and not a good thing)*
Competitive Pressure

Use of the VA base LOWERS the burden on subcontract

– When the discussion turns to “who will Prime,” the team member with the VA base has an advantage
– When the competition turns to LPTA, VA vs. TCI can be the difference in winning and losing for a team

CAUTION: G&A is a “zero sum” game

– If burden on subs goes DOWN, G&A on everything else goes UP
An Example “By the Numbers”

<table>
<thead>
<tr>
<th>Costs</th>
<th>G&amp;A Base</th>
<th>G&amp;A Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct Labor</td>
<td>Costs: 1,000</td>
<td></td>
</tr>
<tr>
<td>Fringe/OH</td>
<td>Costs: 600</td>
<td>Single Element Cost Input: 30.00%</td>
</tr>
<tr>
<td>Subtotal</td>
<td>Costs: 1,600</td>
<td>Value Added Cost Input: 18.75%</td>
</tr>
<tr>
<td>Material</td>
<td>Costs: 400</td>
<td></td>
</tr>
<tr>
<td>Subcontracts</td>
<td>Costs: 1,000</td>
<td>Total Cost Input: 10.00%</td>
</tr>
<tr>
<td>Subtotal</td>
<td>Costs: 3,000</td>
<td></td>
</tr>
<tr>
<td>G&amp;A Expense</td>
<td>Costs: 300</td>
<td></td>
</tr>
<tr>
<td>Total Cost</td>
<td>Costs: 3,300</td>
<td></td>
</tr>
</tbody>
</table>
An Example “By the Numbers”

<table>
<thead>
<tr>
<th></th>
<th>w/ SE Base</th>
<th>w/ VA Base</th>
<th>w/ TC Base</th>
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<tr>
<td><strong>Direct Labor</strong></td>
<td>500</td>
<td>500</td>
<td>500</td>
</tr>
<tr>
<td><strong>Fringe/OH</strong></td>
<td>300</td>
<td>300</td>
<td>300</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td>800</td>
<td>800</td>
<td>800</td>
</tr>
<tr>
<td><strong>Material</strong></td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Subcontracts</strong></td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
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<td><strong>Subtotal</strong></td>
<td>800</td>
<td>800</td>
<td>800</td>
</tr>
<tr>
<td><strong>G&amp;A Expense</strong></td>
<td>150</td>
<td>150</td>
<td>80</td>
</tr>
<tr>
<td><strong>Total Cost</strong></td>
<td>950</td>
<td>950</td>
<td>880</td>
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An Example “By the Numbers”

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<tr>
<td><strong>Subtotal</strong></td>
<td>800</td>
<td>800</td>
<td>800</td>
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<tr>
<td><strong>Material</strong></td>
<td>400</td>
<td>400</td>
<td>400</td>
</tr>
<tr>
<td><strong>Subcontracts</strong></td>
<td>1,000</td>
<td>1,000</td>
<td>1,000</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td>2,200</td>
<td>2,200</td>
<td>2,200</td>
</tr>
<tr>
<td><strong>G&amp;A Expense</strong></td>
<td>150</td>
<td>150</td>
<td>220</td>
</tr>
<tr>
<td><strong>Total Cost</strong></td>
<td>2,350</td>
<td>2,350</td>
<td>2,420</td>
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An Example “By the Numbers”

### UCI Portfolio Comparison

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<th>w/ VA Base</th>
<th>w/ TC Base</th>
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<tbody>
<tr>
<td>No Mat'ls/Subs</td>
<td>950</td>
<td>950</td>
<td>880</td>
</tr>
<tr>
<td>BIG Mat'ls/Subs</td>
<td>2,350</td>
<td>2,350</td>
<td>2,420</td>
</tr>
<tr>
<td>Total Cost</td>
<td>3,300</td>
<td>3,300</td>
<td>3,300</td>
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</table>
Regulatory Pressure

The DCAM cautions auditors to look for evidence of distortion of allocations (of all kinds) in EVERY audit, but especially in indirect cost claims

– Auditors will (occasionally) recommend a change from one base to the other (usually TCI to VA)

– Auditors will (rarely) report a non-compliance with CAS 401, 402, 410 or 418 if distortions are blatant
Regulatory Pressure

When sub content is high, the prime is exposed to potential unallowable costs under FAR 31.203(i), “Excessive Pass-Through Costs” (G&A on subs)

The implementing clause at FAR 52.215-23 can result in disallowed G&A on subs, but specifically recognizes the allowability of “charges for the costs of managing subcontracts and any applicable indirect costs and associated profit/fee based on such costs”
Flexibility

VA is inherently more flexible than TCI

– Remember those “body shop” subs?
– Materials to which you add value?

Judgment calls are permitted in cost classification

Judgment calls are *required* in cost classification

Documentation is *critical*
WHEN
(should you consider a change?)
Business Conditions

Future business forecasts include prime/sub teams (you want to be prime)
- TCI to VA change is easier BEFORE the work is in place
- Future business forecasts or proposals in process (or even planned) justify change

LPTA is around the corner

Large recompetes susceptible to teaming coming up
Timing of a change

Changes in the G&A base MUST be made on a fiscal year boundary
  – There are exceptions to everything, but this one is nearly universal
  – Nature of the change irrelevant

*Declaring* the change at the beginning of a year may be sufficient
  – Subs to be included in base of a S/MH rate don’t have to exist... Yet.
  – A win does not constitute the change, the declaration does
Summary

The cost of awarding, administering and managing subs can be part of the G&A pool (TCI) or a separate pool (VA base with a SMH rate for mat’l/subs)

Both work, both have pro’s and con’s

Regulatory pressure, intended or not, is toward the Value Added base

– Competitive pressures (being the prime)
– Regulatory pressures (IDIQ vehicles and pass-through costs)
<table>
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<tr>
<th>Summary</th>
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<tbody>
<tr>
<td>Making the change is complex, but manageable</td>
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<tr>
<td>We can help.</td>
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Questions?
Contact Us

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