

MASTER AUDIT PROGRAM

Activity Code 19420	Compliance Audit CAS 420
B-1 Planning Considerations	Version 8.0, dated Jan 2023

Type of Service - Attestation Examination Engagement
Audit Specific Independence Determination
Members of the audit team and internal specialists consulting on this audit must complete the Audit Specific Independence Determination (WP 34) prior to starting any work on this assignment. <i>(Note: Because staff is sometimes added to on-going audits, supervisors should ensure that all individuals who are directing, performing audit procedures, or reporting on this audit as a member of the audit team who are performing as a consultant have signed this working paper. For example, an FAO may add additional auditors (e.g., technical specialists) to the audit assignment or may need to consult with an internal specialist (e.g., industrial engineers, and operations research specialists) as the audit progresses.)</i>

Purpose and Scope
1. The purpose of CAS compliance auditing is to determine if the contractor's policies, procedures, and practices used to estimate, accumulate, and report costs on Government contracts and subcontracts comply with the requirements of CAS. CAS 420 establishes criteria for the accumulation of IR&D/B&P costs and for the allocation of such costs to cost objectives. FAR 52.230-2, Cost Accounting Standards, requires the contractor to comply with the CAS 420 criteria (48 CFR 9904.420). FAR 31.205-18 makes CAS 420 partially applicable to all contracts even contracts which are not CAS covered or subject only to modified CAS coverage.
2. The scope of this audit should be limited to the last completed contractor fiscal year. For efficiency, CAS compliance testing, if possible, should be performed concurrently with tests for compliance with FAR and contract terms.
3. This program is intended to provide for the proper planning, performance, and reporting on the contractor's compliance with CAS 420. The audit steps in the program should reflect a documented understanding between the auditor, the technical specialist and/or the supervisor as to the scope required to comply in an efficient and effective manner with generally accepted auditing standards and DCAA objectives. The program steps are intended as general guidance and should be tailored as determined by audit risk.

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Other Planning Considerations

1. Before beginning any CAS compliance audit, the auditor should first determine the contractor is subject to the CAS coverage. If the standard is not applicable to the contractor, the audit should be cancelled.
2. Materiality (see 48 CFR 9903.305) and audit risk assessment are integral parts of the planning process and should be considered in developing the extent of CAS compliance tests.
3. Once it is determined that the standard is applicable, the auditor should assess which provisions of the standard are significant to the contractor; assess control risk; and the results of other relevant audits (e.g., results of prior compliance audits, Disclosure Statement examinations, etc.). The decision to not test whether the contractor is complying with specific provisions of the standard should be documented.
4. Prior to commencing the audit, review Agency guidance that may impact the audit and adjust the scope and procedures appropriately.

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B-1 Preliminary Steps	WP Reference
Version 8.0, dated Jan 2023	
1. Research and Planning	
<p>a. Read and become familiar with the criteria in CAS 420, Chapter 33 of the Selected Areas of Cost Guidebook, CAM 8-420, and any recent Headquarters guidance not incorporated in CAM.</p>	
<p>b. Evaluate applicable parts of the contractor’s Disclosure Statement (e.g., Parts II, III, IV and VIII) to become familiar with the disclosed accounting practices. Determine if the contractor’s accounting practices have remained unchanged since the last CAS 420 compliance audit. If changes have occurred, adjust the audit scope accordingly.</p>	
<p>c. Evaluate recent forward pricing or incurred cost proposals to determine whether total costs subject to CAS 420 are material. Consider contractor’s sales mix (i.e., CAS-covered Government contracts vs. non-CAS-covered and commercial). Materiality should be a consideration only in determining the extent of substantive testing.</p>	
<p>d. Examine other FAO permanent file data (e.g., relevant audit leads) and prior relevant audit work packages to determine what data are available, what audit steps were done in the past, and the results from those steps. This will identify areas of high risk and/or areas where limited or no compliance testing is necessary. Document results.</p>	
<p>e. Review permanent file to determine if previous audits included findings and recommendations that relate to the subject matter. If there were findings material to the subject matter, document this information in the risk assessment and perform the following procedures:</p> <ol style="list-style-type: none"> (1) Ask contractor management if corrective actions were taken to address findings and recommendations reported in previous DCAA audits (e.g., questioned costs, business system deficiencies, CAS audits) that are relevant to the subject matter of audit. If yes, have contractor explain corrective actions taken and determine if additional audit procedures should be included in the fieldwork to test the corrective actions. (GAGAS 7.13) (2) Document the results of the inquiry and the impact of the corrective actions to the subject matter. 	

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B-1 Preliminary Steps	WP Reference
<p>f. Review permanent file to determine if the contractor has previously provided other studies or audits (e.g., summary listing of internal audits or external audit reports) that directly relate to the subject matter. If there are no other studies or audits, document that information in the working papers and perform the procedures below.</p> <ol style="list-style-type: none"> (1) Ask contractor management if internal audits were performed. If yes, request contractor provide a summary listing of the internal audits that would assist us in understanding and evaluating the efficacy of the internal controls relevant to the subject matter of the audit. (2) If the review of the perm file or the contractor identifies relevant internal audits: <ul style="list-style-type: none"> • Determine if access to these reports is necessary to complete the evaluation of the relevant internal controls to support the risk assessment or audit procedures related to the subject matter of the audit. There must be a nexus between the internal audit reports and the scope of this specific assignment. • Document the results of the determination in writing. • If assignment is at a major contractor location, coordinate with the CAD or FAO point of contact (POC) for internal audit reports to request the contractor provide access to the reports. • If assignment is at a non-major contractor and the FAO does not have a designated POC, the auditor should request the contractor provide access to the internal audit reports. • The request should include information on how the internal audit report is relevant to the DCAA audit. Place a copy of the request in the assignment administrative working papers. (3) If the review of the perm file or the contractor identifies relevant other audits or studies: <ul style="list-style-type: none"> • Obtain publicly available information for the relevant other Government agency audits (e.g., websites for DoD IG or other IGs, service audit agencies, etc.). • Make appropriate adjustments to your risk assessment and planned procedures based on the reported findings. (4) Document the results of the inquiries including the response received from the contractor for any request for access to internal audit reports. (If access was not granted this should include the contractor’s rationale or justification for not granting access). (5) Determine if additional audit procedures are needed to respond to identified risk. 	
<p>g. If appropriate, coordinate with the FAO technical specialist, CAD, and/or regional specialist on matters of interpretation and policy.</p>	

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B-1 Preliminary Steps	WP Reference
h. Contact the contracting officer to ascertain any known concerns that will impact the audit and adjust the audit scope and procedures accordingly.	
i. Notify the appropriate contracting officer the commencement of the risk assessment and that the expected completion date will be provided in the formal acknowledgement/notification once the risk assessment is complete. The acknowledgement process should be performed in accordance with CAM 4-104.	
2. Entrance Conference	
a. Arrange and conduct an entrance conference covering the areas highlighted in CAM 4-302 with particular emphasis on:	
(1) Requesting the contractor's explanation of the internal control structure as related to CAS 420.	
(2) Any changes since the last audit.	
(3) The contractor's monitoring process for classifying costs.	
(4) Any identified weaknesses which may have been reported and related follow-up actions. If applicable, include a follow up with contractor management on: (a) corrective actions that address previous DCAA audit findings and recommendations, (b) other studies or audits that impact the subject matter.	
b. If relying on the work of others, follow the procedures in CAM 4-1000.	
c. Issue a notification letter to the contractor regarding the audit in accordance with CAM 4-302.3.	
3. Risk Assessment Steps	
a. Obtain and document an understanding of contractor internal controls relevant to the audit. Auditors may obtain a significant portion of this understanding during the walkthrough.	

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B-1 Preliminary Steps	WP Reference
<p>b. During the entrance conference, or other appropriate meeting, make specific inquiries of contractor management and other appropriate parties regarding the following:</p> <ol style="list-style-type: none"><li data-bbox="302 363 1224 468">(1) Their knowledge of any actual, suspected, or alleged fraud or noncompliance with laws and regulations affecting the period of time corresponding to the subject matter under audit. (AT-C 205.33)<li data-bbox="302 489 1203 632">(2) If any specialists (internal or external) were used in the preparation of the subject matter. If yes, have the contractor explain how the specialists were used in the preparation of the subject matter. (AT-C 205.16)<li data-bbox="302 653 1219 795">(3) Whether any investigations or legal proceedings, that are significant to the engagement objectives, have been initiated or are in process with respect to the period of time corresponding to the subject matter. (GAGAS 7.14)<li data-bbox="302 816 1224 984">(4) The existence of other audits and studies (performed by other than DCAA) that relate to the subject matter under audit. If yes, have the contractor explain the audits and studies performed, any related findings or recommendations, and any contractor corrective actions taken. (GAGAS 7.13) <p><i>Note: Specifically document in the working papers; the inquiries and the corresponding responses as well as how the responses affect the performance of the engagement.</i></p>	

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B-1 Preliminary Steps	WP Reference
<p>c. Based on the team's understanding of the criteria, subject matter, and the contractor and its environment, hold a planning meeting with the audit team (at a minimum, Supervisor and Auditor) to discuss and identify potential material noncompliances, whether due to error or fraud, that could affect the subject matter.</p> <p>The discussion should include:</p> <ul style="list-style-type: none"> • relevant prior audit experience (e.g., questioned cost, relevant reported accounting system deficiencies), • relevant aspects of the contractor and its environment, • risk of material noncompliance due to fraud (e.g., the extent of financial incentives, pressures to meet budgetary and contractual commitments, and opportunities to commit and conceal fraud). Consider the fraud risk factors and scenarios presented in the DoD OIG's webpage: Fraud Detection Resources for Auditors. Copy link and paste into web browser, • other known risk factors identified that could materially affect the subject matter, and <p>the audit team's understanding of relevant key internal controls.</p> <p>Document the factors identified that increase the risk of material noncompliance due to error or fraud that could affect the subject matter, and design audit procedures to respond to the increased risk of material noncompliance.</p>	
<p>Communication among audit team members should continue as needed throughout the audit regarding the risk of misstatement and noncompliance due to error or fraud.</p>	
<p>d. From the information gathered in the preceding steps and using the materiality criteria in 48 CFR 9903.305, assess the audit risk and determine the scope of audit and extent of compliance testing to be performed.</p>	
<p>e. Update the information in the permanent files as needed (MAAR 3)</p>	

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C-1 Accumulation of IR&D / B&P Costs by Project (MAAR 16)	WP Reference
Version 8.0, dated Jan 2023	
1. Analyze job cost ledgers/reports to determine that the cost accumulation system identifies and segregates significant IR&D/B&P effort by individual project (CAS 420.40(a)). Costs of immaterial IR&D or B&P projects may be combined within each category.	
2. Determine proper classification of IR&D/B&P effort by evaluating work authorizations, statement of work or any other similar documents. Verify that the effort charged as IR&D or B&P is neither sponsored by a grant, nor required in performance of a contract. (CAS 420.30(a)(2) and (6)).	
3. Evaluate detailed job cost report to determine that the costs for each IR&D/B&P project include all direct costs for IR&D/B&P projects (CAS 420.40(b) and 50(a)(1)). Direct costs are those costs, which if incurred in like circumstances for a final cost objective, would be treated as direct costs of that final cost objective.	
4. Evaluate the most recent incurred cost submission or forward pricing rate proposal to determine if all allocable overhead costs (except business unit general and administrative (G&A) expenses) of productive activities and other indirect costs (e.g., service center costs) related to the project are applied to the direct costs based on the contractor's cost accounting practices (CAS 420.40(b) and 50(a)(2)).	
5. Evaluate the charging practices for IR&D effort and B&P administration costs to determine that such costs are consistently treated the same in like circumstances. They are to be treated as direct charges, which, if incurred for a final cost objective, would be charged direct to contracts. Otherwise, they should be treated as indirect expenses (CAS 420.50(a) and 60(a)).	
6. Evaluate the most recent incurred cost submission or forward pricing rate proposal to determine that the IR&D/B&P project costs exclude G&A expense (CAS 420.40(b)).	
7. Determine and document the reliability of the information the audit team will use to reach their conclusions in this section.	

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D-1 Accumulation of IR&D / B&P Costs by Pool	WP Reference
Version 8.0, dated Jan 2023	
1. Determine that IR&D/B&P costs are accumulated in a separate pool apart from the G&A pool (CAS 420.40(c)).	
2. Determine that the IR&D/B&P pool costs consist of only:	
a. IR&D/B&P project costs exclusive of G&A (see Step 1 above)	
b. Allocable home office IR&D/B&P costs (see WP E-1, Allocation to Cost Objectives, Step 3.)	
3. Determine that the contractor has consistent and equitable practices regarding the costs of preparing, submitting and supporting proposal efforts resulting from a specific requirement of an existing contract. (CAS 402.61(c))	
4. Determine and document the reliability of the information the audit team will use to reach their conclusions in this section.	

E-1 Allocation to Cost Objectives (MAAR 18)	WP Reference
Version 8.0, dated Jan 2023	
1. Evaluate the objectives and/or work statements for IR&D/B&P projects and identify those projects, which benefit only the performing segment and those benefiting other segments as well.	
2. When the project(s) benefits other segments, determine whether the project costs need to be transferred to the home office. Such project costs need not be transferred to the home office when a direct allocation to the segments is not substantially different from the allocation which would be made if they were to pass through the home office (CAS 420.50(d) and (g)).	
3. For those projects which have been identified as benefiting more than one segment in step 2 above, determine that the projects are transferred to the home office exclusive of G&A. If the work is not a part of an IR&D/B&P project of the performing segment, then transferred costs should include G&A (CAS 420.50(d)).	
4. For those projects which only benefit the performing segment, determine that the project costs are included in the IR&D/B&P pool and allocated on the same base used by the segment to allocate G&A expense under CAS 410 (CAS 420.50(f)(2)).	
5. Determine and document the reliability of the information the audit team will use to reach their conclusions in this section.	

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F-1	Inter-Segment IR&D / B&P Effort	WP Reference
Version 8.0, dated Jan 2023		
1.	Auditors located at segments performing IR&D/B&P effort for another segment must determine whether such effort is part of an IR&D/B&P project of the performing segment.	
a.	Coordinate this determination with the CAD, home office auditor, and/or the auditor at the receiving division prior to proceeding to the next step in the audit program.	
b.	When such effort is part of the performing segment's IR&D/B&P project, determine that the project costs are transferred to the home office exclusive of the segment's G&A.	
2.	Determine and document the reliability of the information the audit team will use to reach their conclusions in this section.	

G-1	Deferral of IR&D / B&P Costs	WP Reference
Version 8.0, dated Jan 2023		
1.	Determine that all B&P costs incurred during a cost accounting period are assigned to that period only. (CAS 420.40(f)(1)).	
2.	Determine that all IR&D costs incurred during a cost accounting period are assigned to that period except as may be permitted by provisions of existing laws, regulations, and other controlling factors. (CAS 420.40(f)(2)).	
3.	Determine and document the reliability of the information the audit team will use to reach their conclusions in this section.	

H-1	Home Office IR&D / B&P Costs	WP Reference
Version 8.0, dated Jan 2023		
1.	Coordination with segment auditors regarding accumulation of IR&D/B&P costs by the home office:	
a.	Coordination with the segment auditor(s) will be required to identify:	
	(1) Those IR&D/B&P projects which will benefit some segments or all segments.	
	(2) Inter-segment IR&D/B&P projects that are part of the IR&D/B&P project of the performing segment.	
b.	For those projects which have been identified as benefiting more than one segment, determine that the costs of such projects have been transferred to the home office from these segments.	

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H-1 Home Office IR&D / B&P Costs	WP Reference
<p>c. Determine that the home office cost accumulation system for such costs is in sufficient detail so that the allocation to the segments can be made in accordance with the allocation requirements identified in Step 2. below.</p>	
<p>2. Allocation to Segments – Evaluate the allocation(s) of home office IR&D/B&P project costs to the segments to determine that: (MAAR 18)</p>	
<p>a. Direct allocations are first made for those projects that can be identified with specific segments (CAS 420.50(e)(1)). Determine if the method used to allocate the costs to more than one segment is based on the beneficial or causal relationships between the projects and the segment.</p>	
<p>b. Those other projects remaining after the direct allocations are made to specific segments are allocated among all segments by means of the same base used to allocate the residual expenses in accordance with CAS 403 (CAS 420.50(e)(2)).</p>	
<p>3. Determine and document the reliability of the information the audit team will use to reach their conclusions in this section.</p>	

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A-1 Concluding Steps	WP Reference
Version 8.0, dated Jan 2023	
1. Summarize and document the results of audit.	
<p>2. Discuss the audit results with the supervisor and, if applicable the technical specialist. The auditor should only report those noncompliances which are considered material. Coordinate significant or unusual issues with the CFAO, FAO Manager, and if applicable, with the CAD network (see CAM 8-302.4, 8-302.6). Coordination should be both before and after discussion of audit results with the contractor. The CFAO should be apprised of noncompliance matters at the earliest possible date. <i>Note: If a noncompliance is considered immaterial, but could become material if circumstances change, notify the CFAO through a memorandum. The memorandum will include a Statement of Condition and Recommendation (SOCAR) and provide the CFAO with sufficient information to understand the condition and the severity of the CAS noncompliance. The only exception to issuing a memorandum is if the audit report includes a material noncompliance(s). When a material noncompliance is reported, the immaterial noncompliance will be reported in a separate exhibit to the report titled "Noncompliance that Warrants Attention of the Cognizant Federal Agency Official." Reference to the exhibit for the immaterial noncompliance will be in the Executive Summary, but will not be included in the Basis of Opinion section, as it is not a material noncompliance.</i></p>	
<p>3. Prepare draft audit report (and memorandum, if applicable). If the audit scope was limited to a certain area(s) of the contractor's accounting practices, modify the subject matter stated in the Report On (from WP A01) and Opinion (from WP A) section of the report as necessary so that they clearly identify the limited areas audited.</p>	
<p>4. If a material weakness or significant internal control deficiency is detected during the course of this audit, ensure that the findings have been fully developed to determine if a significant deficiency in compliance with the DFARS 252.242-7006 criteria exists. If so, open a Business System Deficiency assignment (Activity Code 11090) to report the deficiency and submit it to the contractor for comment.</p>	
<p>5. Hold an exit conference with the contractor and provide a draft report (and memorandum, if applicable) to the contractor for comments in accordance with CAM 4-304. Obtain supervisory review, and management review if required, of the working papers and draft audit results section of the audit report (and memorandum, if applicable) before discussion with the contractor.</p>	
<p>6. Finalize audit report (and memorandum, if applicable) incorporating the contractor's reaction and auditor's response, if applicable.</p>	
<p>7. Complete the administrative working papers.</p>	

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A-1 Concluding Steps	WP Reference
8. Update the permanent files. <i>Ensure that a copy of DMIS Report No. CAS 3 entitled "CAS Compliance Testing (Activity Code 194XX)" is included in the permanent file after the assignment has been closed in DMIS.</i>	
9. Submit the working paper package and draft report (and memorandum, if applicable) to the supervisor/manager for final review and processing.	