

Master Document – Audit Program

Activity Code 17740	Preaward Survey of Prospective Contractor Accounting System
Version 6.11, dated November 2015	
B-1	Planning Considerations
Audit Specific Independence Determination	
<p>Members of the audit team and internal specialists consulting on this audit must complete the Audit Specific Independence Determination (w/p 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 work paper. For example, an FAO may add additional auditors (e.g. FAO technical specialist) 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>	
Purpose and Scope	
<ul style="list-style-type: none"> • The major objectives of this audit are to obtain an understanding of the accounting system to appropriately complete the Preaward Survey of Prospective Contractor Accounting System, SF 1408, and to opine as to whether the design of the contractor’s system is acceptable for the award of a prospective Government contract. • DCAA FLAs have worked with the buying commands to have contractors fill out a checklist asserting they meet the SF 1408 criteria, and providing a narrative describing how they meet each criterion. Once they receive this assertion, they are sending a request to DCAA for audit, with this assertion attached. If the request for audit does not include an assertion from the contractor, contact the CO to determine if one was prepared already. If the CO did not have the contractor prepare the assertion, the auditor should ask the contractor to complete this assertion so that it can be used during the performance of the risk assessment (a proforma letter with the checklist is available as an OAG). • This audit involves only the evaluation of the design effectiveness, not the operating effectiveness of the system. Procedures performed to evaluate design effectiveness include a mix of inquiry of appropriate personnel, observation of the entity's operations, and inspection of relevant documentation. Walkthroughs that include a combination of these procedures ordinarily are sufficient to evaluate the effectiveness of the design. Detailed testing of transactions, and reperformance of the controls are not necessary when testing the design effectiveness. • If requested to perform a Preaward Survey of Prospective Contractor Accounting System Audit on a contractor that has an active Government contract, the auditor should check the files to determine if prior work has been performed that will provide the contracting officer 	

Master Document – Audit Program

the information necessary to fill in the SF 1408 without the completion of the preaward audit (e.g., if a prior preaward or post contract award accounting system audit has been performed). If prior information does exist, contact the contracting officer to determine if the prior report will meet their needs. Additionally, if there are known system deficiencies or voucher processing problems, this information should be provided to the contracting officer as well. Auditors should not issue an opinion stating the design is acceptable for award when there are known deficiencies in the operating effectiveness.

- If this is a follow up request to a previous preaward accounting system survey, determine whether a follow up is appropriate. If the previous preaward was completed less than 12 months ago, and the contractor’s system has not changed, it would be appropriate to perform a follow up to the previous preaward. The auditor should modify the audit program appropriately, and be sure to issue a follow-up preaward report available as an OAG. If the previous preaward accounting system survey was performed more than 12 months ago, and/or the contractor’s system has changed, a full preaward audit should be performed. Be sure to coordinate with the contracting officer if a determination is made that a follow up is not appropriate.
- If requested to perform a Preaward Survey of Prospective Contractor Accounting System Audit on a contractor that has not yet established their accounting structure, policies and procedures, and a plan for implementation, the auditor should contact the contracting officer to inform them that the SF 1408 cannot be completed because the contractor is unable to demonstrate that the design is capable of accomplishing the criteria. An audit should not be performed in these circumstances. Note: This does not include situations where the contractor has designed it systems but has not purchased or implemented the accounting software package.
- If the request is for a Preaward Accounting System Survey for a proposed subcontract, the auditor should determine what effort the prime contractor has taken to determine if the accounting system is acceptable. FAR 9-104.4 indicates the prime contractor is generally responsible for prospective subcontractors. Therefore, the audit may not be necessary unless there are circumstances such as the subcontractor formally denying access to the prime contractor.

Other Planning Considerations

Prior to commencing the audit, review guidance that may impact the audit and adjust the scope and procedures appropriately. Guidance to review includes CAM, open MRDs, FAQ training material, guidebooks, etc. available on the DCAA Intranet.

References

1. CAM 5-200, “Pre-Award Surveys and Adequacy of Accounting System for Contractual Requirements”
2. FAR 9.105, “Procedures (for determination of contractor’s responsibility)”

Master Document – Audit Program

3. FAR 9.106, DFARS 209.106, PGI 209.106, “Preaward Surveys”
4. FAR 52.216-16(g), “Quarterly Limitation on Payments Statement” (FPI contracts); and FAR 52.232-20, “Limitation of Cost.”
5. AICPA Attestation Standards AT Section 501.59, Evaluating Design Effectiveness

B-1	Preliminary Steps	WP Reference
Version 6.11, dated November 2015		
1. Research and Planning		
a.	Review the audit request and contact the Contracting Officer (CO) to ensure that the audit scope addresses any customer concerns that will impact the assessment of audit risk and adjust the audit scope and associated audit procedures accordingly (CAM 4-104.a.).	
b.	Obtain information on the proposed Government contract (e.g., type and amount of contract, special contract provisions, etc.). Contact the CO/PCO/buying command as determined necessary to discuss any questions or concerns that were identified.	
c.	Review the perm file and any prior audits, and document any issues impacting the current scope of audit. If a perm file does not exist or is not current, provide a list of items (e.g., organizational charts, financial statements, policies and procedures, etc.) to be obtained during the field visit to the contractor in advance of the entrance conference, so the contractor has additional time to gather the information. Update the permanent file (See CAM 4-405.1).	
d.	Review permanent file to determine if previous audits included findings and recommendations that impact the subject matter under audit (GAGAS 5.06). If there were findings, auditors should document this information in the risk assessment and perform the following procedures: (1) During the entrance conference, 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. (2) Document the results of the inquiry and the impact of the corrective actions to the subject matter under audit. (Note: The purpose of this question is to follow up with contractor on	

Master Document – Audit Program

<p>relevant prior DCAA audit findings that could have a material effect on the subject matter of audit.)</p>	
<p>e. 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 (GAGAS 5.06). If there are no other studies or audits, document that information in the work papers and perform the procedures below. (If you do not perform the following procedures, you must document your justification for the departure.)</p> <p>(1) During the entrance conference:</p> <ul style="list-style-type: none"> • 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. • Ask contractor management if other types of audits or studies were performed by other than DCAA (e.g., other Government audit agencies, consultants, Independent Public Accountants, etc.) that would impact the subject matter under audit. If yes, have contractor explain what type of audits or studies were performed, if there were any related findings or recommendations, and any contractor corrective actions taken as a result. <p>(2) 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 CAC 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, issued by the CAC, FAO POC or auditor, 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 work papers. 	

Master Document – Audit Program

<p>(3) 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>(4) Document the results of the inquiries including the response received from contractor’s 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>(5) Determine if additional audit procedures are needed to address any identified risk. (Note: The purpose of this question is to discover any new audit leads that could affect the scope of current audit.)</p>	
<p>f. Electronically transmit an acknowledgement/notification to the ACO/Buying Command notifying them of 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. (CAM 2-303). The acknowledgement/notification process should be within the timeframe and in accordance with the procedures in CAM 4-104.</p>	
<p>g. Issue a notification letter to the contractor regarding the audit in accordance with CAM 4-302.3.</p>	
<p>h. Review the contractor’s assertion and narrative describing how they meet the SF 1408 criteria if applicable. The review of this assertion will allow the auditor to make preliminary judgments to obtain an understanding of the controls the contractor has in place, and determine if there are potential noncompliances that could occur. If the contractor does not submit an assertion, the auditor will need to request the contractor describe how they meet the SF 1408 criteria in order to make these preliminary judgments. Any areas of risk identified should be documented, and the necessary audit procedures to address those risk areas should be performed during the fieldwork in C-1.</p> <p>Note: It is important to remember that a smaller, less complex entity might achieve its control objectives in a different manner from a larger, more complex organization (e.g., they may have less employees which limits their opportunities to segregate duties). In these cases, the auditor should evaluate whether the contractor has implemented alternative controls that are effective (e.g., an outside</p>	

Master Document – Audit Program

<p>accountant’s quarterly review, payroll and/or billing invoices prepared by external service).</p>	
<p>i. If this audit is being performed as a follow-up, document the procedures performed to determine that continual reliance can be placed on the worked performed under the initial preaward audit (e.g., what was done to ensure no changes have taken place that would impact the areas we are not specifically looking at in the follow-up).</p>	
<p>j. During the entrance conference, or other appropriate meeting, make inquiries of contractor management regarding knowledge of any fraud or suspected fraud affecting the subject of this audit, managements awareness of allegations of fraud or suspected fraud affecting this audit, and management’s understanding about the risks of fraud relevant to this audit. Note: This discussion and any data submitted should be documented in the working papers.</p>	
<p>k. 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 noncompliances, due to error or fraud, that could materially 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 incentives, pressures and opportunities to commit and conceal fraud, and the propensity to rationalize misstatements), • other known risk factors, • the audit team’s understanding of relevant internal controls, • inquiries to the contractor regarding its fraud management plans and controls. <p>Document fraud risk factor/indicators (see - Sources of Fraud Risk Factors below) that are present and could materially affect the subject matter. If Fraud risk factors are present, document specific audit procedures designed to address the increased risk of material noncompliance due to fraud.</p>	

Master Document – Audit Program

<p>Communication among audit team members about the risk of material misstatement due to error or fraud should continue as needed throughout the audit.</p> <p>Sources of Fraud Indicators:</p> <ul style="list-style-type: none"> • GAGAS Appendix Section A.10 – Examples of Indicators of Fraud Risk (http://gao.gov/products/GAO-12-331G) • AU-C 240.A75 (Appendix A)- Consideration of Fraud in a Financial Statement Audit, Examples of Fraud Risk Factors (http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AU-C-00240.pdf) • DoDIG’s Contract Audit Fraud Scenarios and Resources website (http://www.dodig.mil/resources/fraud/resources.html) <p>(To access the Sources of Fraud Indicators, copy and paste the web address shown above into the address block in Internet Explorer.)</p>	
<p>2. Entrance Conference and Preparation</p>	
<p>Arrange and conduct an entrance conference (see CAM 4-302). Explain to the contractor’s representatives that as issues are developed during the audit, they will be furnished to the contractor for fact-finding and timely resolution. This process should facilitate reduced audit cycle time and efforts to respond to and issue the audit report. If applicable, include a follow up with contractor management on:</p> <ul style="list-style-type: none"> a. corrective actions that address previous DCAA audit findings and recommendations (step 1e), b. other studies or audits that impact the subject matter under audit (step 1f). 	
<p>3. Initial Risk Assessment</p>	
<p>Using the information obtained in steps 1 and 2, prepare an initial risk assessment to determine the scope of the examination (W/P B).</p>	

<p>C-1</p>	<p>Preaward Survey (SF 1408)</p>	<p>WP Reference</p>
	<p>Version 6.11, dated November 2015</p>	
<p>Prepare “Preaward Survey of Prospective Contractor Accounting System” (SF 1408) by completing the following audit steps. The latest version of</p>		

Master Document – Audit Program

<p>the SF 1408 can be obtained at: http://www.gsa.gov/portal/forms/download/115778</p> <p>In WP B-1, the auditor reviewed the contractor assertion or description of how the contractor meets the SF 1408 criteria to assist them in understanding the controls the contractor has in place, and determining if there are potential noncompliances that could occur. In this section, the auditor will determine, based on the contractor’s assertion, and the walkthrough/demonstration (or observations, inquires, and inspections if the system is not implemented), if the contractor’s system is suitably designed for award of a prospective contract.</p> <p>When performing the following audit steps, it is important to remember that procedures performed to evaluate design effectiveness may include a mix of inquiry of appropriate personnel, observation of the entity’s operations, and inspection of relevant documentation (e.g., policies and procedures, prospective reports, and general ledger examples). Transaction testing is not required.</p> <p>If a contractor’s system has been implemented, a documented walkthrough/demonstration of the system is ordinarily sufficient to evaluate design effectiveness.</p> <p>If the contractor has designed the system, but has not yet implemented the system, the evaluation of the effectiveness of the design of the system will need to include a mix of inquiries, observation, and inspection. This may include discussions with responsible personnel, review of written policies and procedures, charts of account, etc. Note: Inquiry alone is not sufficient, observation, and/or inspection of documentation is necessary as well.</p>	
<p>1. Generally Accepted Accounting Principles. Through inquiry, observation and/or inspection, determine if the contractor’s accounting system is designed to be in accordance with GAAP (e.g., does the contractor have or intend to have an accrual basis accounting system, dual entry accounting, a general ledger they plan to post costs to, and the ability to generate basic financial reports). (SF 1408, Section II, 1)</p>	
<p>2. Proper segregation of costs. Through inquiry, observation and/or inspection, determine if the system is designed to preclude direct charging of indirect expenses and indirect charging of direct contract costs. (SF 1408, Section II, 2a)</p>	
<p>3. Direct costs by contract. Through inquiry, observation and/or inspection, determine that the contractor’s system is designed to produce a subsidiary job cost ledger which accumulates costs by contract at a level of detail consistent with that used by the prospective contractor in its proposal. (SF 1408, Section II, 2b)</p>	

Master Document – Audit Program

<p>4. Allocation of indirect costs. Through inquiry, observation and/or inspection, determine that the system is designed to accumulate indirect costs in logical groupings. Determine that the groupings are allocated based on benefits accrued to intermediate and final cost objectives. Is the cost accounting system documented, with a written description of the contents of bases and pools? (SF 1408, Section II, 2c)</p>	
<p>5. Accumulation of costs under general ledger control. Through inquiry, observation and/or inspection, determine if the contractor’s system is designed to allow the contractor’s job cost ledger, or its equivalent, to be reconcilable and routinely posted to the general ledger control accounts (e.g. totals for direct labor, direct material, subcontracts, other direct costs). (SF 1408, Section II, 2d)</p>	
<p>6. Timekeeping system. Through inquiry, observation, and/or inspection, determine that the system is designed to allow labor charging to intermediate and final cost objectives based on a timekeeping document (paper or electronic timecards). Also ensure that the contractor has policies, procedures or instructions that require timesheets be completed and certified by the employees and approved by the employees’ supervisors. (SF 1408, Section II, 2e)</p>	
<p>7. Labor distribution. Through inquiry, observation and/or inspection, determine if the system is designed so that labor cost distribution records (i) are reconcilable to payroll records and (ii) can be reconciled to and from the cost accumulation records in labor subsidiary or general ledger accounts. (SF 1408, Section II, 2f)</p>	
<p>8. Interim determination of costs. Through inquiry, observation and/or inspection, determine that the contractor posts, or plans to post, contract costs at least monthly to books of account. (SF 1408, Section II, 2g)</p>	
<p>9. Exclusion of Unallowables. Through inquiry, observation and/or inspection, discuss and document the contractor’s plan to identify and exclude unallowable costs if the contract is awarded. (SF 1408, Section II, 2h)</p>	
<p>10. Costs by Contract Line Item: If the prospective contract requires costs to be reported by CLIN or unit, determine what level is required. Through inquiry, observation and/or inspection, determine if the contractor’s system is designed to be expanded to the requisite level of detail (i.e. costs can be accumulated by sub accounts within the job cost ledger and includes details by multiple contract line items specified by the contract). (SF 1408, Section II, 2i)</p>	
<p>11. Preproduction Costs (Applies primarily to manufacturing contracts): Through inquiry, observation and/or inspection, determine if the contractor’s system is designed to routinely segregate preproduction</p>	

Master Document – Audit Program

from production costs in order to assist in repricing or follow-on contract pricing. (SF 1408, Section II, 2j)	
12. Limitation of Costs: Through inquiry, observation and/or inspection determine if the contractor’s system is designed so that interim indirect expense rates can be readily calculated from the books of accounts and are routinely monitored. Who is responsible for monitoring total contract expenditure against contract limitations on price or cost, and how frequently is this reviewed? Are controls in place to ensure compliance with the reporting requirements of FAR 52.216-16(g) or FAR 52.232-20? (SF 1408, Section II, 3a)	
13. Billings (e.g. progress payments, public vouchers): (CAM 6-1006) (SF 1408, Section II, 3b and FAR 32.504)	
a. Is the system designed so that billings can be reconciled to the cost accounts for both current and cumulative amounts claimed?	
b. Through inquiry, observation and/or inspection, determine if the contractor has procedures to ensure that subcontractor and vendor costs are only included in billings if payment to the subcontractor or vendor will be made in accordance with the terms and conditions of the subcontract or invoice and ordinarily within 30 days of the contractor’s payment request to the Government?	
14. Adequate, Reliable Data: Based on the procedures above, summarize on WP C your conclusions on whether the contractor’s system is designed to produce cost information at a sufficient level of detail for use in pricing follow-on contracts? (SF 1408, Section II, 4)	

A-1	Concluding Steps	WP Reference
Version 6.11, dated November 2015		
1. Summary Steps		
a.	If there are open or partially completed items, follow-up and resolve them at this time and summarize audit results.	
b.	Complete, index and cross reference working papers.	
c.	Summarize and document the results of audit. Accounting system in operation. Is the accounting system in full operation? If not, which portions are in operation and what is the status of implementing the full accounting system? (SF 1408, Section II, 5)	
d.	Obtain final supervisory auditor/manager review of the working papers and audit results. After management approval, hold and document an exit conference with the contractor representative in accordance with the procedures specified in CAM 4-304.	

Master Document – Audit Program

e. Prepare draft report and SF 1408 to be furnished as part of the audit report. The narrative section of the SF 1408 should only include the following statement “See DCAA Audit Report No. <i>(insert audit report number)</i> , dated <i>(insert date)</i> for information supporting this form.”	
f. Update the permanent file.	