

**Report on Noncompliance
With Cost Accounting Standard 410,
Allocation of Business Unit General Administrative
Expenses to Final Cost Objectives**

March 2005

Reference Number: 2005-1C-045

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



INSPECTOR GENERAL
for TAX
ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

March 29, 2005

MEMORANDUM FOR DAVID A. GRANT
DIRECTOR OF PROCUREMENT
INTERNAL REVENUE SERVICE

Daniel R. Devlin

FROM: Daniel R. Devlin
Assistant Inspector General for Audit (Headquarters Operations
and Exempt Organizations Programs)

SUBJECT: Report on Noncompliance With Cost Accounting Standard 410,
Allocation of Business Unit General Administrative Expenses to
Final Cost Objectives (Audit #20051C0210)

The Defense Contract Audit Agency (DCAA) performed an examination regarding the contractor's compliance with Cost Accounting Standards (CAS) and the Federal Acquisition Regulation (FAR). The purpose of the examination was to determine whether the contractor complied with the requirements of CAS 410 (Allocation of Business Unit General Administrative Expenses to Final Cost Objectives).

The DCAA stated that, during the period April 1, 2003, through March 31, 2004, the contractor was in noncompliance with CAS 410 and the FAR. The DCAA also noted that, as of the date of its report, the condition causing the noncompliance had not been corrected. According to the DCAA, its report is limited to the cited instance of noncompliance. Accordingly, the DCAA expresses no opinion on whether other practices are proper, approved, or agreed to for pricing proposals, accumulating costs, or reporting contractor performance data. However, the DCAA examination disclosed that the contractor's failure to comply with CAS 410 and failure to consistently follow its disclosed accounting practices resulted or may result in increased costs paid by the Federal Government.

The areas of noncompliance and failure to follow disclosed practices are:

- Material costs (purchased parts, service charges, and interdivisional transfer costs) are improperly included in the value-added General and Administrative (G&A) base.

- The Civil Division CAS disclosure statement, effective March 29, 2003, states the G&A base is comprised of total costs incurred less the costs of purchased parts and services, raw material, interdivisional transfer, and other categories.

As a result, the DCAA considers the contractor's actual practices of accumulating or reporting costs to be in noncompliance with its Disclosure Statement because material costs and interdivisional transfer costs should be excluded from the G&A base. Additionally, because of this inconsistent practice, the contractor is not complying with FAR 52.230-2(a)(2). This clause also requires that, if any change is made to those practices, the Disclosure Statement must be amended.

During the review, the DCAA requested the contractor to estimate the magnitude of this noncompliance. The contractor responded that costs of approximately \$1.6 million (0.54 percent of the \$299 million G&A base) were erroneously included in the G&A base, resulting in a 0.06 percent impact on the G&A rate.

The DCAA recommends that the contractor establish and maintain a consistent, current, accurate, and complete description of all cost accounting practices which affect Federal Government contracts and follow the practices outlined in the Civil Division Disclosure Statement, effective March 29, 2003, concerning the G&A base. The DCAA also stated the contractor should remove the material costs (equipment maintenance/repair, equipment maintenance supplies, etc.) and interdivisional transfer costs from the G&A base. Additionally, the contractor should comply with CAS 9904.

This DCAA report was issued on June 16, 2004; however, the Treasury Inspector General for Tax Administration (TIGTA) and the Internal Revenue Service (IRS) did not receive a copy of the report until February 2005. We are transmitting this report to you to enable the IRS to track any financial accomplishments derived from negotiations with the contractor based on the results of this DCAA report.

The information in this report should not be used for purposes other than those intended without prior consultation with the TIGTA regarding their applicability.

If you have any questions, please contact me at (202) 622-8500 or John R. Wright, Director at (202) 927-7077.

Attachment

NOTICE:

The Office of Inspector General for Tax Administration has no objection to the release of this report, at the discretion of the contracting officer, to duly authorized representatives of the contractor.

The contractor information contained in this report is proprietary information. The restrictions of 18 U.S.C. § 1905 must be followed in releasing any information to the public.

This report may not be released without the approval of this office, except to an agency requesting the report for use in negotiating or administering a contract with the contractor.

The TIGTA seal was removed due to its size.