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# THE GOVERNMENT CONTRACTOR<sup>®</sup>

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## ¶ 256 FEATURE COMMENT: Parallel Enforcement Proceedings: Focus On Government Cost Accounting

*David Robbins, Matt Haws and Jennifer Lee\**

Much attention has been paid recently to increased parallel civil and criminal enforcement proceeding risks facing Government contractors. In addition to across-the-board risks, experienced practitioners are noticing that multiple Government agencies are paying increased attention to Government contracts cost accounting issues in particular.

Two recent enforcement resolutions exemplify the increased Government cost and financial accounting risks. In the first, a typical contract audit issue was weaponized into one of the largest procurement fraud settlements through the False Claims Act. In the second, revenue accounting related in part to an Army subcontract became the foundation for the Securities and Exchange Commission to institute cease and desist proceedings.

**The Settlements**—The first is the July 2023 FCA settlement where Booz Allen Hamilton agreed to pay \$377.45 million to resolve alleged Government contracts cost accounting misconduct. Available at [www.justice.gov/opa/pr/booz-allen-agrees-pay-37745-million-settle-false-claims-act-allegations](http://www.justice.gov/opa/pr/booz-allen-agrees-pay-37745-million-settle-false-claims-act-allegations).

The second is the September 2023 SEC charges filed against Fluor Corp., and the company's agreement to pay \$14.5 million to settle allegations relating in part to a fixed-price Government subcontract. Available at [www.sec.gov/news/press-release/2023-170](http://www.sec.gov/news/press-release/2023-170).

**Indirect Cost Accounting**—As summarized by the Department of Justice press release,

The settlement ... resolves allegations that from approximately 2011 to 2021, Booz Allen improperly charged costs to its government contracts and subcontracts that instead should have been billed to its commercial and international contracts. In particular, the government alleged that Booz Allen improperly allocated indirect costs associated with its commercial and international business to its government contracts and subcontracts that either had no relationship to those contracts and subcontracts or were allocated to those contracts and subcontracts in disproportionate amounts.

Available at [www.justice.gov/opa/pr/booz-allen-agrees-pay-37745-million-settle-false-claims-act-allegations](http://www.justice.gov/opa/pr/booz-allen-agrees-pay-37745-million-settle-false-claims-act-allegations).

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\*This Feature Comment was written for *THE GOVERNMENT CONTRACTOR* by David Robbins, Matt Haws and Jennifer Lee. Mr. Robbins co-chairs the Jenner & Block Government Contracts Practice and is a former Procurement Fraud Remedies Director for the U.S. Air Force. Mr. Haws is a partner in Jenner & Block's Washington, D.C. office. And Ms. Lee is a partner in Jenner & Block's San Francisco office and is a former Assistant Director in the SEC's Division of Enforcement.

According to the Government, Booz Allen’s indirect cost pools improperly commingled costs supporting commercial and/or international contracts with those supporting Government contracts and subcontracts in a way that disproportionately allocated the costs to its Government contracts and violated the homogeneity and proportionality requirements in Cost Accounting Standard 418. The Government alleged that Booz Allen also included unallowable costs; failed to disclose current, accurate, and complete cost or pricing data; and submitted inaccurate and/or misleading statements regarding its indirect costs, including in its CAS Disclosure Statements. Id.

**Revenue Recognition**—The SEC charged Fluor Corp. and five “former and current Fluor officers and employees” related to “the company’s improper accounting on two large-scale, fixed-price construction projects.” One of the projects was a Government subcontract. Available at [www.sec.gov/news/press-release/2023-170](http://www.sec.gov/news/press-release/2023-170). According to the SEC, Fluor experienced cost overruns on the projects and “failed to sufficiently maintain internal controls to account for the projects in accordance with the percentage of completion accounting method under U.S. generally accepted accounting principles (GAAP).” Specifically, the SEC alleged Fluor ran afoul of generally accepted accounting principles by not including anticipated costs in each of the troubled projects’ forecasts, which in turn delayed loss recognition. The company also “improperly incorporated revenue from unapproved change orders in the forecasts of one of the projects, including change orders that had not yet been submitted to, or had already been rejected by, the customer.” Id.

The SEC alleged that the accounting errors on one project caused Fluor to materially overstate its net earnings by as much as 37 percent from the company’s fiscal year 2016 through the first quarter of its fiscal year 2019. In addition, the delayed loss recognition on the second project caused Fluor to overstate its net earnings by 22 percent in the second quarter of 2018. As a result, Fluor materially misstated the financial statements included in its periodic filings with the Commission for the corresponding reporting periods. Id.

According to the SEC order, the projects in question included a fixed-price subcontract supporting an Army project, and a fixed-price project with a large, international energy company. Available at [www.sec.gov/files/litigation/admin/2023/34-98292.pdf](http://www.sec.gov/files/litigation/admin/2023/34-98292.pdf).

**Analysis**—The Booz Allen and Fluor resolutions are reminders of the importance of accurate Government contracts cost accounting and financial accounting. Cost accounting compliance allows the Government, among other things, to ensure prices are fair and reasonable at contract formation, and that the Government is only reimbursing approved categories of costs. Contractors are well aware of the usual audit and contract closeout processes, but may be less aware that alleged cost improprieties can—and do—lead to enforcement actions. And for public companies, financial accounting and generally accepted accounting standards compliance gives the investing public accurate information upon which to make investment decisions.

Recent trends suggest that the Government is examining Government contracts cost issues more closely, and not just through the contract administration lens. This suggests either increased coordination among the Defense Contract Audit Agency, the Defense Contract Management Agency, and enforcement officials, or among program offices and enforcement officials.

It also suggests a renewed willingness of enforcement agencies such as DOJ and the SEC to dive deeply into these complex areas and analyze their unique Government contracts aspects.

Now more than ever, Government contractors are well advised to review their cost accounting processes and procedures for compliance and ensure coordination between Government contract and financial accounting processes.

Under normal circumstances, Government contracts cost accounting is a complicated area that requires expert attention. In an era in which traditional contractual oversight is being weaponized into civil and criminal enforcement actions, cost accounting issues can lead to significant enforcement consequences.