



# Audit Preparations

Presented By:  
Daryl Zahn, CFCM, President, NCMA-Wisconsin Chapter

Manager, Contracts & Compliance, DRS Power & Control Technologies, Inc.

# Federal Contracting: Audits:

- Comptroller General of the United States, Government Auditing Standards. Chapter 2: Types of Government Audits
  - 2.2: All audits begin with objectives, and those objectives determine the type of audit to be conducted and the audit standards to be followed. The types of audits, as defined by their objectives, are classified in these standards as **financial audits** or **performance audits**.
  - 2.3 Audits may have a combination of financial and performance audit objectives or may have objectives limited to only some aspects of one audit type.
- Financial audits include financial statement and financial related audits.
- A performance audit is an objective and systematic examination of evidence for the purpose of providing an independent assessment of the performance of a government organization, program, activity, or function

# Why would a Contractor be audited?

- Review Basis of estimates in preparation negotiation.
- Ensure compliance with the Federal Regulations on business practices and accounting practices
- Ensure compliance to product specifications.

# Types of Auditors: Sampling

- Government Accountability Office
  - Audits Federal Agencies
- Department of Labor:
- OSHA
- Department of Defense:
  - DCAA: Defense Contract Audit Agency – Related mostly to Accounting/Financial activity
  - DCMA: Defense Contract Management Agency – Related to Contract Management activity
- Other Federal Agencies
  - May have their own auditors
  - May subcontract with outside firms to perform audits
- Prime Contractors:
  - Often will have their own audit personnel for financial or process related requirement flowdowns.

**This presentation will focus mainly on DoD related audits and audit agencies, and dealings directly between Government and Prime contractor, but the concepts of preparing for an audit should translate well to any audit.**

# Who Audits What: DCAA Audits

- Audit Services
  - Preaward Audits
    - Price Proposals
    - Preaward Surveys – System adequacy
    - Forward Pricing Labor & Overhead Rates
  - Postaward Audits
    - Incurred Cost/Annual Overhead Rates
    - Floor Check
    - Truth in Negotiation Act Compliance
    - CAS Compliance & Adequacy
    - Claims
  - Contractor Business System Audits
    - Accounting
    - Estimating
    - electronic Data Processing
    - Billing
      - Floor check for time keeping is an example of a specific audit
    - Material Management

# Who Audits What: DCMA Audits

- Cost & Pricing
  - DCMA provides Preaward cost audits for proposals below certain thresholds.
- Compliance
  - Quality Assurance Specialists
    - Contract product inspection and Acceptance
  - Government Property
  - Regulation Compliance
  - Contractor Purchasing System Review

# DCAA Pre Award / Post Award

- A Pre-award system audit is meant to confirm that a system (i.e. accounting system) CAN perform as required
- A Post-award system audit tests if the system DOES perform as required. i.e. DOES the accounting system segregate and accumulate direct and indirect costs to the correct cost objective every time?

# DCAA: Helpful documents

- DCAA: Information For Contractors:
  - [http://www.dcaa.mil/DCAAM\\_7641.90.pdf](http://www.dcaa.mil/DCAAM_7641.90.pdf)
- DCAA: Contract Audit Manual is online and available to everyone to allow common understanding of what DCAA will be reviewing in audits:
  - <http://www.dcaa.mil/cam.html>

# DCMA Audits: Main Focus

- Monitor contractor performance
  - Cost
  - Schedule
  - Product Performance
- Provide in-plant representatives for the military as well as other Federal buying agencies
- Contract Closeouts

# Proposal Audits

- DCAA
  - Directed to perform field Pricing Audits only on Cost Type proposals over \$100 Million and Fixed Price proposals over \$10 Million
    - Chapter 3 of DCAA's Information for Contractors Guide provides guidance on proposal requirements and audit evaluations
    - DCAA will look at indirect rates being applied and how they are computed.
    - Looking to see trends and budgetary data, along with explanations to support reasonableness of estimates and price build up.
- DCMA
  - Directed to perform field pricing audits for proposals below the thresholds noted above.

# DCAA Audits

- Provisional Billing Rates
  - FAR 42.704 – applied for billing purposes (not the same as Forward Pricing rates which are related to proposals)
  - Allow for interim reimbursement during contract performance (non FFP efforts)
- Incurred Cost Proposals
  - FAR 52.216-7 Allowable Cost and Payment Clause

# DCMA Audits

- Government Property: FAR 45
- Contractor Purchasing System Review: DFARS 252.244
- Contractor Surveillance:
  - Product compliance
    - Product to specifications
  - Process & Procedures
    - Includes 'paperwork' related items
      - compliance with component certifications,
      - testing
      - Preservation, Packing, Packaging and Marking (PPP&M)
      - Flowdowns to Sub-vendors
      - etc.

# Preparing for DCAA Audit: Best Practices

Taken from NCMA Webinar – Dated June 26, 2012

Presented by: Beverly Arviso, CPA, Fell, CPCM, CFCM: Arviso, Inc.

- **DON'T PANIC**
- Inquire as to the purpose of the visit, e.g., what type(s) of audit they are performing
- Ask for an entrance conference and a list of items you can prepare in advance of the visit
  - 12/15/10 – DCAA is required to provide a notification letter to the contractor during the planning phase of the audit on the nature and scope of the audit, either during or shortly after the entrance conference
  - The notification letter is not supposed to replace the entrance conference

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- Request or download and review the audit program from [www.dcaa.mil](http://www.dcaa.mil)
- Understand what the auditor is asking for and control responses
- Ask why the auditor is requesting data if you are uncertain of the purpose
- Maintain good records and documentation
- Request interim audit results to mitigate potential negative comments/results

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- Get your “house” in order before the audit
  - Accounting System
  - Estimating System
  - Budgeting and Forecasting
  - Timekeeping
  - Travel & Expense
  - Purchasing
  - Education and Training of employees
  - Analyze key accounts

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- Request an exit conference
- Respond to draft reports quickly and obtain outside assistance as needed
- Respond accurately and quickly, but not so quickly as to jeopardize your preparation and audit success
- Request a copy of the final audit report for your records

# Preparing for an audit:

Suggestions noted on Website of Kline & Company, CPA PC

<http://www.klineco.com/WP-DCAA-audit-preparation.php>

- Review the auditor notification that an audit will be performed;
- Ensure you have an understanding of what the auditor will accomplish (subject of the audit) and their request for books, records, reports, operations data, and management assertions;
- Ask for clarification where you have questions;
- If the contractor has no prior audit history with the DCAA, the auditor will have increased preliminary documentation requirements (for the auditor to assess the level of audit risk);
- Try to meet the auditor's schedule for the entrance conference and/or initiation of the audit (at small contractors, the entrance conference and initiation of the audit may be on the same day);
- Do not agree to an onsite visit date when you cannot effectively support the needs of the auditor (contractor personnel with knowledge of the subject under audit must be available);
- Make arrangements for necessary work space; and
- Depending on the audit purpose you may need the following data: Company Financial Statements, historical incurred cost from the general ledger, data related to Cost Proposals such as estimates or indirect rate calculations, employee handbooks and Accounting Policy and Procedure.

# Preparing for Audits of whatever: Obvious Observations of the Obvious

- Know and Understand requirements
- Maintain Discipline of Good Practices
- Train Employees
- Perform self audits
- Document, Document, Document

DOING THING CORRECTLY IN THE FIRST PLACE REDUCES RISK OF  
AUDIT FINDINGS THAT THINGS ARE NOT DONE CORRECTLY!

# Questions?

- Thank you for your attention!