



DEFENSE CONTRACT AUDIT AGENCY
DEPARTMENT OF DEFENSE
8725 JOHN J. KINGMAN ROAD, SUITE 2135
FORT BELVOIR, VA 22060-6219

IN REPLY REFER TO

PPD 730.5.35.1

May 22, 2014
14-PPD-008(R)

MEMORANDUM FOR REGIONAL DIRECTORS, DCAA
HEADS OF PRINCIPAL STAFF ELEMENTS, HQ, DCAA

SUBJECT: Audit Alert on Labor Qualifications for Time and Material Contracts

The purpose of this audit alert is to provide additional information for auditors to consider when they identify employees performing on Time and Material (T&M) contracts who do not meet the labor qualifications set forth in the contract.

Background

MRD 07-PPD-038(R), dated November 26, 2007, discussed the fact that auditors should question costs on Time and Material (T&M) contracts related to labor hours for employees who do not meet the labor qualifications set forth in the contract. The basis for questioning the costs is the T&M payments clause, specifically FAR 52.232-7(a)(3), which states in relevant part:

Labor hours incurred to perform tasks for which labor qualifications were specified in the contract will not be paid to the extent the work is performed by employees that do not meet the qualifications specified in the contract, unless specifically authorized by the Contracting Officer.

Coordination before Questioning

Based on the specific wording in FAR 52.232-7(a)(3), our audit reports must question the labor hours incurred to perform tasks for which labor qualifications were specified in the contract if employees who performed the work did not meet the qualifications specified in the contract, **unless specifically authorized by the Contracting Officer**. Therefore, prior to questioning the hours, the audit team should coordinate with the Contractor and Contracting Officer to determine whether specific authorization has or will be given.

If Specific Authorization Has Been Given

If the Contracting Officer has given specific authorization, the audit team should include documentation of this authorization in the working papers and a non-compliance with FAR 52.232-7(a)(3) should not be cited in the report.

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If Specific Authorization Will Be Given

While FAR 52.232-7(a)(3) requires specific authorization, it does not require the Contracting Officer to provide that authorization prior to the delivery of the work. If the Contracting Officer did not give prior authorization, but is looking into whether specific authorization should be given, the audit team should provide the Contracting Officer with information such as the actual incurred cost of the labor delivered that did not meet the specified qualifications. If the Contracting Officer decides to provide after the fact authorization, the audit team should document this in the working papers and a non-compliance with FAR 52.232-7(a)(3) should not be cited in the report. Part of that documentation should be a written authorization from the Contracting Officer to the Contractor (e.g., an e-mail to the contractor's contract/program manager specifically stating what work performed by employees who did not meet the qualifications specified in the contract is now being authorized for payment).

If Specific Authorization is Not Given

If the Contracting Officer does not give specific authorization, the costs should be questioned in the audit report as a non-compliance with FAR 52.232-7(a)(3). However, in many cases, the contracting officer is not going to withhold payment of all labor costs when an employee does not meet the labor qualifications if the work delivered did adequately complete the scope of work. In these cases, the contracting officer will need to modify the contract for a new rate or contract line item to reimburse the costs. Auditors should assist the contracting officer to help in arriving at a rate that is more appropriate than the rate charged by the contractor (e.g., a rate based on the fully burdened rate of pay for the unqualified employee, or the labor category where that employee truly fits). In order to ensure a timely refund of the money owed to the Government, the auditor should prepare a Form 1 (be sure to consider billed amounts for years outside of the incurred cost year under audit).

Impact on Review of Vouchers

Additionally, when an audit team identifies during an incurred cost audit that a contractor claimed costs for employees who do not meet the specific labor qualifications, the audit team should design procedures for their review of current billings and adjustment vouchers to ensure they are not currently billing for employees who do not meet specific labor qualifications.

Is the Contractor's Failure to Get Prior Authorization a Business System Deficiency?

If the contractor fails to get authorization in advance, auditors should consider whether a DFARS business system deficiency exists. If the audit team determines that the contractor has a material amount of T&M billings that include hours that do not meet the labor qualifications specified in the contract, a significant deficiency related to DFARS 252.242-7006(c)(12) should be reported. The contractor has failed to establish adequate internal controls to exclude from costs charged to Government contracts, amounts that are not allowable in terms of contract

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provisions in the FAR 52.232-7 T&M Payment Clause. An adequate accounting system would include procedures for a contractor to ensure that they get the Contracting Officer's specific authorization prior to the delivery and billing of hours that do not meet the qualifications specified in the contract.

Questions and Other Information

We added a step to the incurred cost audit program to discuss some of the information addressed in this audit alert, and we will include more detailed information in the Guidebook being issued in the near future. FAO personnel should direct questions to their regional points of contact, and regional personnel with questions should contact Policy Programs Division at (703)-767-2270 or by e-mail DCAA-PPD@dcaa.mil.

/Signed/
Donald J. McKenzie
Assistant Director
Policy and Plans

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