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**DEFENSE CONTRACT AUDIT AGENCY
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PSP 730.5.1/2010-009

March 2, 2010
10-PSP-009(R)

**MEMORANDUM FOR REGIONAL DIRECTORS, DCAA
DIRECTOR, FIELD DETACHMENT, DCAA
HEADS OF PRINCIPAL STAFF ELEMENTS, HQ, DCAA**

SUBJECT: Audit Guidance on Inter-Organizational Transfers Included in Contractor Forward Pricing Proposals

The purpose of this memorandum is to clarify the Agency guidance for audit coverage related to inter-organizational transfers included as part of a contractor's forward pricing proposal. The Contract Audit Manual (CAM) 9-105 will be revised accordingly.

Summary

Prime contractor proposals often include proposed costs associated with inter-organizational transfers. Table 15-2 at FAR 15.408 provides instructions for submitting cost/price proposals when cost or pricing data are required. Section II, Paragraph A, Materials and services, of Table 15-2 requires all work performed by the prime contractor, including any inter-organizational work, be included in the prime contractor's own cost or pricing data and submitted to the Government. As a result, the support for inter-organizational transfers should be considered the same as the prime contractor's own cost or pricing data. Therefore, the FAR 15.404-3(b) prime contractor requirement for conducting cost or price analysis of proposed subcontract costs do not apply to inter-organizational transfers. The scope of audit of inter-organizational transfers depends on whether the inter-organizational transfers are based on price (FAR 31.205-26(e)) or cost. The prime contract auditor may require field pricing assistance from the auditor cognizant of the inter-organizational transfer location.

Guidance

Based on the requirements set forth in FAR 15.408 Table 15-2 IIA, Materials and services; prime contractor's should support inter-organizational transfers as if it were the prime contractor's own cost or pricing data. FAR 15.404-3(b) prime contractor requirements for conducting cost or price analysis are not applicable to inter-organizational transfers. The scope of audit of inter-organizational transfers depends on whether the inter-organizational transfers are based on price (FAR 31.205-26(e)) or based on cost. FAR 15.408 Table 15-2 IIA, Materials and services, provides a clear distinction between the requirements for inter-organizational transfers depending on whether they are based on price or cost, as follows:

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- (1) *Adequate Price Competition*: ... For interorganizational transfers priced at other than the cost of comparable competitive commercial work of the division, subsidiary, or affiliate of the contractor, explain the pricing method (see FAR 31.205-26(e)).
- (2) *All other*: For inter-organizational transfers priced at cost, provide a separate breakdown of cost elements.

Therefore, when an auditor receives a request to audit a proposal with significant inter-organizational transfers, the auditor must first determine whether the transfers have been (1) priced based or (2) supported by a separate breakdown of cost elements.

Transfers Based on Price

For price based transfers, auditors should ensure that the requirements of FAR 31.205-26(e) are met (i.e., it is the established practice of the transferring organization to price inter-organizational transfers at other than cost, and the item being transferred qualifies for an exception to the cost or pricing data requirement outlined in FAR 15.403-1(b)). When the pricing is based on adequate price competition, the auditor should review the contractor's supporting competitive bids and market analysis and determination that the price of the inter-organizational transfer is based on adequate competition and the proposed amount is fair and reasonable. When the pricing is not based on adequate price competition (e.g., sole source commercial item), the auditor should review the sales data of the related organization to ensure that the proposed amounts are fair and reasonable. Auditors should only consider those sales to unrelated organizations that are not sales to state, local, or the Federal Government directly or indirectly. The review of sales data may require the auditor at the prime location to request field pricing support from auditors at the inter-organizational location.

If the audit discloses that the proposed items are not supported by adequate price competition or prior sales data, the auditor should evaluate the cost of the proposed transfers using the techniques described below while also ensuring that appropriate adjustments are made to eliminate the intra-company profit included in the proposed prices.

Transfers Based on Cost

For cost based transfers, auditors should ensure that the data required by the FAR 15.408, Table 15-2, are adequately provided. If an audit of the proposed inter-organizational amount requires field pricing support at another segment location, an appropriate request for assist audit services should be issued to the auditors at the inter-organizational location based on the prime auditor's documented risk assessment.

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Make or Buy Considerations

CAM 9-405.2 highlights that intra-company procurement is one of the special considerations related to the audit of make or buy decisions. When inter-organizational transfers are significant, the scope of audit should evaluate the contractor's make or buy practices regarding inter-organizational transfers and report any practices that do not result in fair and reasonable prices. Contractors must support and demonstrate the decision to make the item (i.e., inter-organizational transfer) results in a fair and reasonable price versus buying the item from another vendor. FAR 15.407-2(f) states that the contracting officer shall evaluate proposed make-or-buy decisions as soon as practicable after their receipt and before contract award.

Additionally, failure to meet the requirements of FAR 15.408 and/or FAR 31.205-26(e) or any procurement/estimating practices that do not result in fair and reasonable pricing of inter-organizational transfers should be reported as estimating system deficiencies.

Concluding Remarks

FAO personnel should direct questions to their regional personnel. Regional personnel may direct questions to Pricing and Special Projects Division, at (703) 767-3290 or e-mail at DCAA-PSP@dcaa.mil.

/s/ David E. Johnson
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