

# SIGAR

Special Inspector General for  
Afghanistan Reconstruction

SIGAR 18-07 Financial Audit

## U.S. Army Contracting Command's Interim Contractor Training Support for the Afghan National Army to Maintain and Sustain Mobile Strike Force Vehicles: Audit of Costs Incurred by Textron Inc. Marine & Land Systems

**In accordance with legal requirements, SIGAR has redacted certain information deemed  
proprietary or otherwise sensitive from this report.**



OCTOBER  
2017

# SIGAR

## Special Inspector General for Afghanistan Reconstruction

### WHAT THE AUDIT REVIEWED

On August 31, 2015, the U.S. Army Contracting Command (ACC) awarded a \$17,434,922 contract to Textron Inc. Marine & Land Systems (Textron) to provide interim contractor training support, including mentorship, supply support, and parts management, for the Afghan National Army (ANA). The contract's purpose was to enable the ANA to become self-sufficient in maintaining and sustaining its fleet of Mobile Strike Force Vehicles. After three modifications, the contract's funding increased to \$23,723,646, and the period of performance was extended from August 31, 2016, to February 28, 2017.

SIGAR's financial audit, performed by Mayer Hoffman McCann (MHM), reviewed \$8,011,422 in expenditures that Textron charged to the contract for the period from August 31, 2015, through August 31, 2016. The objectives of the audit were to (1) identify and report on material weaknesses or significant deficiencies in Textron's internal controls related to the contract; (2) identify and report on instances of material noncompliance with the terms of the contract and applicable laws and regulations, including any potential fraud or abuse; (3) determine and report on whether Textron has taken corrective action on prior findings and recommendations; and (4) express an opinion on the fair presentation of Textron's Special Purpose Financial Statement (SPFS). See MHM's report for the precise audit objectives.

In contracting with an independent audit firm and drawing from the results of the audit, SIGAR is required by auditing standards to review the audit work performed. Accordingly, SIGAR oversaw the audit and reviewed its results. Our review disclosed no instances where MHM did not comply, in all material respects, with U.S. generally accepted government auditing standards.

October 2017

### U.S. Army Contracting Command's Interim Contractor Training Support for the Afghan National Army to Maintain and Sustain Mobile Strike Force Vehicles: Audit of Costs Incurred by Textron Inc. Marine and Land Systems

SIGAR 18-07-FA

### WHAT THE AUDIT FOUND

MHM identified one significant deficiency in Textron's internal controls and one instance of noncompliance with the terms and conditions of the contract and applicable regulations. MHM found that Textron misinterpreted the Federal Acquisition Regulation (48 CFR 15.404-4.4iC) and its statutory requirements that fixed fees cannot be higher than 10 percent of the total estimated cost of the contract. Textron overcharged ACC by paying the company's subcontractor a fixed fee of 14.7 percent.

As a result of this internal control deficiency and instance of noncompliance, MHM identified \$301,895 in total questioned costs, entirely consisting of ineligible costs—costs prohibited by the contract, applicable laws, or regulations. However, MHM determined that no reimbursement is due to ACC because Textron deducted the overcharged amount from its billings. MHM did not identify any unsupported costs—costs not supported with adequate documentation or that did not have required prior approval.

Category	Ineligible	Unsupported	Total Questioned Costs
Subcontractor	\$301,895	\$0	\$301,895
<b>Totals</b>	<b>\$301,895</b>	<b>\$0</b>	<b>\$301,895</b>

MHM identified two prior findings with potential material effects on the SPFS. One finding was in the Defense Contract Audit Agency's *Testing of Paid Vouchers for Textron Systems Marine & Land Systems* (audit report no. 01241-2015W11015001), and the other finding was in one of Textron's month-end closing reviews. MHM tested additional transactions and determined that Textron had implemented adequate corrective actions to address these two findings.

MHM issued a qualified opinion on the fairness of Textron's SPFS because Textron did not submit the required management representations indicating that, among other things, it provided all relevant information upon which MHM would base its opinion.

### WHAT SIGAR RECOMMENDS

Based on the results of the audit, SIGAR recommends that the responsible contracting officer at ACC:

- 1. Advise Textron to address the report's one internal control finding.**
- 2. Advise Textron to address the report's one noncompliance finding.**

SIGAR is not making a recommendation related to the questioned costs because Textron deducted the overcharged amount from its billings.



**SIGAR**

Office of the Special Inspector General  
for Afghanistan Reconstruction

October 20, 2017

The Honorable Jim Mattis  
Secretary of Defense

The Honorable Robert M. Speer  
Acting Secretary of the Army

General Joseph L. Votel  
Commander, U.S. Central Command

General John W. Nicholson, Jr.  
Commander, U.S. Forces–Afghanistan and  
Commander, Resolute Support

We contracted with Mayer Hoffman McCann (MHM) to audit the costs incurred by Textron Inc. Marine & Land Systems (Textron) under a U.S. Army Contracting Command (ACC) contract to provide interim contractor training support for the Afghan National Army (ANA) to maintain and sustain its Mobile Strike Force Vehicles (MSFVs).<sup>1</sup> MHM's audit reviewed \$8,011,422 in expenditures that Textron charged to the contract from August 31, 2015, through August 31, 2016. Our contract with MHM required that the audit be performed in accordance with generally accepted government auditing standards issued by the Comptroller General of the United States.

Based on the results of audit, SIGAR recommends that the responsible contracting officer at ACC:

- 1. Advise Textron to address the report's one internal control finding.**
- 2. Advise Textron to address the report's one noncompliance finding.**

Although MHM's audit identified questioned costs, SIGAR is not making a recommendation related to these costs because Textron deducted the overcharged amount from its billings.

The results of MHM's audit are discussed in detail in the attached report. We reviewed MHM's report and related documentation. Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on Textron's Special Purpose Financial Statement. We also express no opinion on the effectiveness of Textron's internal control or compliance with the contract, laws, and regulations. MHM is responsible for the attached auditor's report and the conclusions expressed in it. However, our review disclosed no instances in which MHM did not comply, in all material respects, with generally accepted government auditing standards issued by the Comptroller General of the United States.

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<sup>1</sup> ACC awarded contract number W56HZV-15-C-0108 to Textron. The contract's purpose was to enable the ANA to become self-sufficient in maintaining and sustaining its fleet of MSFVs.



**SIGAR**

Office of the Special Inspector General  
for Afghanistan Reconstruction

We will be following up with your agency to obtain information on the corrective actions taken in response to our recommendations.

John F. Sopko  
Special Inspector General  
for Afghanistan Reconstruction

(F-099)

**TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
Mobile Strike Force Vehicle (MSFV) Interim Contractor Training Support  
For the Afghan National Army (ANA)

For the Period August 31, 2015 through August 31, 2016

# TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
Mobile Strike Force Vehicle (MSFV) Interim Contractor Training Support  
For the Afghan National Army (ANA)

For the Period August 31, 2015 through August 31, 2016

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**Mayer Hoffman McCann P.C.**  
**An Independent CPA Firm**

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October 9, 2017

Enclosed is the final report on the financial audit of costs incurred by Textron, Inc. Marine and Systems ("Textron") under Contract Number W56HZV-15-C-0108 for Mobile Strike Force Vehicle Interim Contractor Training Support for the Afghan National Army. The audit covers the period August 31, 2015 through August 31, 2016.

Included within the final report is a summary of the work performed, our report on the Special Purpose Financial Statement, report on internal control and report on compliance. We do not express an opinion on the summary or any information preceding our reports.

When preparing our report, we considered comments, feedback and interpretations from Textron, the Special Inspector General for Afghanistan Reconstruction and the United States Army Contracting Command. Management of Textron has prepared responses to the findings identified during our audit and those responses are included as part of this report. The responses have not been audited and we express no opinion on them.

Sincerely,

MAYER HOFFMAN McCANN P.C.

A handwritten signature in blue ink, appearing to read "Marcus D. Davis", is written over a horizontal line.

Marcus D. Davis, CPA  
Shareholder

## **TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

For the Period August 31, 2015 through August 31, 2016

### **Background**

On August 31, 2015, the United States Army Contracting Command (“ACC”) awarded Contract Number W56HZV-15-C-0108 (the “Contract”) with Textron Inc. Marine and Land Systems (“Textron”). The purpose of the Contract was to provide interim contractor training support, including training, mentorship, supply support and parts management to the Afghan National Army (“ANA”) in order to enable the Afghans to support their own fleet of Mobile Strike Force Vehicles (“MSFV”). These services were intended to support the U.S. strategic objectives in transitioning the war effort to the Government of the Islamic Republic of Afghanistan. In addition, the overall goal of this program was to enable the Afghans to be self-sufficient in maintaining and sustaining their fleet of MSFV.

The Contract was awarded in the original amount of \$17,434,922, consisting of \$15,906,125 in cost plus fixed fees and \$1,528,797 in firm fixed price components. The Contract had a basic ordering period from August 31, 2015 through August 31, 2016. The Contract was modified three times to update administrative terms and increase the total amount of the Contract to \$23,723,646, consisting of \$22,194,849 in cost plus fixed fees and \$1,528,797 in firm fixed price components. The period of performance was extended to February 28, 2017.

According to background information provided by SIGAR in Appendix I to its Request for Proposal for audit services under Solicitation 16-233-SOL-00642, Textron manufactures and supports armored combat vehicles and marine craft. The Company offers its customers fielding, training, maintenance, and logistics support services throughout each product’s life cycle. Textron is in service with the United States military, international militaries, special operational forces, police forces, and civilian entities worldwide. In addition to its Marine & Land Systems business unit, the Company is comprised of eight other business units: Advanced Information Solutions, Electronic Systems, Geospatial Solutions, Lycoming Engines, Support Solutions, TRU Simulation + Training, Unmanned Systems and Weapon and Sensor Systems.

### **Work Performed**

Mayer Hoffman McCann P.C. (“MHM”) was engaged by the Office of the Special Inspector General for Afghanistan Reconstruction (“SIGAR”) to conduct a financial audit of Textron’s Special Purpose Financial Statement (“SPFS”) for the period August 31, 2015 through August 31, 2016. Total costs reported by Textron and subject to audit during this period were \$8,011,422.

### **Objectives, Scope, and Methodology**

#### **Objectives Defined by SIGAR**

The objectives of the audit include the following:

- *Special Purpose Financial Statement (SPFS)* – Express an opinion on whether Textron’s SPFS



## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

For the Period August 31, 2015 through August 31, 2016

for the Contract presents fairly, in all material respects, revenues received, costs incurred, items directly procured by the U.S. Government, and balance for the period audited in conformity with the terms of the Contract and generally accepted accounting principles or other comprehensive basis of accounting.

- *Internal Controls* – Evaluate and obtain a sufficient understanding of Textron’s internal controls related to the Contract; assess control risk; and identify and report on significant deficiencies including material internal control weaknesses.
- *Compliance* – Perform tests to determine whether Textron complied, in all material respects, with the Contract requirements and applicable laws and regulations; and identify and report on instances of material noncompliance with terms of the award and applicable laws and regulations, including potential fraud or abuse that may have occurred.
- *Corrective Action on Prior Findings and Recommendations* – Determine and report on whether Textron has taken adequate corrective action to address findings and recommendations from previous engagements that could have a material effect on the SPFS or other financial data significant to the audit objectives.

### **Scope**

The scope of this audit included the cost plus fixed fee component of the Contract in the amount of \$22,194,849 and excluded the firm fixed price component of the Contract. This amount is the budgeted ceiling for cost reimbursement, not the actual amount incurred and reimbursed. Our testing of the general and administrative (“G&A”), engineering, manufacturing and materials overhead rates was limited to verifying that the overhead rates were calculated using the rates submitted to the Defense Contract Audit Agency (“DCAA”).

### **Methodology**

In order to accomplish the objectives of this audit, we designed our audit procedures to include the following:

#### **Entrance Conference**

An entrance conference was held via conference call on February 16, 2017. Participants included representatives of MHM, Textron, SIGAR and the ACC.

#### **Planning**

During our planning phase, we performed the following:

## **TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

For the Period August 31, 2015 through August 31, 2016

- Obtained an understanding of Textron;
- Reviewed the Contract and all modifications to date;
- Reviewed sections of the Federal Acquisition Regulation (“FAR”) and the Defense Acquisition Regulation System (“DFARS”) as applicable to the Contract;
- Performed a financial reconciliation; and
- Selected samples based on our approved sampling techniques. According to the approved Audit Plan, we used the detailed accounting records that were reconciled to the financial reports, and based upon the risk assessment and materiality included as part of the approved Audit Plan, we performed data mining to assess individual expenditure accounts and transactions that were considered to be high, medium or low risk for inclusion in our test of transactions. None of the populations were homogeneous in nature, thus statistical sampling was not used. All samples were selected on a judgmental basis. Our sampling methodology for judgmental samples was as follows:
  - For accounts that appear to contain unallowable and restricted items according to the terms of the Contract, Federal Acquisition Regulation (FAR) and any other applicable regulations we will test 100% of the transactions.
  - High risk cost categories – sample transactions that are greater than \$40,900 not to exceed 50% of the total amount expended for each cost category.
  - Medium risk categories – sample transactions that are greater than \$81,800 not to exceed 20% of the total amount expended for each cost category.
  - Low risk categories – sample transactions that are greater than \$81,800 not to exceed 10% of the total amount expended for each cost category, not to exceed 50 transactions in total for all accounts comprising low risk categories.

### Internal Control Related to the SPFS

We reviewed Textron’s internal controls related to the SPFS. The system of internal control is intended to provide reasonable assurance of achieving reliable financial reporting and compliance with applicable laws and regulations. We corroborated internal controls identified by Textron and conducted testing of select key controls to understand if they were implemented as designed and operating effectively.

### Compliance with Agreement Requirements and Applicable Laws and Regulations

We reviewed the Contract and modifications and documented all compliance requirements that could have a direct and material effect on the SPFS. We assessed inherent and control risk as to whether

## **TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

For the Period August 31, 2015 through August 31, 2016

material noncompliance could occur. Based upon our risk assessment, we designed procedures to test a sample of transactions to ensure compliance with the Contract requirements and laws and regulations.

### **Corrective Action on Prior Findings and Recommendations**

We reached out to SIGAR, Textron and the ACC and requested all reports from previous engagements, as well as searched publicly available information for other reports, in order to evaluate the adequacy of corrective actions taken on findings and recommendations that could have a material effect on the SPFS. See the Review of Prior Findings and Recommendations subsection of this Summary for this analysis.

### **Special Purpose Financial Statements**

In reviewing the SPFS, we performed the following:

- Reconciled the costs on the SPFS to the Contract, modifications and general ledger;
- Traced receipt of funds to the accounting records; and
- Sampled and tested the costs incurred to ensure the costs were allowable, allocable to the Contract and reasonable. If the results of a judgmental sample indicated a material error rate, our audit team consulted with our Audit Manager and Project Director as to whether the sample size should be expanded. If it appeared that based upon the results of the judgmental sample, an entire account was deemed not allowable, we did not expand our testing, but instead questioned the entire account.

### **Exit Conference**

An exit conference was held on July 12, 2017 via conference call. Participants included representatives from MHM, Textron, SIGAR and the ACC. During the exit conference, we discussed the preliminary results of the audit and established a timeline for providing any final documentation for consideration and reporting.

### **Summary of Results**

Our audit of the costs incurred by Textron under the Contract with the ACC identified the following audit results. Findings are classified as either internal control, compliance, or a combination of internal control and compliance.

### **Auditors' Opinion on SPFS**

We issued a qualified opinion on the fairness of the presentation of the SPFS. This opinion was a result of Textron not providing required management representations indicating that it has provided us with all relevant information, among other matters, upon which we would base our opinion. In the absence of such representations, the scope of our work was limited to enable us to express an unmodified opinion

## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

For the Period August 31, 2015 through August 31, 2016

on the Special Purpose Financial Statement. See Independent Auditor's Report on the SPFS on page 7. A summary of findings and questioned costs is as follows:

### **Summary of Findings and Questioned Costs**

Finding Number	Nature of Finding	Matter	Questioned Costs	Total Cumulative Questioned Cost
2017-1	Internal control – significant deficiency Non-Compliance	Excess fixed fees paid to subcontractor, including applicable indirect costs	\$301,895	\$301,895

It must be noted that no amount is due to the ACC because Textron deducted the above excess fixed fees from its billings back to the ACC. Textron made these deductions on each billing submitted to the ACC.

### **Internal Control Findings**

Our audit discovered one internal control finding, which is classified as a significant deficiency. See Independent Auditor's Report on Internal Control on page 13. The complete management response from Textron to the internal control finding can be found in Appendix A to this report.

### **Compliance Findings**

As part of obtaining reasonable assurance as to whether the SPFS is free from material misstatement, we tested Textron's compliance with certain provisions of the Contract and other laws and regulations, noncompliance with which could have a direct and material effect on the determination of amounts in the SPFS. The results of our tests disclosed one instance of noncompliance related to this audit. See Independent Auditor's Report on Compliance on page 15. The complete management response from Textron to the compliance finding can be found in Appendix A to this report.

### **Review of Prior Findings and Recommendations**

We requested copies of prior engagements including audits, reviews and evaluations pertinent to Textron's activities under the Contract. We identified two findings from two prior engagements that could have a material effect on the SPFS. We tested transactions and determined that Textron has taken adequate corrective action to address the findings. See the Status of Prior Findings on page 17 for a detailed description of the prior findings and recommendations.

## **TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

For the Period August 31, 2015 through August 31, 2016

### **Summary of Textron's Responses to Findings**

Textron disagreed with Finding 2017-1 indicating that there should be no deduction in the fixed fees as it is in accordance with their subcontract. Additionally, Textron disagrees with the presentation of overhead rates in the report. The complete responses received can be found in Appendix A to this report.



## **INDEPENDENT AUDITOR'S REPORT ON SPECIAL PURPOSE FINANCIAL STATEMENT**

Board of Directors  
Textron Inc. Marine & Land Systems  
1010 Gause Boulevard  
Slidell, Louisiana 70458

Office of the Special Inspector General for Afghanistan Reconstruction  
2530 Crystal Drive  
Arlington, Virginia 22202

### **Report on the Special Purpose Financial Statement**

We have audited the accompanying Special Purpose Financial Statement of Textron Inc. Marine & Land Systems ("Textron") under Contract No. W56HZV-15-C-0108 ("Contract") with the United States Army Contracting Command ("ACC") for Mobile Strike Force Vehicle ("MSFV") Interim Contractor Training Support for the Afghan National Army ("ANA") for the period August 31, 2015 through August 31, 2016, and the related notes to the Special Purpose Financial Statement.

### ***Management's Responsibility for the Special Purpose Financial Statement***

Management is responsible for the preparation and fair presentation of the Special Purpose Financial Statement in accordance with the methods of preparation described in Note 2; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements (including the Special Purpose Financial Statement) that are free from material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on the Special Purpose Financial Statement based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Special Purpose Financial Statement is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Special Purpose Financial Statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the Special Purpose Financial Statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the Special Purpose Financial Statement in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies

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used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the Special Purpose Financial Statement.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Basis for Qualified Opinion***

Management of Textron refused to provide us with certain representations that we requested to represent that it has responsibility for the presentation of the Special Purpose Financial Statement and that it has provided us with all relevant information, among other matters, upon which we would base our opinion.

### ***Opinion***

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the Special Purpose Financial Statement referred to above presents fairly, in all material respects, the respective revenue received and costs incurred by Textron under the Contract for the period August 31, 2015 through August 31, 2016 in accordance with the basis of accounting described in Note 2.

### ***Restriction on Use***

This report is intended for the information of Textron, ACC, and the Special Inspector General for Afghanistan Reconstruction ("SIGAR"), and is not intended to be and should not be used by anyone other than these specified parties. Financial information in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public. However, subject to applicable laws, this report may be released to Congress and to the public by SIGAR in order to provide information about programs and operations funded with amounts appropriated or otherwise made available for the reconstruction of Afghanistan.

### **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our reports dated October 9, 2017 on our consideration of Textron's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Textron's internal control over financial reporting and compliance.



Irvine, California  
October 9, 2017

**TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

## Special Purpose Financial Statement

For the Period August 31, 2015 through August 31, 2016

	Budget	Actual	Questioned Costs			Notes
			Ineligible	Unsupported	Total	
Revenues:						
W56HZV-15-C-0108	<u>\$ 22,194,849</u>	<u>\$ 8,011,422</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	(3)
Total revenues	<u>22,194,849</u>	<u>8,011,422</u>	<u>-</u>	<u>-</u>	<u>-</u>	
Costs incurred:						
FSR labor	15,765,837	6,301,142	301,895	-	301,895	(A)
Other direct costs	1,690,117	301,093	-	-	-	
FSR support and interpreters	2,796,413	1,166,810	-	-	-	
Fixed fee	<u>1,942,482</u>	<u>242,377</u>	<u>-</u>	<u>-</u>	<u>-</u>	
Total costs incurred	<u>22,194,849</u>	<u>8,011,422</u>	<u>301,895</u>	<u>-</u>	<u>301,895</u>	
Outstanding fund balance	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (301,895)</u>	<u>\$ -</u>	<u>\$ (301,895)</u>	(5),(B)

See Notes to Special Purpose Financial Statement  
and Notes to Questioned Costs Presented on Special Purpose Financial Statement



## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

Notes to Special Purpose Financial Statement

For the Period August 31, 2015 through August 31, 2016

### (1) **Background**

On August 31, 2015, the United States Army Contracting Command ("ACC") entered into Contract Number W56-HZV-15-C-0108 (the "Contract") with Textron Inc. Marine and Land Systems ("Textron"). The purpose of the Contract was to provide interim contractor training support, including training, mentorship, supply support and parts management to the Afghan National Army ("ANA") in order to enable the Afghans to support their own fleet of Mobile Strike Force Vehicles ("MFSVs"). These services were intended to support the U.S. strategic objectives in transitioning the war effort to the Government of the Islamic Republic of Afghanistan. In addition, the overall goal of this program was to enable the Afghans to be self-sufficient in maintaining and sustaining

The Contract was awarded in the original amount of \$17,434,922, consisting of \$15,906,125 in cost plus fixed fee and \$1,528,797 in firm fixed price components. The Contract had a basic ordering period from August 31, 2015 through August 31, 2016. The Contract was modified three times to update administrative terms and increase the total amount of the Contract to \$23,723,646, consisting of \$22,194,849 in cost plus fixed fee and \$1,528,797 in firm fixed price components. The period of performance was extended to February 28, 2017.

### (2) **Summary of Significant Accounting Policies**

#### **Basis of Presentation**

The accompanying Special Purpose Financial Statement ("SPFS") includes costs incurred for the MSFV Interim Contractor Training Support for the ANA for the period August 31, 2015 through August 31, 2016. Because the SPFS presents only a selected portion of the operations of Textron, it is not intended to and does not present the financial position, changes in financial position, or cash flows of Textron. The information in the SPFS is presented in accordance with the requirements specified by the Special Inspector General for Afghanistan Reconstruction ("SIGAR"), accounting principles generally accepted in the United States of America, and is specific to the aforementioned Contract.

#### **Basis of Accounting**

Expenditures reported on the SPFS are required to be presented in accordance with accounting principles generally accepted in the United States of America and, therefore, are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in Federal Acquisition Regulation ("FAR") Part 31 – *Contracts with Commercial Organizations*

## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

Notes to Special Purpose Financial Statement

(Continued)

### (2) Summary of Significant Accounting Policies (Continued)

#### Currency

All amounts presented are shown in U.S. dollars, the reporting currency of Textron. Textron did not pay any amounts under the Contract in a foreign currency. Accordingly, no foreign conversion was required.

### (3) Revenue

As of August 31, 2016, Textron has reported \$8,011,422 in revenue. This revenue equals the expenditures invoiced to the ACC for the period August 31, 2015 through August 31, 2016.

### (4) Indirect Cost

Textron's indirect cost rates for the period August 31, 2015 through August 31, 2016 as submitted to the DCAA were as follows.

<u>Indirect Cost</u>	<u>Rates as Submitted to DCAA</u>
████████████████████	████████
████████████████████████████████	████████
████████████████████████	████████
████████	████████

### (5) Outstanding Fund Balance

As of August 31, 2016, there was no outstanding fund balance under the Contract as the SPFS is prepared under the accrual basis of accounting described in Note 2.

### (6) Subsequent Events

Textron has evaluated subsequent events through October 9, 2017, which is the date the SPFS was available to be issued. There were no subsequent events identified that would impact the SPFS as of this date.

## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

Notes to Questioned Costs Presented on Special Purpose Financial Statement

For the Period August 31, 2015 through August 31, 2016

There are two categories of questioned costs, ineligible and unsupported. Ineligible costs are those costs that are explicitly questioned because they are unreasonable; prohibited by the Contract or applicable laws and regulations; or not Contract related. Unsupported costs are not supported with adequate documentation or did not have required prior approvals or authorizations.

### (A) FSR Labor

Textron reported FSR labor in the amount of \$6,301,142 for the period August 31, 2015 through August 31, 2016. During our audit of these costs, we noted the following, which resulted in ineligible costs.

<u>Finding Number</u>	<u>Observation</u>	<u>Ineligible Costs</u>
2017-1	Excess fixed fees paid to subcontractor	<u>\$301,895</u>
Total ineligible costs		<u>\$301,895</u>

It must be noted that no amount is due to the ACC because Textron deducted the above excess fixed fees from its billings back to the ACC. Textron made these deductions on each billing submitted to the ACC.

### (B) Outstanding Fund Balance

The total outstanding fund balance as of August 31, 2016 in the amount of \$(301,895) represents the total questioned costs, consisting of \$301,895 of ineligible costs.



**Mayer Hoffman McCann P.C.**

**An Independent CPA Firm**

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
BASED ON AN AUDIT OF THE SPECIAL PURPOSE FINANCIAL STATEMENT  
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

**INDEPENDENT AUDITOR'S REPORT**

Board of Directors  
Textron Inc. Marine & Land Systems  
1010 Gause Boulevard  
Slidell, Louisiana 70458

Office of the Special Inspector General for Afghanistan Reconstruction  
2530 Crystal Drive  
Arlington, Virginia 22202

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Special Purpose Financial Statement of Textron Inc. Marine & Land Systems ("Textron") representing revenues received and costs incurred under Contract No. W56HZV-15-C-0108 ("Contract") with the United States Army Contracting Command ("ACC") for Mobile Strike Force Vehicle ("MSFV") Interim Contractor Training Support for the Afghan National Army ("ANA") for the period August 31, 2015 through August 31, 2016, and the related Notes to the Special Purpose Financial Statement, and have issued our report thereon dated October 9, 2017.

**Internal Control over Financial Reporting**

In planning and performing our audit of the Special Purpose Financial Statement, we considered Textron's internal control over financial reporting (internal control) to determine the audit procedures that were appropriate in the circumstances for the purpose of expressing our opinion on the Special Purpose Financial Statement, but not for the purpose of expressing an opinion on the effectiveness of Textron's internal control. Accordingly, we do not express an opinion on the effectiveness of Textron's internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a

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combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify one deficiency in internal control, described in the accompanying Detailed Audit Findings as Finding 2017-1, that we consider to be a significant deficiency.

### **Textron's Response to Findings**

Textron's response to the finding identified in our audit is included verbatim in Appendix A. Textron's response was not subjected to the auditing procedures applied in the audit of the Special Purpose Financial Statement and, accordingly, we express no opinion on it.

### **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and the result of that testing, and not to provide an opinion on the effectiveness of Textron's internal control. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

This report is intended for the information of Textron, ACC, and the Special Inspector General for Afghanistan Reconstruction ("SIGAR"), and is not intended to be and should not be used by anyone other than these specified parties. Financial information in this report may be privileged. The restrictions of 18 U.S.C. 1905 should be considered before any information is released to the public. However, subject to applicable laws, this report may be released to Congress and to the public by SIGAR in order to provide information about programs and operations funded with amounts appropriated or otherwise made available for the reconstruction of Afghanistan.



Irvine, California  
October 9, 2017



**Mayer Hoffman McCann P.C.**

**An Independent CPA Firm**

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**REPORT ON COMPLIANCE AND OTHER MATTERS  
BASED ON AN AUDIT OF THE SPECIAL PURPOSE FINANCIAL STATEMENT  
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

**INDEPENDENT AUDITOR'S REPORT**

Board of Directors  
Textron, Inc. Marine & Land Systems  
1010 Gause Boulevard  
Slidell, Louisiana 70458

Office of the Special Inspector General for Afghanistan Reconstruction  
2530 Crystal Drive  
Arlington, Virginia 22202

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Special Purpose Financial Statement of Textron Inc. Marine & Land Systems ("Textron") representing revenues received and costs incurred under Contract No. W56HZV-15-C-0108 ("Contract") with the United States Army Contracting Command ("ACC") for Mobile Strike Force Vehicle ("MSFV") Interim Contractor Training Support for the Afghan National Army ("ANA") for the period August 31, 2015 through August 31, 2016, and the related Notes to the Special Purpose Financial Statement, and have issued our report thereon dated October 9, 2017.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Textron's Special Purpose Financial Statement is free from material misstatement, we tested Textron's compliance with certain provisions of laws, regulations, and the aforementioned Contract, noncompliance with which could have a direct and material effect on the determination of Special Purpose Financial Statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. As we performed our testing, we considered whether the information obtained during our testing indicated the possibility of fraud or abuse. The results of our tests disclosed one instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which is described in the accompanying Detailed Audit Findings as Finding 2017-1.

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## **Textron's Response to Findings**

Textron's response to the finding identified in our audit is included verbatim in Appendix A. Textron's response was not subjected to the auditing procedures applied in the audit of the Special Purpose Financial Statement and, accordingly, we express no opinion on it.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

This report is intended for the information of Textron, ACC, and the Special Inspector General for Afghanistan Reconstruction ("SIGAR"), and is not intended to be and should not be used by anyone other than these specified parties. Financial information in this report may be privileged. The restrictions of 18 U.S.C. 1905 should be considered before any information is released to the public. However, subject to applicable laws, this report may be released to Congress and to the public by SIGAR in order to provide information about programs and operations funded with amounts appropriated or otherwise made available for the reconstruction of Afghanistan.



Irvine, California  
October 9, 2017

## **TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

### **Status of Prior Findings**

For the Period August 31, 2015 through August 31, 2016

We requested copies of prior engagements including audits, reviews and evaluations pertinent to Textron's activities under the Contract. We reviewed the corrective actions taken to address findings and recommendations from prior engagements that could have a material effect on the SPFS. There were two prior engagements included in the scope of our audit. These engagements identified two findings with a potential material effect on the SPFS and/or control deficiencies effect on the Contract. Based on our review, adequate corrective action was implemented on these prior findings.

### **Defense Contract Audit Agency (DCAA) Audit Report No 01241-2015W11015001, Testing of Paid Vouchers for Textron Systems Marine & Land Systems**

There was one finding identified in DCAA's Audit Report No. 01241-2015W11015001. DCAA noted that the Textron combines direct and indirect costs into a single line item when requesting government reimbursement. During our review of reimbursement requests, we noted separate subitems identifying indirect costs and the applicable rate. As such, the corrective action has been adequately implemented.

### **Textron Audit Services Month-End Closing Review**

This internal audit report identified one recommendation for improvement. Textron Audit Services noted that Textron used Excel spreadsheets to adjust account balances prior to entering into its financial management system. During our review of the financial records, we noted that Textron is posting adjustments directly to its financial system and is no longer using Excel spreadsheets to record adjustments. As such, the corrective action has been adequately implemented.



## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

### Detailed Audit Findings

For the Period August 31, 2015 through August 31, 2016

#### **Finding 2017-1: Excess Fixed Fees Paid to Subcontractor**

##### **Nature of Finding:**

Internal control – significant deficiency  
Non-Compliance

##### **Condition:**

During our testing procedures, we identified that Textron used a subcontractor, AAI Corporation d/b/a Textron Systems Support Solutions (TSSS), to provide Field Service Representatives for in-country work. TSSS is a related party of Textron. The total estimated costs of the contract between Textron and TSSS is \$10,359,356. In addition, Textron included a negotiated fixed fees of [REDACTED] which equates to \$994,498 based upon total estimated costs. As of August 31, 2016, the total costs incurred by the subcontractor were \$5,800,132, and the fixed fees charged was \$852,499, or 14.7% of total costs incurred which Textron overcharged the ACC in excess of fixed fees. The estimated costs upon which the fixed fees should have been calculated correctly excluding the fixed fees as follows:

Fixed fees paid to subcontractor	\$ <u>852,499</u>
Allowable fixed fees:	
Total actual costs incurred	5,800,132
Negotiated fixed fees rate	<u>9.6%</u>
Allowable fixed fees	<u>[REDACTED]</u>
Excess fixed fee paid to subcontractor	\$ <u>[REDACTED]</u>

##### **Criteria:**

Contract W56HZV-15-C-0108, Section I-124, 52.244-2 *Subcontracts*, states, in part:

“...(g) No subcontract or modification thereof placed under this contract shall provide for payment on a cost-plus-a-percentage-of-cost basis, and any fee payable under cost-reimbursement type subcontracts shall not exceed the fee limitations in FAR 15.404-4(c)(4)(i)...”

48 CFR 15.404-4, Profit, states, in part:

“(a) *General*. This subsection prescribes policies for establishing the profit or fee portion of the Government prenegotiation objective in price negotiations based on cost analysis.

## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

### Detailed Audit Findings

(Continued)

“(1) Profit or fee prenegotiation objectives do not necessarily represent net income to contractors. Rather, they represent that element of the potential total remuneration that contractors may receive for contract performance over and above allowable costs. This potential remuneration element and the Government’s estimate of allowable costs to be incurred in contract performance together equal the Government’s total prenegotiation objective. Just as actual costs may vary from estimated costs, the contractor’s actual realized profit or fee may vary from negotiated profit or fee, because of such factors as efficiency of performance, incurrence of costs the Government does not recognize as allowable, and the contract type...”

(c) *Contracting officer responsibilities...*

(4)(i) The contracting officer shall not negotiate a price or fee that exceeds the following statutory limitations, imposed by 10 U.S.C. 2306(d) and 41 U.S.C. 3905):...

(C) For other cost-plus-fixed-fee contracts, the fee shall not exceed 10 percent of the contract’s estimated cost, excluding fee.”

According to the FAR as cited above, the fixed fee cannot be negotiated higher than 10% of the total estimated costs, which Textron negotiated rate was 9.6%. However, the FAR also clarifies that profit represents potential remuneration and that the actual rate may differ from the negotiated rate, just as actual costs may differ from estimated costs. In the case of Textron, actual costs were less than total estimated costs at August 31, 2016, thus the actual fixed fees will be less than the estimated fixed fees.

#### **Cause:**

Textron misinterpreted and applied the FAR statutory requirements incorrectly by indicating that the fixed fees were negotiated based upon the total estimated costs and that the fixed fees are not adjusted if actual costs are less than estimated costs.

#### **Effect:**

By not applying the negotiated fixed fees percentage to the actual costs incurred, Textron paid its subcontractor a fixed fees in excess of allowable amounts.

#### **Questioned Costs:**

Total ineligible excess fixed fees related to FSR labor costs, including the associated materials fees, are as follows:

## TEXTRON INC. MARINE & LAND SYSTEMS

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

### Detailed Audit Findings

(Continued)

	<u>Ineligible Costs</u>
FSR labor	██████████
Materials overhead (██████████)	— ██████████
Total ineligible costs	<u>\$301,895</u>

It must be noted that no amount is due to the ACC because Textron deducted the above excess fixed fees from its billings back to the ACC. Textron made these deductions on each billing submitted to the ACC.

### **Recommendation:**

We recommend that Textron establish policies and procedures that specifically address the calculation of the fixed fees to ensure that subcontractors comply with contract requirements and Federal regulations.

# TEXTRON Systems

## **TEXTRON'S RESPONSE TO THE FINANCIAL AUDIT** **OF COSTS INCURRED UNDER CONTRACT NO. W56HZV-15-C-0108** **BY THE SPECIAL INSPECTOR GENERAL FOR AFGHANISTAN RECONSTRUCTION**

### **I. Background**

Textron Inc. d/b/a Textron Systems Marine & Land Systems ("Textron") was awarded the Mobile Strike Force Vehicle Interim Contractor Training Support for the Afghan National Army ("ANA") contract, Contract Number W56HZV-15-C-0108, on 31 August 2015 (the "Contract"). Pursuant to the Contract, Textron provided contractor training support, including training, mentorship, supply support, and parts management to the ANA. The Contract was predominantly a Cost-Plus-Fixed-Fee ("CPFF") type contract and ultimately had a total dollar value of \$33,772,457 (including all modifications).

The scope of the audit performed by Mayer Hoffman McCann P.C. (the "Auditor"), on behalf of the Special Inspector General for Afghanistan Reconstruction ("SIGAR"), was limited to the first year of the Contract (31 August 2015 through 31 August 2016), which had a total dollar value of \$17,434,922. Prior to contract award, the United States Army Contracting Command ("ACC") and Textron negotiated a 9.6% fee rate. This rate was then applied to the negotiated cost estimate of \$15,863,464 yielding a total fixed fee, as set forth in the Contract, of \$1,571,458.

Textron subcontracted the performance of the in-country Field Service Representative ("FSR") work to an affiliated company, AAI Corporation d/b/a Textron Systems Support Solutions ("TSSS"). The subcontract was also structured as a CPFF contract and had a cost estimate of \$10,359,356 and associated fixed fee of \$994,602, totaling a dollar value of \$11,353,958 in the first year. However, TSSS incurred less cost than estimated so they only received cost reimbursement of \$5,800,132 plus a fixed fee of \$852,499, which was commensurate with their scope of work. This amount was lower than the negotiated amount, \$994,602, because the Contract contained certain Level-of-Effort ("LOE") tasks in the base work which, if performed, resulted in the contractor being entitled to the fixed fee associated with the specific LOE. Since the total costs incurred were lower than the estimate, TSSS's realized fee rate was 14.7%.

The audit report (the "Audit Report") prepared by the Auditor identifies one finding based on their financial audit of the costs incurred under the Contract. The finding, that "excess fixed fee [was] paid to [the] subcontractor," is identified as a "significant deficiency" in Textron's internal controls. The amount of the finding is [REDACTED] plus the applicable material overhead rate resulting in a total finding of "ineligible costs" of \$301,895. The Audit Report states that "Textron interpreted the [Federal Acquisition Regulation] incorrectly by indicating that the fixed fee was negotiated based upon the total estimated costs and that the fixed fee is not adjusted if actual costs are less than estimated costs." The Audit Report draws this conclusion based on the Auditor's interpretation of several Federal Acquisition Regulation ("FAR") sections. The Auditor states that "the FAR also clarifies that profit represents potential remuneration and that the actual rate may differ from the negotiated rate, just as actual costs may differ from estimated costs" which led the Auditor to the conclusion that Textron overcharged the Government because "actual costs were less than estimated at August 31, 2016, thus the actual fixed fee [should] be less than the estimated fixed fee." The Audit Report then subtracts the result of the fee rate of 9.6% applied to the actual costs incurred of \$5,800,132, which is [REDACTED], from TSSS's fixed fee of \$852,499, yielding the Auditor's finding of [REDACTED] (before application of the material overhead rate). Based on this finding, the Audit Report recommends that Textron reimburse ACC for \$301,895 and "establish policies and procedures that specifically address the calculation of the fixed fee...."

### **II. Cost-Plus-Fixed-Fee Contracts**

Before the Government awards a non-competitive CPFF contract, it negotiates a cost estimate based on the scope of work with the contractor. This cost estimate becomes the dollar value of the contract (not including fee) but the contractor is only entitled to reimbursement of its allowable costs in accordance with the Allowable Cost and Payment clause, which may be more or less than the cost estimate. See FAR 52.216-7. In addition to cost

reimbursement, the contractor is entitled to a fixed fee based on the cost estimate. This contract structure results in the Government bearing the cost risk associated with deviations from the estimated cost of performance and the contractor bearing the risk of profitability. With respect to the fixed fee, FAR 16.306(a) states that:

A cost-plus-fixed-fee contract is a cost-reimbursement contract that provides for payment to the contractor of a negotiated fee that is fixed at the inception of the contract. The fixed fee does not vary with actual cost, but may be adjusted as a result of changes in the work to be performed under the contract.

In practice, the Government and contractor will negotiate the fixed fee based on a fee rate that reflects the risk associated with the work, which must not exceed the statutory cap on fee (10% except for certain exceptions). 10 U.S.C. §2306(d) (2011), 41 U.S.C. §3905 (2010), and FAR 15.404-4(c)(4)(i). So, for example, if the parties agree to a cost estimate of \$200 and a fee rate of 9%, the fixed fee specified in the contract will be \$18. This fixed fee dollar amount becomes part of the contract, not the fee rate, which may vary depending on the actual costs incurred. See, for example, *CACI, Inc.-Federal*, 64 Comp. Gen. 439 (1985), where the Comptroller held that when estimated costs ultimately turn out to be lower than proposed, the actual fee earned can exceed ten percent of the actual costs incurred.

In the Audit Report, the Auditor takes the position that Textron incorrectly applied the CPFF concepts to its subcontractor, TSSS. However, Textron negotiated the fixed fee in accordance with the FAR and, although TSSS incurred less actual costs than estimated, TSSS was still entitled to the full fixed fee (less the amount of fixed fee associated with the unperformed LOE work).

### III. Cost-Plus-Percentage-of-Cost Contracts

Textron disagrees with the Audit Report's calculation of the finding and its recommended corrective action. The Auditor, by applying a downward adjustment to the fixed fee, calculated the finding using a Cost-Plus-Percentage-of-Cost ("CPPC") method. In other words, applying the fee rate of 9.6% to the actual incurred costs results in a fee that varies based on actual costs. CPPC contracting in Government contracting is expressly prohibited by statute. See 10 U.S.C. §2306(a) and 41 U.S.C. §3905(a). The Comptroller General originally established the criteria for determining what constituted a CPPC contract. See *Mktg. Consultants Int'l Ltd.*, 55 Comp.Gen. 554 (1975). Several years later, the Federal Circuit adopted the same test:

We accept, at the outset, the general criteria (adopted by the Board) which were developed by the Comptroller General for determining whether a contract is a cost-plus-a-percentage-of-cost contract: (1) payment is on a predetermined percentage rate; (2) the predetermined percentage rate is applied to actual performance costs; (3) the contractor's entitlement is uncertain at the time of contracting and (4) the contractor's entitlement increases commensurately with increased performance costs.

*Urban Data Systems, Inc. v. U.S.*, 699 F.2d 1147, 1150 (Fed. Cir. 1983).

The Auditor has recommended a finding and corrective action which meet this test. The Auditor states that we should apply a predetermined percentage rate to our actual performance costs which were uncertain at the time of contracting. In the current situation, this results in a downward adjustment since TSSS incurred less costs than estimated but, applying the same logic in the opposite situation, would have resulted in TSSS being entitled to more fee if actual costs would have exceeded the estimated costs.

CPPC contracting is also prohibited by regulation. See FAR 16.102(c) and FAR 44.203(b)(2). Adjusting TSSS's fee based on the Auditor's recommendation that "the subcontract should be paid cost plus a percentage", would have violated our statutory, regulatory, and contractual obligations, and could even call into question our approved Purchasing System. As a result, the Auditor's finding and the recommended corrective action are in direct contradiction with Textron's legal and contractual requirements.

**IV. Material Cost Principle**

When contracting between affiliated companies, such as between Textron and TSSS, under a U.S. Government prime contract, the contractor is not entitled to charge fee on fee unless certain exceptions are met. FAR 31.205-26. To comply with the material cost principle, TSSS sold its services to Textron on a cost incurred basis. See FAR 31.205-26(e). However, this cost principle does not prohibit affiliated contractors from internally allocating and apportioning fee provided that the fee is not pyramided. In other words, contractors are free to internally allocate the fixed fee but, for example, Textron could not include TSSS's fee in its cost base upon which additional fee is calculated and charged to the Government. Defense Contract Audit Agency, *Contract Audit Manual*, §§ 9-404.4, 9-404.5 (Jun. 29, 2016). For purposes of performing the Contract, Textron and TSSS agreed to internally allocate and apportion the fixed fee among the two entities based on the work being performed by each. Textron manages these allocations in accordance with its approved Accounting system.

Moreover, Textron believes that the Special Purpose Financial Statement ("SPFS") prepared by the Auditor does not accurately represent the adjustment made to costs in accordance with this cost principle nor the actual fee that was invoiced on the Contract. Textron removed TSSS's fee from its invoices to ensure its compliance with the cost principle and that fee was not inadvertently pyramided. These measures ensured the Government was not overbilled. In fact, the Auditor reviewed Textron's invoices related to this Contract and agreed that the Government was not overbilled.

**V. Overhead Rates**

The Audit Report also identifies several overhead rates as "rates as submitted to DCAA" (see, *e.g.*, page 10 of the Audit Report). Textron believes these rates are incorrect and is not sure how they were calculated. The time period audited spans two separate fiscal periods so, in any event, these rates would not be representative of Textron's actual overhead rates during this time period.

**VI. Conclusion**

For the reasons discussed herein, Textron respectfully disagrees with the Audit Report's finding and recommended corrective action. In summary, the Contract was (i) a CPFF contract which entitled TSSS to the fixed fee; (ii) that fixed fee was not adjustable based on the fee rate negotiated pre-contract award (which, if implemented, would convert the CPFF structure to an illegal CPPC contract); and, (iii) Textron complied with the material cost principle applicable to intracompany work/subcontracts thus preventing any overbilling to the Government.

**TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

Auditor's Rebuttal to Textron's Response to Findings

For the Period August 31, 2015 through August 31, 2016

Textron disagreed with Finding 2017-1. We have reviewed management's response and provide the following rebuttal.

**Finding 2017-1: Excess Fixed Fees Paid to Subcontractor**

Textron disagreed with this finding for the following reasons:

- (1) The type of contract entitled the subcontractor to the fixed fee. Textron stated that its contract with the subcontractors is a cost-plus-fixed fee contract meaning that the fee to the subcontractor is fixed. Textron indicated that the fee is negotiated with the Government to reflect the risk associated with the work to be performed and would not vary with actual costs.
- (2) The fixed fee is not adjustable based on the fee rate negotiated pre-contract. Otherwise Textron may be in violation of various statutory, regulatory, and contractual obligations and could even be a violation of their approved purchasing system. Textron stated that the recommendation to the finding would mean that the contract should be a cost-plus-percentage of cost contract, which would make their actions in direct contradiction with Textron's legal and contractual requirements.
- (3) Textron complied with the material cost principle applicable to intracompany work/subcontracts which prevented any overbilling to the government. Textron states that it is entitled to their fixed fee and are free to internally allocate the fee. Textron asserts that it did not include the subcontractor's fee in the base that was used to calculate the amounts charged to the Government. Textron's billings to the Government reflect that the subcontractor fee was removed and that the Government was not inadvertently overbilled.

We reviewed the disagreements above and agree that the Government was not billed for the subcontractor's fixed fees. However, the subcontractor's fee is presented in the SPFS as a cost incurred. The purpose of this audit is to opine that the costs incurred are allowable based on contractual and regulatory requirements. The inclusion of the subcontractor fees in the costs incurred is incorrect. Moreover, 48 CFR 15.404-4, *Profit*, which is referenced in the Contract, stipulates that fixed fees can be adjusted based on efficiency of operations. As such, our finding and recommendation remains unchanged.

**Presentation of Overhead Rates**

Textron disagreed with the presentation of the overhead rates in the report. It indicated that the rates are incorrect and do not represent Textron's actual overhead rates during the audit period. The rates

**TEXTRON INC. MARINE & LAND SYSTEMS**

Contract No. W56HZV-15-C-0108  
MSFV Interim Contractor Training Support  
For the ANA

Auditor's Rebuttal to Textron's Response to Findings

For the Period August 31, 2015 through August 31, 2016

presented in the audit were provided by Textron to us and were indicated that these were the rates as submitted to DCAA.



## SIGAR's Mission

The mission of the Special Inspector General for Afghanistan Reconstruction (SIGAR) is to enhance oversight of programs for the reconstruction of Afghanistan by conducting independent and objective audits, inspections, and investigations on the use of taxpayer dollars and related funds. SIGAR works to provide accurate and balanced information, evaluations, analysis, and recommendations to help the U.S. Congress, U.S. agencies, and other decision-makers to make informed oversight, policy, and funding decisions to:

- improve effectiveness of the overall reconstruction strategy and its component programs;
- improve management and accountability over funds administered by U.S. and Afghan agencies and their contractors;
- improve contracting and contract management processes;
- prevent fraud, waste, and abuse; and
- advance U.S. interests in reconstructing Afghanistan.

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- Phone DSN Afghanistan: 318-237-3912 ext. 7303
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## Public Affairs

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