

Training Information – Indirect Rate Analysis

**SUBJECT: “GOVERNMENT-SITE OVERHEAD RATES” and
 “MODIFIED OVERHEAD RATES” VS “CONTRACTOR-
 SITE OVERHEAD RATES” FOR CSS/CONTRACTOR
 STAFF EFFORT REQUIRED BY
 RFP/SOLICITATION/CONTRACT TO BE PERFORMED
 AT MILITARY INSTALLATIONS/RENTAL OFFICES.**

“The physical location of where the contractor’s employees will be working on a daily basis is very important.” This can be a much-overlooked consideration for many procurement officials. The contractor with a strong cost maximization objective *and* common sense may consider taking advantage of the Government’s lack of understanding with regard to the impact of indirect rates on total procurement prices. Lack of a Government requirement for a contractor submission of a Government-Site Overhead Rate or a Modified Overhead Rate in cases where the required work is to be performed on a Government facility “*almost always*” results in excessive Government payment of indirect costs (e.g. fringe, overhead, G&A) and associated fee. Profitable companies know how to read an RFP and will take advantage of every opportunity for cost maximization. The difference between a Government-Site Overhead Rate and a full Contractor-Site Overhead Rate is typically rather significant. In many cases a contractor’s Modified Overhead Rate is more practical for the small business that bids staff and/or provides staff for daily work over extended periods of time at a military installation/office space wherein the government customer is paying for the office space, etc.

“Government-Site Overhead Rates should be based on *eliminating*, from the overhead pool, those indirect costs that do **not** benefit Government-Site activities/work to be performed at the Government-Site.”

Purification of the indirect overhead cost pool as discussed below is extremely important to ensure that the Government is not paying for something that is **not** related to the immediate purchase/procurement which in terms of classic CPFF service type contracts; is mostly direct labor hours from the contractor for work that will be performed at the Government site (e.g. military installation, government rented offices, etc.). When the Government issues a properly prepared adequate solicitation/RFP document and then accepts a full Contractor-Site Overhead Rate (i.e.... indirect cost pool, etc.) instead of an equitable Modified Overhead Rate or a Government-Site Overhead Rate, the Government is in most cases “*overpaying*” and effectively paying the contractor for all of the typical overhead costs listed below; that in many cases have *absolutely no relevancy* to the immediate purchase of “direct labor hours” for effort to be completed at a workstation/desk/cube on the Government-Site (e.g. military installation, etc.).

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Government-Site Overhead Pools that pertain to contractor work to be performed at specific customer sites (e.g. military installations, etc.) are utilized to accumulate indirect overhead costs specific to the particular site. The site-specific indirect cost overhead pool often described, as the “Government-Site Overhead Rate” and the “Modified Overhead Pool” should **NOT** in most cases, include contractor costs such as:

- 1) *Indirect labor* and associated fringe costs because the Government is NOT typically buying indirect labor for Government-Site work. There “may” be *minimal* Supervisory/Indirect Labor and associated fringe costs placed in the Government-Site Overhead Pool or Modified Overhead Pool depending upon whether or not there is a Program Manager *or* Site Manager charged direct to manage the program or project whom would be managing the contractor’s staff that is working on the Government-site. A contractor may attempt to incorporate a significant amount of indirect Supervisory level labor costs into a developed rate for obvious reasons. Only an equitable amount of indirect labor and associated fringe costs would typically be reasonable and consistent with the properly prepared RFP/Solicitation – contract requirements should be considered.
- 2) Rental cost associated with the contractor’s office(s)
- 3) Utility cost associated with the contractor’s office(s)
- 4) Real estate tax costs associated with the contractor’s office(s)
- 5) Heating costs associated with the contractor’s office(s)
- 6) Building/office repairs and maintenance associated with the contractor’s office(s)
- 7) Building Insurance costs associated with the contractor’s office(s)
- 8) Property grounds repairs and maintenance associated with the contractor’s office(s)
- 9) Property-umbrella insurance costs associated with the contractor’s office(s)
- 10) Building/office depreciation costs associated with the contractor’s office(s)
- 11) Furniture & Equipment depreciation costs associated with the contractor’s office(s)
- 12) Amortization of leasehold improvements costs associated with the contractor’s office(s)
- 13) Permits and Licenses costs associated with the contractor’s office(s)
- 14) Office Supplies associated with the contractor’s office(s)
- 15) Other general costs associated with facilities because facilities are furnished by the Government

In addition, only equitable shares of “general business, employee payroll taxes, employer paid payroll taxes, and benefit costs” applicable to each of the contractor’s staff assigned to work on the Government-Site; would be included in the Government-Site Overhead Rate or Modified Overhead Rate. *Again*, such costs would only be the costs relevant to each of the contractor’s employees assigned to work in office space or workstations at the Government-Site (e.g. military installation, etc.). The following types of *general business expenses* are just another sampling of indirect costs that in many cases may **NOT** be allocable to the Government-Site Overhead Pool:

- a. *Indirect Travel* costs – because there is no expected indirect travel to take place by the contractor’s staff that is working on the Government-Site.
- b. *Temporary Help* costs – for the same concept/reason stated above in Item a.
- c. *Relocation* costs - for the same concept/reason stated above in Item a.
- d. *Business meal* costs - for the same concept/reason stated above in Item a.
- e. *Telephone* costs (Main Office land line/receptionist) - for the same concept/reason stated above in Item a.
- f. *Cell Phones* - because the Government-site desk has a telephone – a cell phone is normally only acceptable for positions that require immediate contact of the contractor employee by the Government staff for which the contractor is providing direct labor support services.
- g. *Telecopies* costs – Government copier machine and supplies would typically be used.
- h. *Restructuring* costs - for the same concept/reason stated above in Item a.
- i. *Dues, membership* costs - for the same concept/reason stated above in Item a.
- j. *Indirect Labor for Program Manager or Project Manager* - for the same concept/reason stated above in Item a.

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Remember, as per FAR 15-401-1(c)(2)(ii) “in conducting the evaluation of the effect of the offeror’s current practices on future costs, the contracting officer shall ensure that the effects of inefficient or uneconomical past practices are NOT projected into the future.” Furthermore, FAR 31.203 (f) states that “separate cost groupings for costs allocable to offsite locations may be necessary to permit equitable distribution of costs on the basis of the benefits accruing to the several cost objectives.”

Sources used/quoted for the above material include:

1. DCAA Audit Manual
2. Contract Pricing and Reference Guide, Volume 3, Chapter 9
3. Federal Acquisition Regulations
4. Accounting for Government Contracts (Matthew Bender)

For Public Reference Purposes:

File Name: Training Notes for Discussion of Contractor-Site Overhead Rates vs Government-Site Overhead Rates