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Business Management

Why Accurate FAR Rates, Proper Controls Are Essential

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Your firm is engaged in federally funded government contracting. You aren't paying attention to your overhead rates and don't have the proper controls and procedures in place to ensure that you are recording costs appropriately. You are facing severe implications because of your lack of action and appropriate knowledge.



In addition to the government agencies requesting significant reimbursements from prior requisitions, they are withholding payments related to the current work performed. You have been informed that there is a possibility that your firm could be barred from doing business with the government agencies in the future. This severely hampers your ability to stay productive. How could you allow this to happen to your company?

Your firm needs to be aware of this worst-case scenario. To avoid these disastrous events, it is imperative that your company gets the knowledge to calculate the correct overhead rate in accordance with Federal Acquisition Regulations (FAR). The correct rate is essential to the profitability of your business. The calculation of your firm's overhead rate is based

on specific criteria, and if you are not following those methods you could be miscalculating your rate.

If your overhead is not calculated correctly you are at serious risk. If the rate you are charging is too low it will result in lower reimbursement for work performed. A rate higher than your correct rate may result in lost work. Either way, your bottom line will suffer. If it is determined

that the rate you are charging for reimbursement was over-stated, your company will be required to reimburse the government agency for amounts reimbursed in excess of the actual rate. In order to calculate the correct rate, your company must have knowledge of allowable and unallowable costs, in addition to the proper allocation of direct and indirect costs. This knowledge will ensure that overhead rates are in compliance with FAR and that your company will be charging the correct reimbursement rate.

With many government contracts, the contractor will use an estimated reimbursements rate for a period until the actual rate is calculated at the end of the year. Often, the government agencies require the contractor to have their overhead rates certified by an independent auditor. The

certified rate will be compared to the estimated rate that was used during that period. Additionally the government agencies have the right to perform their own audit of the calculation of the contractor's rate. In these situations, errors

and honesty. Contractors need to have a written code of business ethics and conduct. In order to promote compliance with such code of business ethics and conduct, contractors are advised to have an employee business ethics and com-

pliance training program and a suitable internal control system. This system should be suitable to the size of the company; facilitate timely discovery and disclosure of improper conduct in connection with government contracts; and ensure corrective measures are promptly instituted and car-

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are often identified when unallowable costs are included in the rate calculation. In both of these cases, the contractor will be liable to the government agency for any amounts over-charged due to using a rate higher than the actual.

In addition to the knowledge needed to calculate the proper rate the contractor must be aware of certain internal controls, policies and procedures that are required under government contracts. There are a number of requirements in place stating that government contractors must conduct themselves with the highest degree of integrity

ried out. Further guidance states that internal control systems should provide for the following:

- Assignment of responsibility at a sufficiently high level in the organization to ensure adequate resources are provided for both the training and internal control system;
- Reasonable efforts to ensure that a contractor's leaders have not engaged in illegal conduct or conduct that violates the contractor's code of conduct;
- Periodic reviews of company practices, procedures, policies

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and internal compliance controls, including monitoring and auditing activities to detect criminal conduct;

- Periodic reviews of the effectiveness of the company's training and internal control programs;
- Periodic assessments of risk with appropriate steps to design, implement or modify the compliance training program and internal control system to reduce the identified risk;
- Disciplinary action for improper conduct or for failing to take reasonable steps to prevent or detect improper conduct.

The contractor should be aware that they could be in violation of their contract terms if these policies and procedures are not followed.

In these tough economic times, you cannot afford to miscalculate rates or not have the proper control in place. Missed opportunities could seriously affect your profitability and overall business. If you are unsure about reporting correct

rates or if you don't know if your company has implemented proper controls, you should consider having an outside advisor review your procedures. When conducting federally funded work, you need to identify ways to improve your profit margins on contracts and maximize your return by ensuring you are receiving all allowable costs under the FAR. Precise overhead rates are essential to being competitive and the proper controls are vital to your business success.

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