

Recommendation 12: Require DCAA to obtain peer review from a qualified external organization.

Problem

Peer reviews are designed to validate a professional service organization's compliance with professional standards. The peer review process can provide valuable outside perspectives and insights to the organization. According to GAGAS, the peer reviewer must (a) understand GAGAS, (b) be independent from the organization subject to peer review, and (c) collectively have enough knowledge to perform the peer review.¹

DoDIG currently performs the peer review for DCAA; however, DoDIG's mission is vastly different than DCAA's and as a result the two organizations do not perform similar services. The audits DoDIG conducts are FAR different in scope, method, and purpose than contract audits conducted by DCAA.

Background

According to the Inspector General (IG) Act of 1978 (as amended), DoDIG is required to:

*(10) conduct, or approve arrangements for the conduct of, external peer reviews of Department of Defense audit agencies in accordance with and in such frequency as provided by Government auditing standards as established by the Comptroller General of the United States.*²

DoDIG has not exercised the option to use another organization to conduct peer review of DCAA. In addition to the peer review, the IG Act directs DoDIG to directly "monitor and evaluate" DCAA for its work, as well as checking DoD organizations' responses to contract audit recommendations.³

Findings

DoDIG cannot serve as an independent, qualified peer reviewer of DCAA while supervising DCAA in oversight of contract audits. More importantly, DoDIG auditors do not perform contract audits, do not advise contracting officers during preaward contract activity, and are not part of the acquisition team. For a peer review to be useful, the reviewer must be well-versed on how the professional standards apply to the services provided. The effect of the DoDIG peer review of DCAA is to further remove DCAA auditors from being advisors to contracting officers and members of the acquisition team.

The Blue Ribbon Commission on Defense Management (also referred to as the Packard Commission) recommended the Undersecretary of Defense (Acquisition) provide overall policy guidance for contract audits.⁴ At the time of the recommendation (and continuing to today), the DoDIG has the role of developing policy for contract audit and evaluating audit performance as well as the peer review of

¹ GAO, *Government Auditing Standards, 2011 Revision*, GAO-12-331G, accessed November 20, 2017, <http://www.gao.gov/assets/590/587281.pdf>.

² Inspector General Act of 1978, as amended, "Section 8, subsection (10)", accessed November 20, 2017, [https://www.ignet.gov/sites/default/files/files/igactasof1010\(1\).pdf](https://www.ignet.gov/sites/default/files/files/igactasof1010(1).pdf).

³ Ibid.

⁴ GAO, *Defense Management: Status of Recommendations by Blue Ribbon Commission on Defense Management*, GAO/NSIAD-89-19FS, 66, accessed November 24, 2017, <http://www.gao.gov/assets/90/88245.pdf>.

DCAA.⁵ GAO noted that DoD did not adopt the Packard Commission recommendation to improve the acquisition system by reforming contract audit performance due to the statutory assignment of contract audit policy development and oversight to DoDIG through the IG Act.⁶

Conclusions

DCAA peer review should be performed by an organization other than DoDIG. Congress should amend the targeted DoD-specific portions of the IG Act and other relevant sections of U.S. Code to DoDIG as the peer reviewer for DCAA.

DoDIG's continued monitoring and evaluation of DCAA's contract audits is problematic because DoDIG, as an enforcement agency, is not DCAA's peer. The conduct of a peer review by the IG creates a natural conflict and is not conducive to independent peer review espoused by audit standards. In contrast, an IPA can provide a peer review to DCAA that will accomplish the mission of a periodic peer review: professional review from similarly trained experts not otherwise responsible for the agency's day-to-day operations.

Implementation

Legislative Branch

- Revise 10 U.S.C. § 2313b(e) to require periodic peer review of DCAA by a commercial auditor.

Executive Branch

- Amend the targeted DoD-specific portions of the IG Act to remove DoDIG as the peer reviewer for DCAA.

Implications for Other Agencies

- There are no cross-agency implications for this recommendation.

⁵ Inspector General Act of 1978, as amended, "Section 8, subsection (10)", accessed November 20, 2017, [https://www.ignet.gov/sites/default/files/files/igactasof1010\(1\).pdf](https://www.ignet.gov/sites/default/files/files/igactasof1010(1).pdf).

⁶ GAO, *Defense Management: Status of Recommendations by Blue Ribbon Commission on Defense Management*, GAO/NSIAD-89-19FS, 66, accessed November 24, 2017, <http://www.gao.gov/assets/90/88245.pdf>.

Recommendations 6, 7, 8, and 12

1 from the contracting officer (and subject to any extension authorized pursuant to subsection (c)).
 2 The time limits in subsection (b) shall take effect on October 1, 2019.

3 “(b) TIME LIMITS.—

4 “(1) ON-DEMAND ACTIVITIES.—The following time limits shall apply under the
 5 procedures prescribed under subsection (a):

Matter for DCAA review	DCAA time limit
Contractor submission of pre-award cost proposal	90 days from date of contracting officer request for review
Contractor submission of invoices for direct contract costs	90 days from date of contracting officer request for review
Any other contractor submission in connection with awarding, administering, or terminating a particular contract	180 days from date of contracting officer request for review

6 “(2) PREDICTABLE ACTIVITIES.—The following time limits shall apply under the
 7 procedures prescribed under subsection (a):

Matter for DCAA review	DCAA time limit
Contractor submission of forward pricing rate proposal	90 days from date of contracting officer request for review
Contractor submission of provisional billing rate proposal	30 days from date of receipt of the contractor submission
Contractor submission of Cost Accounting Standards (CAS) disclosure statement	If the contracting officer requests DCAA review of the adequacy of the CAS disclosure statement, 60 days from date of contracting officer request for review

Contractor submission of cost accounting practice changes referred to as a General Dollar Magnitude (GDM) proposal	90 days from date of contracting officer request for review
Contractor submission of cost accounting practice changes referred to as a Detailed Cost Impact (DCI) proposal	180 days from date of contracting officer request for review
Contractor compliance with Cost Accounting Standards in accordance with the contractor's CAS disclosure statement	90 days from date of contracting officer request for review
Contractor compliance with an individual Cost Accounting Standard	90 days from date of contracting officer request for review

1 “(c) EXTENSIONS.—

2 “(1) AUTHORITY FOR EXTENSIONS.—The procedures prescribed under subsection
3 (a) shall provide that a contracting officer may grant an extension of a time limit under
4 this section (whether the applicable time limit is prescribed under subsection (b) or was
5 agreed to by DCAA at the time of the request from the contracting office). Those
6 procedures shall require that any such extension be recorded separately from the original
7 time limit.

8 “(2) TYPES OF EXTENSIONS.—Any such extension shall be categorized as one of
9 the following:

10 “(A) Contracting officer change.

11 “(B) DCAA request.

12 “(C) Contractor request or contractor caused.

13 “(3) REQUIREMENT AS TO CONTRACTOR REQUESTED OR CAUSED EXTENSIONS.—An
14 extension may not be categorized as having been requested or caused by a contractor

1 unless the contractor is informed that the extension will be so categorized. If the
2 contractor disagrees with that categorization, the contracting officer shall record such
3 disagreement.”.

4 (2) CLERICAL AMENDMENT.—The table of sections at the beginning of such
5 chapter is amended by inserting after the item relating to section 2313b the following new
6 item:

“2313c. DCAA review of contractor submissions and contractor compliance: time limits.”.

7 (b) TIMELINESS OF INCURRED COST AUDITS.—

8 (1) CONSISTENCY WITH NEW SECTION 2313C.—Subsection (g) of section 2313b of
9 title 10, United States Code, is amended—

10 (A) by striking paragraph (2);

11 (B) by redesignating paragraph (3) as paragraph (2) and in that
12 paragraph—

13 (i) by striking “qualified” both places it appears; and

14 (ii) by striking “on or after the date of the enactment of this
15 section” and inserting “after December 11, 2017.”;

16 (C) by redesignating paragraph (4) as paragraph (3) and in that
17 paragraph—

18 (i) by striking “paragraph (5)” and inserting “paragraph (4)”; and

19 (ii) by striking “qualified”; and

20 (D) by redesignating paragraph (5) as paragraph (4) and in that
21 paragraph—

22 (i) by striking “The Under Secretary of Defense (Comptroller) may
23 waive the requirements of paragraph (4) on a case-by-case basis” and

1 inserting “(A) The contracting officer (or an official within the contracting
2 activity senior to the contracting officer) may grant an extension of the
3 time limit under paragraph (2) for issuance of audit findings for an
4 incurred cost submission and may waive the requirements of paragraph (3)
5 with respect to the period of any such extension. Any such extension and
6 waiver may only be made on a case-by-case basis and only”;

7 (ii) by designating the sentence beginning “The Director of” as
8 subparagraph (B) and in that subparagraph—

9 (I) by inserting “for any fiscal year” after “of this title”; and

10 (II) by inserting “under this paragraph during such fiscal
11 year” after “waivers issued”; and

12 (iii) by adding at the end the following new subparagraphs:

13 “(C) The provisions of section 2313c(c) of this title shall apply to an extension granted
14 under this paragraph.

15 “(4) A time limit under this subsection for issuance of audit findings for an incurred cost
16 submission does not apply in a case in which the contractor requests a multiyear audit and the
17 contracting officer (or an official within the contracting activity senior to the contracting officer)
18 approves.”.

19 (b) CONFORMING AND TECHNICAL AMENDMENTS.—Such section is further amended—

20 (1) in subsection (b)(1)—

21 (A) in subparagraph (B), by striking “a qualified incurred” and inserting
22 “an incurred”; and

23 (B) in subparagraph (E)—

- 1 (i) by redesignating clauses (A) and (B) as clauses (i) and (ii),
2 respectively;
- 3 (ii) by striking “a qualified incurred” in clause (i) (as so
4 redesignated) and inserting “an incurred”; and
- 5 (iii) by striking “more than 12 months before the date of the
6 enactment of this section” and inserting “before December 12, 2016”; and
- 7 (2) in subsection (i)—
- 8 (A) by striking paragraph (6); and
- 9 (B) by redesignating paragraph (7) as paragraph (6).

10 **SEC. 202. PEER REVIEW OF DEFENSE CONTRACT AUDIT AGENCY.**

11 (a) REMOVAL OF DCAA PEER REVIEWS FROM DoD IG. —Section 8(c)(10) of the
12 Inspector General Act of 1978 (5 U.S.C. App) is amended by inserting before the period at the
13 end the following: “, except that this paragraph does not apply to the Defense Contract Audit
14 Agency”.

15 (b) REQUIREMENT FOR DCAA PEER REVIEW BY COMMERCIAL AUDITOR.—Section
16 2313b(e) of title 10, United States Code, is amended—

- 17 (1) by redesignating paragraph (2) as paragraph (3);
- 18 (2) by designating the second sentence of paragraph (1) as paragraph (2) ; and
- 19 (3) in paragraph (2), as so designated, by inserting before “Such peer review” the
20 following: “The Secretary of Defense shall provide for periodic peer review of the
21 Defense Contract Audit Agency by a commercial auditor.”.

22 **SEC. 203. DEFENSE CONTRACT AUDIT AGENCY ANNUAL REPORT.**

1 (a) REVISIONS TO REPORT ELEMENTS.—Subsection (a) of section 2313a of title 10, United
2 States Code, is amended—

3 (1) in paragraph (1), by striking “significant” and all that follows and inserting
4 “the regulatory requirements that create compliance difficulties for contractors, including
5 an analysis of how those regulatory requirements affect contractors of different sizes and
6 industries;”;

7 (2) in paragraph (2)—

8 (A) by striking subparagraphs (A) through (E) and inserting the following:

9 “(A) the total number of new audit or advisory engagements, by type (pre-
10 award, incurred cost, other post-award, and business system), with time limits
11 expiring during the fiscal year that were completed or were awaiting completion,
12 as compared to total audit and advisory engagements completed or awaiting
13 completion during the year;

14 “(B) on-time performance relative to time limits for each type of audit or
15 advisory engagement (shown separately for the Defense Contract Audit Agency
16 and qualified private auditors retained by the agency);

17 “(C) the time limit (expressed in days) for each type of audit or advisory
18 engagement, along with the shortest period, longest period, and average period of
19 actual performance (shown separately for the Defense Contract Audit Agency and
20 qualified private auditors retained by the agency);

21 “(D) for pre-award audits and advisory engagements of contractor costs,
22 sustained costs as a total number and as a percentage of total questioned costs,
23 where questioned costs are expressed as the impact on negotiable contract costs

1 (shown separately for the Defense Contract Audit Agency and qualified private
2 auditors retained by the agency);

3 “(E) for post-award audits and advisory engagements of contractor costs,
4 the questioned costs accepted by the contracting officers and contractors as a total
5 number and as a percentage of total questioned costs, where questioned costs are
6 expressed as the impact on reimbursable contract (shown separately for the
7 Defense Contract Audit Agency and qualified private auditors retained by the
8 agency);” and

9 (B) in subparagraph (H)—

10 (i) by inserting “post-award” after “dollar value of”; and

11 (ii) by striking “submission” and inserting “proposal”;

12 (3) by redesignating paragraphs (3), (4), (5), (6), and (7) as paragraphs (4), (5),
13 (6), (7), and (9), respectively;

14 (4) by inserting after paragraph (2) the following new paragraph (3):

15 “(3) A summary of the reasons for the difference between questioned and
16 sustained costs shown in the statistical tables under paragraph (2).”;

17 (5) in paragraph (4) (as redesignated by paragraph (3) of this subsection), by
18 striking “needed to improve the audit process;” and inserting “needed by the Defense
19 Contract Audit Agency to improve the audit process or that would enhance compliance
20 with regulatory requirements.”;

21 (6) in paragraph (7) (as redesignated by paragraph (3) of this subsection), by
22 striking “more effective use of audit resources;” and inserting “contract compliance and

1 professional development of the Defense Contract Audit Agency workforce (shown
2 separately for collaborative outreach actions and other outreach actions).”; and

3 (7) by inserting after paragraph (7) (as redesignated by paragraph (3) of this
4 subsection) the following new paragraph:

5 “(8) A statistically representative survey of contracting officers from Department
6 of Defense buying commands, the Defense Contract Management Agency, and small and
7 large business representatives from industry to measure the timeliness and effectiveness
8 of audit and advisory services provided (shown separately for the Defense Contract Audit
9 Agency and qualified private auditors retained by the Defense Contract Audit Agency).”.

10 (b) CONFORMING AMENDMENTS.—Subsection (a) of such section is further amended—

11 (1) in the matter preceding paragraph (1), by striking “shall include, at a
12 minimum—“ and inserting “shall include the following.”;

13 (2) by capitalizing the first letter following the paragraph designation in each of
14 paragraphs (1), (2), (4), (5), (6), (7), and (9); and

15 (3) by striking the semicolon at the end of each of paragraphs (1), (2), (5), and (6)
16 and inserting a period.

17 (c) DEFINITIONS.—Subsection (d)(1) of such section is amended by striking “qualified
18 incurred cost submission” and inserting “qualified private auditor”.

19 (d) EFFECTIVE DATE.—The amendments made by this section shall take effect on
20 October 1, 2020.

21 **SEC. 204. REVIEW OF ROLES OF DEFENSE CONTRACT AUDIT AGENCY AND**
22 **DEFENSE CONTRACT MANAGEMENT AGENCY.**

1 (a) REVIEW.—The Secretary of Defense, acting through the Chief Management Officer of
2 the Department of Defense, shall direct the Under Secretary of Defense for Acquisition and
3 Sustainment and the Under Secretary of Defense (Comptroller) to conduct a joint review of the
4 functions of the Defense Contract Management Agency and the Defense Contract Audit Agency
5 to determine whether there are functions being performed by either Agency that could more
6 appropriately be performed by the other Agency. The review shall consider the extent to which
7 redundancies exist between the two Agencies and how best to align the functions and workload
8 of the two Agencies to best serve the acquisition community.

9 (b) REPORT.—The Under Secretaries shall submit to the Secretary of Defense a report
10 with the results of the review under subsection (a) not later than 180 days after the date of the
11 enactment of this Act. The report shall include a draft of any statutory or regulatory change
12 needed to implement recommendations of the review.

SECTIONS AFFECTED BY THE PROPOSAL

[The material below shows changes proposed to be made by the proposal to the text of existing statutes. Matter proposed to be deleted is shown in ~~stricken through~~ text; matter proposed to be inserted is shown in *bold italic*. (Where an amendment in the proposal would add a full new section to existing law, the text of that proposed new section is NOT set forth below since it is set out in full in the legislative text above.)]

[NOTE: Text shown as current law incorporates amendments made by the FY2018 NDAA, Public Law 115-91, enacted Dec. 12, 2017]

Section 8 of the Inspector General Act of 1978

SEC. 8. ADDITIONAL PROVISIONS WITH RESPECT TO THE INSPECTOR GENERAL OF THE DEPARTMENT OF DEFENSE.

(a) No member of the Armed Forces, active or reserve, shall be appointed Inspector General of the Department of Defense.

(b)(1) Notwithstanding the last two sentences of section 3(a), the Inspector General shall be under the authority, direction, and control of the Secretary of Defense with respect to audits or investigations, or the issuance of subpoenas, which require access to information concerning—

- (A) sensitive operational plans;
- (B) intelligence matters;
- (C) counterintelligence matters;
- (D) ongoing criminal investigations by other administrative units of the Department of Defense related to national security; or
- (E) other matters the disclosure of which would constitute a serious threat to national security.

(2) With respect to the information described in paragraph (1) the Secretary of Defense may prohibit the Inspector General from initiating, carrying out, or completing any audit or investigation, from accessing information described in paragraph (1), or from issuing any subpoena, after the Inspector General has decided to initiate, carry out or complete such audit or investigation, access such information, or to issue such subpoena, if the Secretary determines that such prohibition is necessary to preserve the national security interests of the United States.

(3) If the Secretary of Defense exercises any power under paragraph (1) or (2), the Inspector General shall submit a statement concerning such exercise within thirty days to the Committees on Armed Services and Governmental Affairs of the Senate and the Committee on Armed Services and the Committee on Government Reform and Oversight of the House of Representatives and to other appropriate committees or subcommittees of the Congress.

(4) The Secretary shall, within thirty days after submission of a statement under paragraph (3), transmit a statement of the reasons for the exercise of power under paragraph (1) or (2) to the congressional committees specified in paragraph (3) and to other appropriate committees or subcommittees.

(c) In addition to the other duties and responsibilities specified in this Act, the Inspector General of the Department of Defense shall—

- (1) be the principal adviser to the Secretary of Defense for matters relating to the prevention and detection of fraud, waste, and abuse in the programs and operations of the Department;
- (2) initiate, conduct, and supervise such audits and investigations in the Department of Defense (including the military departments) as the Inspector General considers appropriate;
- (3) provide policy direction for audits and investigations relating to fraud, waste, and abuse and program effectiveness;
- (4) investigate fraud, waste, and abuse uncovered as a result of other contract and internal audits, as the Inspector General considers appropriate;
- (5) develop policy, monitor and evaluate program performance, and provide guidance with respect to all Department activities relating to criminal investigation programs;
- (6) monitor and evaluate the adherence of Department auditors to internal audit, contract audit, and internal review principles, policies, and procedures;

(7) develop policy, evaluate program performance, and monitor actions taken by all components of the Department in response to contract audits, internal audits, internal review reports, and audits conducted by the Comptroller General of the United States;

(8) request assistance as needed from other audit, inspection, and investigative units of the Department of Defense (including military departments);

(9) give particular regard to the activities of the internal audit, inspection, and investigative units of the military departments with a view toward avoiding duplication and insuring effective coordination and cooperation; and

(10) conduct, or approve arrangements for the conduct of, external peer reviews of Department of Defense audit agencies in accordance with and in such frequency as provided by Government auditing standards as established by the Comptroller General of the United States, *except that this paragraph does not apply to the Defense Contract Audit Agency.*

(d) ***

Title 10, United States Code

§ 2313a. [current law shown as in effect on October 1, 2018] Defense Contract Audit Agency: annual report

(a) REQUIRED REPORT.—The Director of the Defense Contract Audit Agency shall prepare an annual report of the activities of the Agency during the previous fiscal year. The report shall include, ~~at a minimum~~—*the following*:

(1) ~~[a] A description of significant problems, abuses, and deficiencies encountered during the conduct of contractor audits~~ *the regulatory requirements that create compliance difficulties for contractors, including an analysis of how those regulatory requirements affect contractors of different sizes and industries*[:].

(2) ~~[s] Statistical tables showing—~~

~~(A) the total number and dollar value of audit reports completed and pending, set forth separately by type of audit;~~

~~(B) the priority given to each type of audit;~~

~~(C) the length of time taken for each type of audit, both from the date of receipt of a qualified incurred cost submission and from the date the audit begins;~~

~~(D) the sustained questioned costs, set forth separately by type of audit, both as a total value and as a percentage of the total questioned costs for the audit;~~

~~(E) the total number and dollar value of incurred cost audits completed, and the method by which such incurred cost audits were completed;~~

(A) the total number of new audit or advisory engagements, by type (pre-award, incurred cost, other post-award, and business system), with time limits expiring during the fiscal year that were completed or were awaiting completion, as compared to total audit and advisory engagements completed or awaiting completion during the year;

(B) on-time performance relative to time limits for each type of audit or advisory engagement (shown separately for the Defense Contract Audit Agency and qualified private auditors retained by the agency);

(C) the time limit (expressed in days) for each type of audit or advisory engagement, along with the shortest period, longest period, and average period of actual performance (shown separately for the Defense Contract Audit Agency and qualified private auditors retained by the agency);

(D) for pre-award audits and advisory engagements of contractor costs, sustained costs as a total number and as a percentage of total questioned costs, where questioned costs are expressed as the impact on negotiable contract costs (shown separately for the Defense Contract Audit Agency and qualified private auditors retained by the agency);

(E) for post-award audits and advisory engagements of contractor costs, the questioned costs accepted by the contracting officers and contractors as a total number and as a percentage of total questioned costs, where questioned costs are expressed as the impact on reimbursable contract (shown separately for the Defense Contract Audit Agency and qualified private auditors retained by the agency);

(F) the aggregate cost of performing audits, set forth separately by type of audit;

(G) the ratio of sustained questioned costs to the aggregate costs of performing audits, set forth separately by type of audit; and

(H) the total number and dollar value of *post-award* audits that are pending for a period longer than one year as of the end of the fiscal year covered by the report, and the fiscal year in which the qualified ~~submission~~ *proposal* was received, set forth separately by type of audit[;] .

(3) A summary of the reasons for the difference between questioned and sustained costs shown in the statistical tables under paragraph (2).

~~(3)~~(4) [a] A summary of any recommendations of actions or resources needed by *the Defense Contract Audit Agency* to improve the audit process *or that would enhance compliance with regulatory requirements*[;] .

~~(4)~~ (5) [a] A summary, set forth separately by dollar amount and percentage, of indirect costs for independent research and development incurred by contractors in the previous fiscal year[;] .

~~(5)~~ (6) [a] A summary, set forth separately by dollar amount and percentage, of indirect costs for bid and proposal costs incurred by contractors in the previous fiscal year[;] .

~~(6)~~ (7) [a] A description of outreach actions toward industry to promote ~~more~~ *effective use of audit resources; contract compliance and professional development of the Defense Contract Audit Agency workforce (shown separately for collaborative outreach actions and other outreach actions).*

(8) *A statistically representative survey of contracting officers from Department of Defense buying commands and the Defense Contract Management Agency and representatives of small and large businesses to measure the timeliness and effectiveness of audit and advisory services provided by the Defense Contract Audit*

Agency (shown separately for the Defense Contract Audit Agency and qualified private auditors retained by the agency).

(7) (9) [a] Any other matters the Director considers appropriate.

(b) SUBMISSION OF ANNUAL REPORT.—Not later than March 30 of each year, the Director shall submit to the congressional defense committees the report required by subsection (a).

(c) PUBLIC AVAILABILITY.—Not later than 60 days after the submission of an annual report to the congressional defense committees under subsection (b), the Director shall make the report available on the publicly available website of the Agency or such other publicly available website as the Director considers appropriate.

(d) DEFINITIONS.—

(1) The terms “incurred cost audit” and “~~qualified incurred cost submission~~ *qualified private auditor*” have the meaning given those terms in section 2313b of this title.

(2) The term “sustained questioned costs” means questioned costs that were recovered by the Federal Government as a result of contract negotiations related to such questioned costs.

§ 2313b. Performance of incurred cost audits

(a) COMPLIANCE WITH STANDARDS OF RISK AND MATERIALITY.—Not later than October 1, 2020, the Secretary of Defense shall comply with commercially accepted standards of risk and materiality in the performance of each incurred cost audit of costs associated with a contract of the Department of Defense.

(b) CONDITIONS FOR THE USE OF QUALIFIED AUDITORS TO PERFORM INCURRED COST AUDITS.—(1) To support the need of the Department of Defense for timely and effective incurred cost audits, and to ensure that the Defense Contract Audit Agency is able to allocate resources to higher-risk and more complex audits, the Secretary of Defense shall use qualified private auditors to perform a sufficient number of incurred cost audits of contracts of the Department of Defense to—

(A) eliminate, by October 1, 2020, any backlog of incurred cost audits of the Defense Contract Audit Agency;

(B) ensure that incurred cost audits are completed not later than one year after the date of receipt of ~~a qualified an~~ incurred cost submission;

(C) maintain an appropriate mix of Government and private sector capacity to meet the current and future needs of the Department of Defense for the performance of incurred cost audits;

(D) ensure that qualified private auditors perform incurred cost audits on an ongoing basis to improve the efficiency and effectiveness of the performance of incurred cost audits; and

(E) limit multiyear auditing to ensure that multiyear auditing is conducted only—

(A) (i) to address outstanding incurred cost audits for which ~~a qualified an~~ incurred cost submission was submitted to the Defense Contract Audit Agency

~~more than 12 months before the date of the enactment of this section~~ *before December 12, 2016*; or

(B) (ii) when the contractor being audited submits a written request, including a justification for the use of multiyear auditing, to the Under Secretary of Defense (Comptroller).

(2) The Secretary of Defense shall consult with Federal agencies that have awarded contracts or task orders to qualified private auditors to ensure that the Department of Defense is using, as appropriate, best practices relating to contracting with qualified private auditors.

(3) The Secretary of Defense shall ensure that a qualified private auditor performing an incurred cost audit under this section—

(A) has no conflict of interest in performing such an audit, as defined by generally accepted government auditing standards;

(B) possesses the necessary independence to perform such an audit, as defined by generally accepted government auditing standards;

(C) signs a nondisclosure agreement, as appropriate, to protect proprietary or nonpublic data;

(D) accesses and uses proprietary or nonpublic data furnished to the qualified private auditor only for the purposes stated in the contract;

(E) takes all reasonable steps to protect proprietary and nonpublic data furnished during the audit; and

(F) does not use proprietary or nonpublic data provided to the qualified private auditor under the authority of this section to compete for Government or nongovernment contracts.

(c) PROCEDURES FOR THE USE OF QUALIFIED PRIVATE AUDITORS.—(1) Not later than October 1, 2018, the Secretary of Defense shall submit to the congressional defense committees a plan to implement the requirements of subsection (b). Such plan shall include, at a minimum—

(A) a description of the incurred cost audits that the Secretary determines are appropriate to be conducted by qualified private auditors, including the approximate number and dollar value of such incurred cost audits;

(B) an estimate of the number and dollar value of incurred cost audits to be conducted by qualified private auditors for each of the fiscal years 2019 through 2025 necessary to meet the requirements of subsection (b); and

(C) all other elements of an acquisition plan as required by the Federal Acquisition Regulation.

(2) Not later than April 1, 2019, the Secretary of Defense or a Federal department or agency authorized by the Secretary shall award a contract or issue a task order under an existing contract to two or more qualified private auditors to perform incurred cost audits of costs associated with contracts of the Department of Defense. The Defense Contract Management Agency or a contract administration office of a military department shall use a contract or a task order awarded or issued pursuant to this paragraph for the performance of an incurred cost audit, if doing so will assist the Secretary in meeting the requirements in subsection (b).

(3) To improve the quality of incurred cost audits and reduce duplication of performance of such audits, the Secretary of Defense may provide a qualified private auditor with information on past or ongoing audit results or other relevant information on the entities the qualified private auditor is auditing.

(4) The Secretary of Defense shall consider the results of an incurred cost audit performed under this section without regard to whether the Defense Contract Audit Agency or a qualified private auditor performed the audit.

(5) The contracting officer for a contract that is the subject of an incurred cost audit shall have the sole discretion to determine what action should be taken based on an audit finding on direct costs of the contract.

(d) QUALIFIED PRIVATE AUDITOR REQUIREMENTS.—(1) A qualified private auditor awarded a contract or issued a task order under subsection (c)(2) shall conduct an incurred cost audit in accordance with the generally accepted government auditing standards.

(2) A qualified private auditor awarded a contract or issued a task order under subsection (c)(2) shall develop and maintain complete and accurate working papers on each incurred cost audit. All working papers and reports on the incurred cost audit prepared by such qualified private auditor shall be the property of the Department of Defense, except that the qualified private auditor may retain a complete copy of all working papers to support such reports made pursuant to this section.

(3) A breach of contract by a qualified private auditor with respect to use of proprietary or nonpublic data may subject the qualified private auditor to—

(A) criminal, civil, administrative, and contractual actions for penalties, damages, and other appropriate remedies by the United States; and

(B) civil actions for damages and other appropriate remedies by the contractor or subcontractor whose data are affected by the breach.

(e) PEER REVIEW.—(1) Effective October 1, 2022, the Defense Contract Audit Agency may issue unqualified audit findings for an incurred cost audit only if the Defense Contract Audit Agency is peer reviewed by a commercial auditor and passes such peer review.

(2) ***The Secretary of Defense shall provide for periodic peer review of the Defense Contract Audit Agency by a commercial auditor.*** Such peer review shall be conducted in accordance with the peer review requirements of generally accepted government auditing standards, including the requirements related to frequency of peer reviews, and shall be deemed to meet the requirements of the Defense Contract Audit Agency for a peer review under such standards.

(2) (3) Not later than October 1, 2019, the Secretary of Defense shall provide to the Committees on Armed Services of the Senate and the House of Representatives an update on the process of securing a commercial auditor to perform the peer review referred to in paragraph (1).

(f) NUMERIC MATERIALITY STANDARDS FOR INCURRED COST AUDITS.—(1) Not later than October 1, 2020, the Department of Defense shall implement numeric materiality standards for incurred cost audits to be used by auditors that are consistent with commercially accepted standards of risk and materiality.

(2) Not later than October 1, 2019, the Secretary of Defense shall submit to the congressional defense committees a report containing proposed numeric materiality standards required under paragraph (1). In developing such standards, the Secretary shall consult with commercial auditors that conduct incurred cost audits, the advisory panel authorized under section 809 of the National Defense Authorization Act for Fiscal Year 2016 (Public Law 114-92; 129 Stat. 889), and other governmental and nongovernmental entities with relevant expertise.

(g) **TIMELINESS OF INCURRED COST AUDITS.**—(1) The Secretary of Defense shall ensure that all incurred cost audits performed by qualified private auditors or the Defense Contract Audit Agency are performed in a timely manner.

~~(2) The Secretary of Defense shall notify a contractor of the Department of Defense within 60 days after receipt of an incurred cost submission from the contractor whether the submission is a qualified incurred cost submission.~~

~~(3) (2)~~ With respect to **qualified** incurred cost submissions received ~~on or after the date of the enactment of this section~~ *after December 11, 2017*, audit findings shall be issued for an incurred cost audit not later than one year after the date of receipt of such **qualified** incurred cost submission.

~~(4) (3)~~ Not later than October 1, 2020, and subject to paragraph ~~(5) (4)~~, if audit findings are not issued within one year after the date of receipt of a **qualified** incurred cost submission, the audit shall be considered to be complete and no additional audit work shall be conducted.

~~(5) (4)(A) The Under Secretary of Defense (Comptroller)~~ *The contracting officer (or an official within the contracting activity senior to the contracting officer) may grant an extension of the time limit under paragraph (2) for issuance of audit findings for an incurred cost submission and may waive the requirements of paragraph (4) (3) with respect to the period of any such extension. Any such extension and waiver may only be made on a case-by-case basis and only if the Director of the Defense Contract Audit Agency submits a written request.*

(B) The Director of the Defense Contract Audit Agency shall include in the report required under section 2313a of this title for any fiscal year the total number of waivers issued under this paragraph during such fiscal year and the reasons for issuing each such waiver.

(C) The provisions of section 2313c(c) of this title shall apply to an extension granted under this paragraph.

(5) A time limit under this subsection for issuance of audit findings for an incurred cost submission does not apply in a case in which the contractor requests a multiyear audit and the contracting officer (or an official within the contracting activity senior to the contracting officer) approves.

(h) **REVIEW OF AUDIT PERFORMANCE.**—Not later than April 1, 2025, the Comptroller General of the United States shall submit to the congressional defense committees a report that evaluates for the period beginning on October 1, 2019, and ending on August 31, 2023—

(1) the timeliness, individual cost, and quality of incurred cost audits, set forth separately by incurred cost audits performed by the Defense Contract Audit Agency and by qualified private auditors;

(2) the cost to contractors of the Department of Defense for incurred cost audits, set forth separately by incurred cost audits performed by the Defense Contract Audit Agency and by qualified private auditors;

(3) the effect, if any, on other types of audits conducted by the Defense Contract Audit Agency that results from incurred cost audits conducted by qualified private auditors; and

(4) the capability and capacity of qualified private auditors to conduct incurred cost audits for the Department of Defense.

(i) **DEFINITIONS.**—In this section:

(1) The term “commercial auditor” means a private entity engaged in the business of performing audits.

(2) The term “incurred cost audit” means an audit of charges to the Government by a contractor under a flexibly priced contract.

(3) The term “flexibly priced contract” has the meaning given the term “flexibly-priced contracts and subcontracts” in part 30 of the Federal Acquisition Regulation (section 30.001 of title 48, Code of Federal Regulations).

(4) The term “generally accepted government auditing standards” means the generally accepted government auditing standards of the Comptroller General of the United States.

(5) The term “numeric materiality standard” means a dollar amount of misstatements, including omissions, contained in an incurred cost audit that would be material if the misstatements, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the Government made on the basis of the incurred cost audit.

~~(6) The term “qualified incurred cost submission” means a submission by a contractor of costs incurred under a flexibly priced contract that has been qualified by the Department of Defense as sufficient to conduct an incurred cost audit.~~

(7) (6) The term “qualified private auditor” means a commercial auditor—

(A) that performs audits in accordance with generally accepted government auditing standards; and

(B) that has received a passing peer review rating, as defined by generally accepted government auditing standards.

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