

MASTER AUDIT PROGRAM

Activity Code 17500	Progress Payment, Percentage of Completion
Version 6.1, dated January 2021	
B-1	Planning Considerations
Type of Service - Attestation Examination Engagement	
Audit Specific Independence Determination	
<p>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.</p>	
<p><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></p>	
<p>1. This program is intended to provide a logical sequence to the audit effort and to reflect a mutual understanding between the auditor and the supervisor as to the scope required to meet auditing standards and DCAA objectives for the current assignment. The audit steps in the program are intended as general guidance and should be modified as considered necessary to fit the current audit. Portions of the audit which are covered in other assignments (e.g., accounting systems, Material Management and Accounting Systems) should be referenced at the appropriate place in this program.</p>	
<p>2. The basic authority for progress payments based upon a percentage or stage of completion is included in FAR 32.101 and 32.102(e)(1) and (2), which state that this type of progress payment may be used as a payment method under agency procedures. The current FAR provisions require that such agency procedures must ensure that:</p>	
<p>a. Payments are commensurate with work accomplished, which meets the quality standards established under the contract; and</p>	
<p>b. Progress payments may not exceed 80 percent of the eligible costs of work accomplished on undefinitized contract actions.</p>	

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3. DFARS 232.102(e)(2) limits such progress payments within DoD to contracts for construction, shipbuilding and ship conversion, alteration or repair. Generally speaking, the requirements of FAR/DFARS are implemented through department or agency directives or instructions. For example, the Navy implements these requirements through Secretary of the Navy (SECNAV) Instruction 7810.12C, Shipbuilding Progress Payments (current version is dated December 23, 2005). Typically, a special contract clause is negotiated based on that instruction which authorizes progress payments based on a percentage or stage of completion, subject to several restrictions and limitations specified in the contract clause. The clauses used for Navy contracts have usually included provisions which specifically address the criteria for (a) computation of payments, (b) establishing billing price, (c) allocating total contract price of each vessel, (d) invoices, (e) physical progress and weighting factors, (f) incurred costs, (g) retentions, and (h) certifications and audits. This contract clause is normally supplemented by Memorandums of Agreement (MOAs) relating

to billing price revisions, the contractor's progressing system, and physical progress and weighting factors.

4. Contract financing should be administered to aid the acquisition process; however, the contracting officer needs to avoid any undue risk of monetary loss to the Government through financing. Therefore, the contractor's use of the contract financing provided and the contractor's financial status need to be monitored. The risk of an overstated request for progress payment is highest when a contractor is experiencing cash flow or performance problems. Consequently, the auditor should be alert for high risk situations such as poor financial conditions, low cash balances, losses on contract work, etc. During performance of risk assessments, auditors are reminded to contact the contracting officer to obtain the contractor's financial condition information for risk assessment purposes. The purpose of the audit is to evaluate the propriety of the progress payment request. Critical factors in making this determination include:

a. The contractor's compliance with the contract clause, memorandums of agreement, and progressing system as approved by the contracting officer.

b. The reasonableness of the contractor's estimates to complete. Understatement of the estimates at completion could result in overpayment and excessive financing costs.

c. The reliability of the contractor's accounting systems. To the extent that payments may be limited to a percentage of incurred costs and the physical completion percentage is computed based on labor hours and costs incurred, auditors must consider the reliability of the accounting systems that record and report such actual data when planning the scope of the review. Furthermore, costs related to undefinitized contract actions must be separately identified since FAR 32.102(e)(2) limits progress payments on these costs.

d. The proper liquidation of progress payments. Upon preliminary acceptance of a vessel, progress payments should be liquidated to the extent paid under the contract for that vessel.

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<p>e. The adequacy of the contractor's financial condition to continue contract performance (see B-1, Step 10). While the contracting officer is responsible for assessing the contractor's financial condition, auditors should immediately alert the contracting officer if they become aware of information that may indicate unfavorable or adverse financial conditions that could impede a contractor's ability to perform on Government contracts (e.g. audit leads, significant events, current economic conditions, etc.).</p>
<p>5. The scope of progress payment reviews will depend on how much reliance can be placed on the contractor's accounting system, internal controls, cost representations, and billing procedures. If the results of prior audits and the preliminary audit steps indicate low audit risk, a limited review of the progress payment should be made. This decision must reflect a mutual understanding between the auditor and supervisor as to the scope required to meet auditing standards and DCAA objectives for the current assignment. This program does not replace individual auditor judgment and may be supplemented to satisfy the needs of a particular assignment.</p>
<p>Other Planning Considerations</p>
<p>Prior to commencing the audit, review Agency guidance that may impact the audit and adjust the scope and procedures appropriately.</p>
<p>References</p>
<p>1. The Progress Payment clause in the contract</p>
<p>2. FAR 32.102(e) and DoD FAR Supplement 232.102</p>
<p>3. Price Revision Clause in the contract</p>
<p>4. CAM 14-300 "Assessing a Contractor's Financial Capability"</p>
<p>5. CAM 14-200 "Audit of Progress Payments"</p>

B-1	Preliminary Steps	WP Reference
Version 6.1, dated January 2021		
1.	Obtain the request for audit, the contractor's progress payment request, and the supervisory auditor's risk assessment and preaudit instructions. Review and consider in establishing the scope of audit to ensure appropriate coverage of specific areas of concern.	
2.	Review permanent files and/or current audit assignments to ensure that related findings from earlier audits are considered in the scope of follow-up reviews. (Note: Such information may not be separately maintained in a permanent file, but rather may be contained in individual current audit assignments.)	

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<p>3. Review permanent file to determine if previous audits included findings and recommendations that impact the subject matter. If there were findings, auditors should document this information in the risk assessment and perform the following procedures:</p> <ul style="list-style-type: none">a. 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.b. Document the results of the inquiry and the impact to the subject matter.	
<p>4. 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 under audit. If there are no other studies or audits, document that information in the working papers and perform the procedures below.</p> <ul style="list-style-type: none">a. Ask contractor management if internal audits were performed. If yes, request contractor provide a summary listing of the internal audits that	

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<p>would assist us in understanding and evaluating the efficacy of the internal controls relevant to the subject matter of the audit.</p> <p>b. If the review of the perm file or the contractor identifies relevant internal audits:</p> <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. <p>c. If the review of the perm file or the contractor identifies relevant other audits or studies:</p> <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. <p>d. 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).</p> <p>e. Determine if additional audit procedures are needed to respond to identified risk.</p>	
<p>5. Using the framework and the guidelines in WP B-2, obtain and document an understanding of the contractor's key internal controls that are relevant to the audit. Auditors should be able to obtain a major portion of this understanding during a walkthrough of the subject matter.</p>	
<p>6. Review the contract/contract brief and referenced Memorandums of Agreement (MOAs) for terms and conditions affecting progress payment requests and cost or performance reporting requirements.</p>	

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<p>7. Review the contractor's progressing system description. Most contract payment clauses require the contractor to submit a description of its "progressing system" for review and approval by the contracting officer. The system should provide:</p> <ul style="list-style-type: none"> a. Documentation supporting the physical percentage of completion computation for the specific contract. b. Traceability of allocable costs from the progress payment billings and physical completion computation to the cost accounting system. 	
<p>8. Obtain and review the contractor's most recent detailed (bottom-up) estimate at completion (EAC). Ensure that it is no older than the required revision frequency specified in the progress payment clause (normally quarterly).</p>	
<p>9. Review any Integrated Program Management Reports (IPMRs), Cost/Schedule Status Reports (C/SSRs) - (see CAM 14-205(e)(1)(b)), or similar reports or charts prepared by the contractor, and identify any cost, technical, or schedule problems which could affect the EAC.</p>	
<p>10. Contact Government contract administration and program office officials to (1) identify any cost, technical, or schedule problems and (2) determine what these officials have done to evaluate the EAC. Assess the adequacy of any evaluations performed as follows:</p> <ul style="list-style-type: none"> a. Review the latest copies of any Government specialist evaluations, cost analyses, or other program management reports pertaining to evaluation of costs or schedule. This includes any progress/milestone charts or similar systems which assess contractor progress. b. Determine if the Government evaluations of the EAC considered any cost or schedule problems (identified in IPMRs, progress/milestone charts, or similar data). (see CAM 14-205). c. When these evaluations present a range of EACs, inquire as to which is most likely. 	
<p>11. Request a Government specialist evaluation of the progress payment request if appropriate (see CAM Appendix B-100).</p>	
<p>12. Contact the contracting officer to ascertain any known concerns that impact the audit and adjust the audit scope and procedures accordingly.</p>	
<p>13. Notify the appropriate contracting officer of the commencement of the risk assessment and that the expected completion date will be provided in the formal acknowledgement once the risk assessment is complete. The acknowledgement process should be performed in accordance with CAM 4-104.</p>	
<p>14. Determine if the progress payment request includes significant costs or estimates applicable to subcontractors or partners under teaming arrangements. If so, determine what actions the contractor has taken to</p>	

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<p>ensure that progress payments to its subcontractors or partners conform to the progress payment provisions of the contract. If the required analyses are not performed or are considered inadequate and these costs cannot be evaluated by other techniques (other current or historical data), an assist audit should be coordinated/requested (see CAM 14-205i.).</p>	
<p>15. During the entrance conference, or other appropriate meeting, make specific inquiries of contractor management and other appropriate parties regarding the following:</p> <ul style="list-style-type: none">a. 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 205.32)b. 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)c. 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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<p>16. 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 estimating or 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 budget or contractual commitments, and opportunities to commit and conceal fraud). See the DoD IG website Fraud Detection Resources for Auditors for common fraud risk factors. Copy link and paste into web browser, • other factors identified that increase the risk of material noncompliance with laws and regulations, and • the audit team's understanding of relevant key internal controls. 	
<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 material misstatement and noncompliance due to error or fraud.</p>	
<p>17. Arrange and conduct an entrance conference with the contractor's designated representative. If applicable, include a follow up with contractor management on:</p> <ul style="list-style-type: none"> • corrective actions that address previous DCAA audit findings and recommendations, • other studies or audits that impact the subject matter. 	
<p>18. Issue a notification letter to the contractor regarding the audit in accordance with CAM 4-302.3.</p>	

C-1	Estimate To Complete	
Version 6.1, dated January 2021	WP Reference	
<p>Evaluate the reasonableness of the contractor's EACs used in calculating billing prices and weighting factors. The scope of review should depend on the auditor's knowledge of the contractor and the results of prior audits and risk assessment.</p>		

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1. When IPMRs or C/SSRs are available, determine if the EAC appears reasonable when compared to projections using trend analysis techniques: <i>NOTE: Do not duplicate analyses available from the Contract Administration Office (CAO) or Program Office.</i>	
a. Compare the cumulative to date Budgeted Cost of Work Scheduled (BCWS), Budgeted Cost of Work Performed (BCWP), and Actual Cost of Work Performed (ACWP), on a monthly basis. Depending upon the stage of contract completion, this comparison may be best shown by use of a graph. Compare to identify unusual fluctuations (positive and negative) and trace to the cost account level to identify the underlying reasons.	
b. Project the EAC using Cost Performance Indices (CPI)s and Schedule Performance Indices (SPI)s as explained in Trend Analysis of EAC using Performance Indexes.	
c. Significant differences between the EACs projected using the CPI and SPI and the contractor's "bottom-up" EAC may indicate serious problems in the contractor's estimates and/or system and must be thoroughly investigated.	
d. Discuss significant differences with the contractor, the CAO, and the Program Office, and request an explanation for the difference.	
e. If not explained to the satisfaction of the auditor, request a specialist evaluation on the items in question.	
2. Evaluate the reasonableness of the contractor's EAC using the guidance in CAM 9-300.	
a. Verify that the contractor has been consistent in its EAC preparation.	
b. Verify that the contractor has used appropriate rates and factors.	
c. Review the quantitative and qualitative aspects of the EAC for reasonableness utilizing Government specialist assistance and assist audits if considered necessary (see CAM B-100).	

D-1	Incurred Costs	
Version 6.1, dated January 2021		WP Reference
Incurred Costs. Contract payment clauses used by the Navy generally limit payment to a specified percentage of allowable costs incurred as of the date the progress payment/invoice is submitted. On each invoice, the contractor must certify the allowable costs incurred. Such certification shall provide for cost category reporting in accordance with the contractor's normal accounting system and be broken down into direct material, direct labor, and indirect costs. In evaluating this incurred cost limitation, the auditor should:		

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1. Verify that costs incurred are based on currently posted job cost subsidiary ledgers or similar authorization controls.	
2. If retirement fund contributions are paid less frequently than quarterly, verify that pension accruals are excluded from incurred costs until such costs are paid.	
3. Ensure that progress payment requests on costs related to undefinitized contract actions are separately identified and are limited to 80% of eligible costs as determined by the contract terms (see FAR 32.102(e)(2)). In addition, for DoD contracts, the auditor should be aware that no more than 50% of the not-to-exceed price shall be expended by the Government until the contractor submits a qualifying proposal to definitize the action. Limitations are covered by DFARS 217.7404-4 for undefinitized contract actions and DFARS 243.204-70-4 for undefinitized change orders. See CAM 14-202.3.e for guidance.	

E-1	Other Areas - Percentage Of Completion	
	Version 6.1, dated January 2021	WP Reference
	1. Review the contractor's progress payment request to:	
	a. Determine whether the progress payment, retention, holdback, etc., rates are in agreement with the payment clause.	
	b. Check the accuracy of the contractor's progress payment request calculations.	
	c. Verify that billed costs do not exceed the target or ceiling cost stated in the contract.	
	d. Verify that the payment requested by the contractor based on the percentage of physical progress does not exceed the amount billable based on the incurred cost limitations specified in the contract clause.	
	2. Verify that the billed escalation amounts for materials and other types of costs included in the progress payment request are in accordance with the contract provisions.	
	3. Verify that progress payments are being properly liquidated. Upon delivery or preliminary acceptance of each vessel, progress payments should be liquidated to the extent paid under the contract.	
	4. Be alert for changes in financial condition that may impact future contract deliveries. If the contractor is in a loss situation on the contract, inform the administrative contracting officer.	

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5. Test the contractor's accounting system's internal controls related to billings for reconciling amounts received on billings for this contract. If the test finds that the contractor has received overpayments, further test the contractor's controls for notifying the contracting officer and the paying office.	
6. Add any additional audit steps considered necessary under the circumstances.	

F-1	Percentage Of Physical Progress	
Version 6.1, dated January 2021	WP Reference	
Percentage of Physical Progress. The contract payment clause provides for the computation of progress payments and retention amounts based on specific criteria for physical progress. In determining the reasonableness of that physical progress percentage, review the following:		
1. Billing Price - The contract billing price should equal the total revised contract price or the sum of the projected final cost and projected profit. Most contract clauses require that any proposed contractor revision to the billing price must be separately set forth in a supplemental agreement to the contract, and include the computations upon which the revision to the billing price is based.		
2. Allocated Total Contract Price of Each Vessel - Determine if the computed price is based on appropriate factors. In no event should the allocated total contract price of all vessels exceed the total contract price. The allocated amount is determined by multiplying the total contract price by a percent fraction (representing the quotient from dividing the original unit target price of the vessel by the original total target price).		
3. Weighting Factors - These factors are used to measure physical completion by categories of labor and material cost. These factors are revised quarterly or when factual data indicates they are no longer representative of the actual labor and material distribution. Revisions must be supported by detailed de-escalated EACs for direct labor, direct material, and indirect costs with additional data concerning the cause of the changes.		
a. Determine if a MOA exists between the Government and the contractor for the weighting factors used to prepare the progress payment.		
b. Verify that the contractor used the weighting factors contained in the most current valid agreement.		

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<p>c. Review the basis of the agreed to weighting factors and determine if they are reflective of actual labor and material distribution. If the MOA appears to contravene the requirements of either the contract clause or the applicable service instruction, the auditor should pursue the issues in accordance with CAM 5-307(d).</p>	
<p>d. Reconcile the supporting documentation for the cost element weights to the contractor's latest IPMR, C/SSR, or other similar internally generated management reports.</p>	

A-1	Concluding Steps	
	Version 6.1, dated July 2021	WP Reference
	1. Discuss audit findings with supervisor and hold an exit conference (follow the guidance in CAM 4-304.4).	
	2. Auditors should document and communicate with the contracting officers upon the completion of our audit:	
	<p>a. Brief the contracting officer on significant questioned, unsupported, unresolved costs or other significant and/or complex findings/issues, and/or</p>	
	<p>b. Coordinate with the contracting officer to find out and determine if inclusion of detailed explanatory notes in our report would serve a useful purpose when there are no findings.</p>	
	3. Complete indexing and cross-reference working papers.	
	4. Draft Report (CAM 14-206 and Chapter 10).	
	<p>a. When an assist audit and/or a specialist evaluation is necessary, and is not obtained, the Audit Opinion paragraph should be properly annotated for the scope limitation.</p>	
	<p>b. If the contractor's accounting system is considered inadequate for the administration of progress payments, describe the findings and fully explain why the conditions need to be corrected by the contractor. The report should include specific recommendations to the ACO as to whether the progress payment(s), in whole or in part, should be paid to the contractor under the circumstances.</p>	
	5. Significant procedural or control deficiencies, or CAS/FAR noncompliances should be cited in this report and also reported separately. If a material weakness or significant internal control deficiency are identified resulting in a significant deficiency in a business system, ensure the findings have been fully developed to determine if a significant deficiency exists. If so, open a Business System Deficiency assignment (Activity Code 11090) to report the deficiency.	

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6. If the auditor has encountered information that constitutes evidence or raises suspicion that fraud or other illegal acts have occurred, refer such suspicion by completing a DCAA Form 2000 (see CAM 4-702.4 and 5).	
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