DCAAM 7640.1; DCAA Contract Audit Manual

Chapter 1

Introduction to Contract Audit

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1-000 - Introduction To Contract Audit **

1-001 Scope of Chapter **

This chapter provides information on the contract audit mission; responsibilities of DCAA and the contract auditor; and the relationships of DCAA with other Department of War (DoW) components, other Government agencies, and contractors.

1-100 Section 1 - Establishment and Responsibilities of DCAA **

The Defense Contract Audit Agency was established by DoD Directive 5105.36 for the purpose of performing all contract auditing for the Department of Defense (DoD), now DoW, and providing accounting and financial advisory services to all DoW procurement and contract administration activities.

1-101 Nature of Contract Auditing **

The purpose of contract auditing is to assist in achieving prudent contracting by providing those responsible for Government procurement with financial information and advice relating to contractual matters and the effectiveness, efficiency, and economy of contractors' operations. Contract audit activities include providing professional advice on accounting and financial matters to assist in the negotiation, award, administration, repricing and settlement of contracts. Audits are performed to determine compliance with laws and regulations. Contract auditors perform evaluations of contractors' cost estimates, costs incurred, and compliance with laws and regulations. DCAA audits are conducted in accordance with Generally Accepted Government Auditing Standards (GAGAS).

1-102 Access to Records of Contractor **

The clause at FAR 52.215-2 provides the auditor's primary authority for access to contractor records. This clause provides the contracting officer's representative with the authority to examine and audit contractors' books, records, documents and other evidence and accounting procedures and practices, regardless of form or type, sufficient to reflect properly all costs claimed to have been incurred or anticipated to be incurred in performing cost-reimbursement, incentive, time-and-material, labor-hour, or price-redeterminable contracts. If audit teams experience issues gaining access to contractor records, they should follow the process in DCAA Instruction (DCAAI) 7640.17.

1-200 Section 2 - Relationships with the Government Accountability Office and DoW OIG **

DCAA Instruction (DCAAI) 7050.2 contains the process that should be used for any oversight reviews performed by the DoW Office of the Inspector General (OIG) or the Government Accountability Office (GAO). If an office receives a request from either of these groups directly, they should coordinate with the Headquarters, Auditing Standards Division (CASD) before providing any information or responses.

1-300 Section 3 - Audit and Advisory Services for Non-DoW Agencies **

1-301 Introduction **

In addition to performing contract audits for the DoW, DCAA also provides contract audit and advisory services to other Federal agencies, typically on a reimbursable basis. This section provides general policy for performing these services for Non-DoW Agencies.

1-302 Processing Non-DoW Agency Requests for Audit and Advisory Services **

Requests for DCAA to perform audits and advisory services for a Non-DoW agency can come from two sources. First, a Non-DoW agency may initiate a request directly. Second, a DCAA auditor may solicit a Non-DoW agency to participate in an audit of a contractor where DoW is cognizant (see FAR 42.003 for details on determining cognizance). In this case, the Non-DoW agency pays a pro-rata share of the percentage of the cost of the audit. Regardless of the source, customers must provide sufficient funding to cover the cost of audit, as outlined below.

1-302.1 Responding to Non-DoW Agency Requests for Audit and Advisory Services **

All requests should be promptly acknowledged in writing. Such requests must be processed promptly, since the requesting agency will need to make other arrangements if DCAA does not agree to accept the engagement or to coordinate proper funding. The response should state whether DCAA will accommodate or decline the request. Typically, such work will be accepted if the audit effort falls within the normal scope of DCAA work and the requesting agency agrees to pay for the audit effort. If the request is accepted, the response should include the anticipated audit report or memorandum date. If the request is declined, the reasons should be stated. Directorates will notify Headquarters, Attention: OWD, of audit requests of an unusual nature from non-DoW agencies (e.g. outside services routinely provided).

1-302.2 Customer Funding for Non-DoW Audits and Advisory Services **

DCAA will not perform audit procedures or advisory services on behalf of a Non-DoW entity until a signed funding document has been received and DCAA Accounting has input that document into DCAA records. Performing reimbursable work without funding in place may lead to violations of the Anti-Deficiency Act. A promise to provide future funding is not sufficient to perform reimbursable effort.

1-302.3 Insufficient Customer Funding **

When the auditor notes that estimates for the engagement will exceed currently funded amounts, they should coordinate and request additional funds from the customer. If the customer will not provide additional funding for the customer's portion of the audit, and the audit cannot be deferred, the auditor should advise the requestor of the following available options:

(1) The requestor can request that audit effort continue until the auditor depletes the remaining funds. The audit report will reflect an audit opinion appropriate for the audit procedures completed (i.e., this could mean a qualified opinion or disclaimer of opinion will be issued if the auditor cannot complete all necessary audit procedures due to the funding limitation); or

(2) The requestor can direct immediate termination of work on the customer's behalf and DCAA will not issue an audit report to the customer.

a. If fieldwork has not yet begun,

(1) Notify the Non-DoW contracting officer(s) that their agency's contracts will not be included in the audit and no audit report will be issued to their office.

(2) Adjust the scope of audit as necessary.

(3) For billing purposes, audit effort should be allocated to DoW and other participating Non-DoW agencies.

(4) Exclude the presentation of information on applicable non-DoW contracts from the audit report.

(5) The Non-DoW contracting officer(s) should be advised when the audit discloses significant noncompliances or findings that may impact their agency's contracts. Auditors should not expand effort to specifically address issues for non-DoW agencies that are not funding for audit services.

b. If, after the audit report has been issued, a reimbursable customer approaches the DCAA office to request audit services for which funding authorization is subsequently made available, the following procedures apply:

(1) The DCAA office should obtain funding authorization from the contracting officer.

(2) The DCAA office should set up a separate assignment and perform the necessary audit steps and testing procedures to cover the requested non-DoW contracts.

(3) Additional audit effort should be billed to the non-DoW customer.

(4) A separate audit report should be issued that includes direct costs on applicable non-DoW contracts.

1-302.4 High Risk Conditions **

a. Funding constraints may limit the ability of some non-DoW customers to request and pay for routine DCAA audit and advisory services for their contracts. However, when performing audits or advisory services, auditors sometimes become aware of high-risk conditions (e.g., financial distress or nonperformance of Government contracts) that may impact these non-DoW agencies. Although DCAA auditors should not expand efforts to specifically address issues for non-DoW agencies that are not paying for services, DCAA has a professional responsibility to advise all affected agencies of conditions or situations that may place the Government at significant risk.

b. Audit reports that identify such high-risk conditions shall be distributed to all materially affected agencies. This does not include audit reports addressed to administrative contracting officers (e.g., CAS noncompliance reports) since these contracting officers are responsible for resolving the issues and the results will apply to all Government contracts.

1-303 Audit Scope for Non-DoW Audits **

DCAA is responsible for determining the scope of audit, including the manner and level of effort necessary to provide complete contract audit coverage. Auditors should take into consideration any additional areas for coverage suggested by the requesting agency. The Federal Acquisition Regulation (FAR) is the primary regulation for use by all Federal executive agencies in acquiring supplies and services with appropriated funds. Agencies are authorized to issue supplemental regulations tailored to their organizational needs. Thus, the cost principles and procedures applicable to a specific non-DoW organization consist of the FAR together with that agency's supplemental regulation, if any. Auditors should ensure applicable criteria in both FAR and agency supplements are considered in the audits. The contract or solicitation will identify the applicable criteria. A list of all agency supplements can be found at www.acquisition.gov.

1-304 Audit Reporting for Non-DoW Audits **

DCAA Forms 1 and 1c or their equivalents will not be used to report suspended and/or disapproved costs to certain contracting organizations. Such reporting will be accomplished promptly after disclosure of the suspended or questioned item by means of a letter or audit report.

1-305 Non-DoW Agency Requests for Audit Working papers and Reports **

DCAA may receive requests from Non-DoW agencies for contractor information, audit working papers, memoranda, or reports. The Non-DoW agency may have provided funding for the work product or not. The guidance below explains what can be provided.

1-305.1 Non-DoW Agency Requests for Audit Working Papers and Reports When Funding was Provided **

When a Non-DoW agency provided funding for an audit or advisory service, DCAA will distribute a copy of the report or memo to the funding Non-DoW agency. In addition, DCAA will make available specific audit working papers upon customer request when additional information is needed to understand a specific finding. Audit working papers prepared during audits for Federal agencies are the property of DCAA and will remain in the possession of the auditor. If audit cognizance is transferred from DoW to another Federal agency, and audit files are requested to be released, the office should coordinate with Headquarters, CASD, through their Directorate.

1-305.2 Non-DoW Agency Requests for Audit Working Papers and Reports When Funding was Not Provided **

In general, if a non-DoW agency requests working papers or audit reports related to an engagement they did not participate in, we should not provide copies. However, DCAA can provide final indirect rates if requested and they are readily available in our files.

1-306 Non-DoW Agency Requests for Contractor Information Not Connected to an Audit **

a. DCAA will be responsive to requests received from Government agencies outside the DoW for information available in the audit files when the circumstances clearly show that the requestor is entitled to the requested information. There is a presumption of entitlement if the requesting agency has a contract or anticipating to contract with the contractor and the information desired is related to the negotiation or administration of that contract. Requests for specific cost information which are readily available, without audit effort, will be accommodated without reimbursement. If the auditor has any doubt as to whether the requesting agency is entitled to the information, the auditor must obtain clearance from the contractor before releasing any specific cost or financial data, such as overhead rates, or discuss with the supervisor and manager.

b. If a non-DoW agency requests contractor cost or financial data, written material, or access to working papers or audit files, which pertains to a matter unrelated to the negotiation or administration of a contract by the requesting agency, the request should be referred to Headquarters, CASD, for consideration.

1-307 Attending Negotiation and Follow-Up **

The auditor should support any negotiation or follow-up effort performed as requested by the non-DoW agency.

1-400 Section 4 - Relationships with Other Government Organizations **

1-401 Introduction **

This section provides guidance and procedures governing relationships with other Government organizations.

1-402 General **

Government personnel may communicate with DCAA personnel on official business. In all cases, the identity of the individual and his or her need to know should be established prior to furnishing any information either written or oral. Appropriate security precautions should be observed with respect to both classified military information and contractor information.

1-403 Relationships with DoW Procurement and Contract Administration Organizations **

1-403.1 DCAA Responsibilities to Procurement and Contract Administration Organization **

a. As the audit and financial advisor to procurement and contract administration activities, auditors must understand and support the service needs of these organizations. DCAA is committed to providing timely and responsive services and will maintain communications and liaison services sufficient to continuously assess if customer needs are being met.

b. Organizationally, DCAA is separate and independent from acquisition components of the DoW. Auditors are expected to exercise independent judgment in planning the type and extent of audit testing sufficient to render an audit opinion but should consider and address areas of concern or informational needs of requestors. The auditor will also exercise independence in the formulation of audit opinions, recommendations, and conclusions contained in audit reports.

c. Effective communication between the DCAA auditor and the contracting officer's representatives is essential. To ensure continuous close cooperation, DCAA should give procurement personnel timely notification of any significant changes in audit plans.

1-403.2 Resolving Contract Audit Recommendations **

a. DCAA audit report recommendations may lead to disagreements between the auditor and the contracting officer. When disagreements occur, the auditor should maintain communications with the contracting officer for a satisfactory resolution of the issue prior to contract negotiations.

b. The DFARS Procedures, Guidance and Information (PGI) section 215.406-1, Pre-negotiation Objectives, outlines the process for resolving significant contract audit recommendations. DoW Components have established corresponding policies and procedures implementing the policy. DCMA has established the Contract Management Board of Review process in the DCMA Boards of Review Manual. The Rules of Engagement Guidebook contains the steps in the process for audit teams to follow.

1-403.3 Signing Certificates of Non-Disclosure and Statements of Financial Interest **

Source Selection Authorities (SSA) from various Service program offices may ask auditors and Customer Specialists to sign Certificates of Non-Disclosure and Statements of Financial Interest to acknowledge understanding of the requirements set forth in FAR 3.104-4, "Disclosure, Protection, and Marking of Contractor Bid or Proposal Information and Source Selection Information". However, auditors should not be required to sign a non-disclosure agreement. Auditors are already required by 18 U.S.C. 1905 and Agency policy to protect contractor data from unauthorized disclosure. It is permissible for Customer Specialists advising on Source Selection Evaluation Boards to sign such certificates as they may have access to all of the bidders' source sensitive information.

1-404 Relationship with DoW OIG and Other Executive Branch Internal Audit Organizations **

1-404.1 Organizations for Government Internal Audit **

Internal audit, oversight, and investigative services are performed by the offices of the Assistant DoW OIGs for Audit, Evaluations, and Administrative Investigations. DoW component internal audit organizations include the Army Audit Agency, the Naval Audit Service, and the Air Force Audit Agency. The various Military Services also have additional internal review and audit groups such as the Inspector Generals of the Army, Navy and the Air Force. Most non-DoW agencies have similar activities for the performance of internal audit within their organizations. The following guidance also applies to non-DoW executive agencies.

1-404.2 DCAA Assistance to Government Internal Audit Organizations **

a. When internal audits require verification of contractor data or records at contractors' plants, the internal audit organization normally will obtain fact-finding assistance from DCAA.

b. Support will be furnished to the internal auditor, when doing so does not conflict with the contract auditor's basic role of providing advisory services to contracting officers. Requests requiring contract auditors to evaluate contracting officers' performance are inappropriate, whereas assistance concerning contractors' performance is appropriate. Any requests received from internal auditors from other Government organizations should be coordinated with Directorate leadership and Headquarters, CASD, as needed.

1-404.3 Oversight Reviews **

Oversight reviews are coordinated through DCAA Headquarters, CASD, in accordance with DCAAI 7050.2.

1-404.4 Visits by the DoW OIG and Military Inspectors General **

When an Inspector General of a DoW component, or his/her representative, visits an audit office, the auditor should, verify the identity of the individual, cooperate fully in responding to inquiries pertaining to the audit of contracts under the auditor's cognizance. Requests for sensitive information, or requests that require the assignment of an auditor for a substantial period of time, should be in writing. The auditor should report such visits to their Directorate Director. Before furnishing any sensitive information, the auditor should coordinate the matter with the Directorate Director and Headquarters, CASD.

1-405 Relationship with Investigative Agencies of the Government **

Any requests received from the Federal Bureau of Investigation, DoW criminal investigators, and criminal investigators from other agencies should be coordinated with the Headquarters, Operations Investigative Support (OIS) Division . If the office is contacted directly by an investigative agency for written material, access to files and working papers, interviews, meetings, or other requests for contractor information, they should refer the investigative agency to the OIS who will facilitate any meetings needed and the transfer of any written material or access to files.

1-406 Relationship with Government Legal Counsel in Contract Disputes, Bid Protests, and Other Matters **

a. When requested, it is Agency policy to assist Government counsel in auditing matters in all contract disputes, bid protests, and other matters, whether initiated through an Agency finding or by other means. Audit support should fully respond to the needs of counsel and may consist of comprehensive audit and accounting advisory services; accounting research applicable to the specific case, including testimony relative to the audit report; or testimony as an expert on accounting and auditing practices and procedures. All work done at the request of the Government trial attorney is subject to the attorney work product privilege. As such, while DCAA may maintain custody of any documents developed while providing support to the trial attorney, control over the documents, and any decision pertaining to the release of these documents, rests with the trial attorney or his/her successor. This policy is in keeping with the Agency's assigned responsibility to provide accounting and financial advisory services to all DoW procurement and contract administration activities in negotiating, administering, and settling contracts.

b. Although control of the documents rests with the trial attorney, the DCAA auditor is responsible for their content. Should the trial attorney attempt to obtain audit working papers prior to release of the report, the cognizant office should:

(1) offer to provide copies of any relevant documents and

(2) explain to the trial attorney that the audit process is incomplete until required supervisory reviews are completed.

Review of incomplete audit files may lead the attorney to draw erroneous inferences regarding the DCAA audit position. Should the trial attorney persist in a request for incomplete working papers, Headquarters, CASD, should be notified before incomplete audit files are released.

c. Under certain circumstances, trial attorneys may request DCAA auditors to sign a litigation protective order. A litigation protective order usually restricts the use of contractor information to the conduct of the trial (i.e., it could not be used for any other purpose). The restrictions could impair DCAA's audit rights and use of contractor data for all other appropriate Government purposes. Auditors approached by trial attorneys to sign a litigation protective order should not sign the order. However, if trial attorneys insist, auditors should elevate the request to their Directorate leadership.

1-406.1 Armed Services Board of Contract Appeals (ASBCA) **

The ASBCA Charter are found in Appendix A to the Defense FAR Supplement. If an auditor is contacted in regard to an ASBCA case, they should review the guidance in DCAA Instruction 5410.11, Release of Official Information in Litigation and Testimony by DCAA Personnel as Witnesses. This instruction requires that all such inquiries be transmitted to DCAA Office of General Counsel (OGC) and that responses not be provided without specific instructions from OGC.

1-407 Relationship with the Internal Revenue Service (IRS) **

a. Branch offices may receive direct requests from the IRS for records and files related to an IRS investigation or tax matters. The office should coordinate IRS requests for investigative or tax information with their Directorate, before providing any information of this type to the IRS. With Directorate approval, information related to an IRS fraud or criminal investigation, or in connection with a docketed case before the U.S. Tax Court, should be released directly to the IRS. The office should request the IRS to provide information showing that the requested information relates to these situations.

b. For requests related to civil investigation or administrative inquiry, the office is only authorized to release information that would normally be releasable to the general public under the Freedom of Information Act. If the requested documents would not normally be releasable by DCAA to the general public (e.g., audit reports or contractor proprietary information), the Directorate should forward the request to the OGC for a release determination. The Directorate should provide OGC with a summary of the information requested, purpose of release, and other pertinent information.

1-408 Relationship with Members of Congress and Congressional Committees **

a. Upon receipt of a congressional request or a request from a customer for help responding to a congressional request, offices are to immediately notify, and send a copy to, the DCAA Chief of Staff. The Chief of Staff will provide instructions and relevant due dates for providing a response, scheduling a congressional visit, or helping a customer.

b. DCAA personnel will cooperate with members of Congress, congressional committees, and their staffs by promptly providing full responses to official requests for information on the Agency's programs and operations.

c. Congressional requests may come in the form of official requests for

(1) information,

(2) visits by congressional committees or their staff,

(3) replies to constituents' letters, or

(4) comments on legislation and legislative matters .

d. The Chief of Staff will coordinate with the responsible Headquarters element, General Counsel, and other DoW elements; and will review all proposed responses and DCAA documents, before responding directly to the requestor. All materials must have the proper CUI markings.

e. The DCAA General Counsel will coordinate, review, and send comments on legislative matters.

1-409 Assistance in Preparing Claims Against the Government **

Officers and employees of the Government are prohibited by law (18 U.S.C. 205) from acting as agents or attorneys for prosecuting any claim against the United States or aiding or assisting in the prosecution or support of any such claim other than in the proper discharge of their official duties. A part of the auditor's official duties is to inform contractors of the manner in which public vouchers, termination settlement proposals, cost statements, and other financial representations connected with the negotiation and performance of Government contracts should be prepared and submitted.

1-500 Section 5 - Relationship with the News Media **

The Communications Director is responsible for deciding how requests from the media will be satisfied and for obtaining appropriate clearance for the release of information. If an auditor is contacted by the new media, they should promptly elevate through their leadership to the Communications Director.

1-600 Section 6 - Processing Freedom of Information Act (FOIA) Requests **

The Freedom of Information Act, 5 U.S.C. 552, is a public law which is designed to allow the general public access to Government records. DCAA Instruction 5410.8, DCAA Freedom of Information Act Program, implements DoD Directive 5400.07, DoD Freedom of Information Act Program. Any FOIA requests should be processed in accordance with the DCAAI.

1-700 Section 7 - Auditor Participation on Government and Contractor Process Action Teams (PATs); Integrated Product Teams (IPTs); Management Councils **

1-701 Auditor's Role on Government and Contractor Teams Such as PATs, Steering Committees, and Management Advisory Boards **

a. Auditors can fully participate as voting members on Government teams that are studying processes involving DCAA mission responsibilities. Examples of Government teams on which auditors are frequently asked to participate include Process Action Teams (PATs) formed to study and suggest improvements on acquisition processes or regulations.

b. Auditors do not participate on contractor teams, committees or task forces. The auditor’s role is in a purely advisory non-voting capacity on issues related to the knowledge and skills of the auditor to avoid impairing their independence. Auditors must not be involved in making management decisions or performing management functions. DCAA's role as independent financial advisor to the contracting officer precludes our participation as members on contractor teams, management advisory boards, steering committees, or other similar groups. The auditor can only attend as an observer at meetings of these groups.

c. The auditor’s attendance as an observer of contractor teams does not preclude DCAA from conducting audits and expressing an independent opinion on the particular process in the future.

1-702 Integrated Product Teams (IPTs) **

1-702.1 Integrated Product Teams (IPTs) – Background **

An Integrated Product Team (IPT) is a multidisciplinary group of people who are collectively responsible for delivering a defined product or process. The IPT is composed of people who plan, execute, and implement life-cycle decisions for the system being acquired. The intent in using IPTs is to avoid rework at the end of a process by identifying problems and finding potential solutions at the earliest possible point in the procurement process. In general, the procuring contracting officer (PCO) is encouraged to establish a procurement IPT to aid in making the best decisions on significant aspects of the procurement. The IPT will begin work when the RFP/RFQ is being developed. The IPT normally continues its work throughout the procurement cycle from proposal development to contract award. The PCO usually chairs the IPT, determines its composition, and sets its scope. The major objectives of an IPT are better RFPs/RFQs, better proposals, reduced cycle time between issuance of RFP/RFQ and contract award, and better understanding of the contract requirements. The makeup of the IPT will normally include the buying activity, DCMA, and the contractor.

1-702.2 Auditor's Role on IPTs and Related Streamlined Acquisition Initiatives **

a. DCAA does not participate as a member in IPT arrangements (e.g., Alpha Pricing, Omega Pricing). DCAA's role as the independent financial advisor precludes us from engaging in activities that impair the auditor's independence. An impairment to independence would be noncompliant with GAGAS. Although DCAA auditors may not be a team member of an IPT, DCAA will continue to provide audit services, as requested, to assist the contracting officer in determining a fair and reasonable price. There are three guidelines that need to be followed (all three must be met) to perform the audit.

- The contracting officer requests the audit services;
- The audit covers a "management approved" proposal or part of a proposal; and
- The issued report reflects an opinion that is not influenced by the contractor or Government Officials.

b. Upon receipt of a contracting officer request, the auditor should coordinate with the contracting officer to determine if the proposal will involve a buying command and contractor IPT. If so, the auditor should establish exactly what services are required (e.g., an examination of the complete proposal, examination of part of the proposal, or an application of agreed-upon procedures). The auditor should acknowledge the request for services after obtaining a clear understanding of the contracting officer's needs.

To avoid the appearance of a lack of independence, auditors will not provide input during an IPT process without issuing an audit report that captures all significant audit results. This may result in several audit reports being issued throughout the IPT process.

1-703 Other Working Groups or Councils **

a. If an auditor is asked to participate in any other type of working group or council by a member of the Government procurement community they should follow the following basic overarching principles. Auditors should participate as a non-voting observer in these working groups/councils and provide any needed financial advice.

b. DCAA representatives should not be involved in making management decisions or performing management functions. If there are any questions regarding the appropriateness of our participation, elevate those concerns through Directorate leadership.

1-704 Memorandum of Agreement **

When participating on a PAT (or other similar team) or Management Council the auditor may be asked to sign a teaming agreement or Memorandum of Agreement. Auditors generally should not sign these agreements. The auditing standard of independence precludes DCAA from entering into agreements relating to audit scope. Even when the agreement does not relate to audit scope, there is sometimes an appearance of independence problems when DCAA signs an agreement. Instead of signing an agreement, the auditor may satisfy the customer's needs by communicating to the team leader in writing the auditor's expected role on the team (e.g. DCAA's role should be in a non-voting, purely advisory capacity and not involved in making management decisions or performing management functions). If the contractor, Federal agency, or team leader insists on the office entering into an agreement, the office should send the proposed memorandum of agreement and background material through the regional office to Headquarters, CASD, for coordination before executing the agreement.