

## The Business Systems Rule

The viewpoint of the United States Government is that “contractor business systems and internal controls are the first line of defense against waste, fraud and abuse. Weak control systems increase the risk of unallowable and unreasonable costs on Government contracts.”

On February 24, 2012, the Department of Defense (“DOD”) issued the final “Business Systems Rule” which establishes mandatory requirements for contractor business systems.

The requirements, which are applicable to CAS-covered contracts awarded after May 18, 2011, impose mandatory financial penalties for any noncompliance that is deemed a “significant deficiency.” A significant deficiency is defined as: “shortcomings in the system that materially affect the ability of officials of the DOD to rely upon information produced by the system that is needed for management purposes.”

The lack of well-defined criteria for assessing a system deficiency and the vague terminology in the guidance poses an increased risk to contractors. Disapproved systems subject the contractor to withholdings of payments related to all billings under covered contracts of 5% for one disapproved system, or up to 10% for two or more disapproved systems.

The DoD Federal Acquisition Regulation Supplement (“DFARS”) outlines Business Systems Rule requirements for the following six contractor systems:

- Accounting System;
- Purchasing System;
- Estimating System;
- Material Management and Accounting System (“MMAS”);
- Earned Value Management System (“EVMS”); and
- Property Management System

DFARS provides some discretion to contractors for achieving compliance with these requirements. Contractors must establish a compliance baseline that sets forth what the contractor has determined is required, given its circumstances, to meet a particular business system requirement. Contractors must also be prepared to demonstrate their compliance with the requirements.

Though the Business Systems Rule was originally limited to DOD contractors, the requirements are being adopted by other government agencies as well.

The Defense Contract Audit Agency (“DCAA”) and Defense Contract Management Agency (“DCMA”) are assigned responsibility for audits and reviews of business systems. Specifically, DCAA is designated for performing audits of the Accounting, Estimating, and MMAS systems. DCMA is designated for auditing the EVMS, Purchasing, and Government Property systems.

In conjunction with the audits, contractor personnel who perform the processes/functions are expected to provide detailed demonstrations (walk-throughs) of the policies and procedures, practices, and processes that demonstrate how systems comply with the DFARS criteria. Personnel are expected to be knowledgeable of end-to-end processes, understand DFARS criteria, and provide documentation (e.g., flowcharts, narratives, etc.) to auditors that sufficiently help them understand the processes. Common controls across systems that will be considered include:

- Adequacy of current systems to meet compliance requirements;
- Adequacy of written policies and procedures;
- Employee knowledge and compliance with policies and procedures;
- Consistent application of policies and procedures; and
- Management review and remediation.

## The Chess Consulting Advantage

Our professionals have a track record of success assisting clients throughout the life cycle of a government contract including pre-award, post-award, and dispute-related matters. We bring to each engagement a unique combination of government contracting regulatory expertise, technical financial accounting and reporting knowledge, and an understanding of our client’s business processes, risks, and challenges.

With decades of government contracting compliance and financial reporting experience, as well as firsthand experience implementing the requirements of the Federal Acquisition Regulation, DFARS, Cost Accounting Standards, and Sarbanes-Oxley (“SOX”), our professionals are skilled in analyzing, testing, and modifying internal control systems and procedures.

Chess Consulting (“Chess”) assists contractors by ensuring that critical management and accounting systems withstand scrutiny by government agency or other third party auditors. Our professionals are recognized experts who understand the complex business and regulatory climate in which government contractors operate. We understand the nuances of the different industry risks and have experience tailoring our approach to properly assess the relevant criteria that will be used to evaluate a contractor’s compliance. Our team helps contractors interpret and understand government regulations, analyze and test effectiveness of current controls and procedures, assist with the preparation of policy manuals related to each critical system, and provide training to client personnel.

Notable client engagements include:

- *Publicly traded, international biopharmaceutical company.* Chess was engaged to evaluate and assess the adequacy of the company’s compliance with DFARS and other regulatory requirements. Tasks performed included, but were not limited to:
  - Evaluating the existing overall control environment;
  - Establishing the scope of work to determine the key systems and controls to assess;
  - Developing and tailoring control documentation, testing plans, and strategy to compare with key compliance regulations;
  - Documenting existing internal controls leveraging SOX controls as appropriate, assessing their effectiveness, and identifying control gaps;
  - Preparing recommendations to remediate identified control weaknesses and providing implementation assistance;
  - Identifying and exploiting process re-engineering opportunities to improve operational efficiencies; and
  - Providing training to client personnel to increase awareness regarding compliance requirements as well as the respective controls in place to address the requirements and mitigate risks.

Within one year after completing the assessment and remediating gaps, the company was subject to agency reviews of its EVMS and accounting systems and no deficiencies were identified by the agency auditors.

- *A publicly traded aerospace and defense contractor.* In conjunction with the company’s implementation of a fully integrated IT system, Chess was engaged to collaborate with the IT implementation team to evaluate, and identify opportunities to properly configure/enhance, the system structure to comply with DFARS and other regulatory requirements. The assessment included:

- Assessing, and providing a synopsis of, business system criteria that the company intended to address using system controls versus manual controls;
- Collaborating with process owners and system integrators to identify optional, user-defined fields that could be used to enhance data capture and automate certain internal controls;
- Prior to go-live, assisting with validation of system configuration (e.g. evaluating the adequacy of data capture and other system controls such as segregation of duties);
- After go-live, assisting with validation of data accuracy; and
- Collaborating with process owners to develop manual controls to mitigate risks not addressed as part of the system configuration.

## Chess Consulting Differentiators

**Deep industry knowledge** and technical expertise which helps clients deal effectively with the complexities of the processes and issues facing its business.

**Profitability focus** concentrating on actions and solutions that create a competitive business advantage while fully complying with regulatory requirements.

**Practical and creative solutions** that effectively address difficult compliance and business issues.

**Supportable positions** that have been proven to withstand scrutiny from regulatory agencies such as the SEC, DCAA, DOJ, and GAO.

**Reduced risk** of noncompliance with increasingly stringent SEC regulations.

**Ready access** to skilled resources.