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| **Subcontractor Proposal Cost Analysis** | |

# Purpose and Scope

THE COMPANY has an obligation to prove that THE COMPANY is contracting at rates and prices that are fair and reasonable and are compliant with Canadian Law. There are two parts to determining fair and reasonable **for single or sole source procurements**: price analysis and cost analysis.

* A price analysis determines whether the proposed pricing is fair and reasonable in comparison to other proposals and/or other available data points. For details see *Subcontractor Price Analysis*. A price analysis should always precede a cost analysis.
* A cost analysis analyses the elements of an individual proposal to determine if it is fair and reasonable.

A financial review is the cost analysis tool THE COMPANY uses to assess and document compliant fair and reasonable pricing for single or sole source procurements over $1 million dollars (new subcontracts/agreements and subcontract changes over $1 million dollars). The purpose of this work instruction is to guide you and your team through the financial review process.

There are two types of financial review:

* **Desktop Financial Review**: new procurement ≤ $2,000,000 and changes over $1,000,000: *Desktop Financial Review*, which involves a research-based analysis of the proposal elements (rates, hours, and material costs).
* **Full Financial Review**: new procurement > $2,000,000: *Full Financial Review*, which includes a detailed review of the proposal elements (rates, hours, and material costs) and an evaluation of the factors that comprise each element. This includes a review with the Supplier and an optional on-site visit.

Guidelines for when a financial review is required is governed by the procedure *Supplier Contracting*.

Please note, this process may also be used to conduct a supplier discretionary review post-subcontract award.

# Definitions

**Direct Cost:** The cost of materials which can be specifically identified and measured as having been used or to be used in the performance of the subcontract and which are so identified and measured consistently by THE COMPANY's cost accounting practices.

**Process Gate**: A key point of management engagement as the financial review progresses.

**Indirect Cost:** Or “overhead costs" meaning those costs which, though necessarily having been incurred during the performance of the subcontract for the conduct of the Subcontractor's business in general, cannot be identified and measured as directly applicable to the performance of the Subcontract.

**Non-Applicable Costs:** As detailed in section 1031-2 of the SACC manual, Non-Applicable Costs are costs may have been or may be reasonably and properly incurred by the subcontractor in the performance of the subcontract, they are considered non-applicable costs to the subcontract.

**Reasonable Cost:** A cost is reasonable if the nature and amount do not exceed what would be incurred by an ordinary prudent person in the conduct of a competitive business (source: [https://buyandsell.gc.ca](https://buyandsell.gc.ca/), 1031-2 SACC Clause).

# Desktop Financial Review

A desktop financial review applies to single or sole source procurements over $1 million and less than or equal to

$2 million dollars CAD and changes over $1 million dollars. Complete the follow steps:

1. Define the need and update the *Financial Review Tracker* to include a record of the new need, including the need date.
2. Conduct an initial review of the Supplier Proposal:
   * Break down the proposal by rates, hours, and material costs (as indicated in *Subcontractor Desktop Financial Review Template*).
   * Define initial allowable profit determination (see *Subcontractor Desktop Financial Review Template*, Section III B).
   * Create first draft of the *Subcontractor Desktop Financial Review* based on received proposal.
3. Define the list of questions for supplier and submit to the supplier. See [Appendix A](#_bookmark2) [Sample Questions for](#_bookmark2) [Supplier.](#_bookmark2)
4. Complete the *Subcontractor Desktop Financial Review* report for rates, hours and material costs. Analyse conclusions from the review to draw negotiation objectives and strategy (see *Negotiation Strategy and Objectives*). Each element of the proposal (hours, rates, material costs) should be determined to be one of the following, with rationale:
   * Fair and reasonable
   * Understated
   * Overstated
5. Archive the final report, negotiation objectives and related documentation in accordance with department standard practices.

# Full Financial Review

A full financial review applies to single or sole source procurements over $2 million.

* 1. **Overview**

The following table describes the steps, deliverables, and links to key references in the full financial review process. Additional descriptions of each process step can be found in Section [4.2.](#_bookmark0)

**Table 4-1 Financial Review Process Summary**

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|  | **Milestone** | **Outcome** | **Duration** | **References** |
| **1** | Define Need | * Update Financial Review Tracker to include record of new need including need date | --- | *Financial Review Tracker* |
| **2** | Build your Financial Review Team | * List of team members and assigned roles in the financial review * Review of team member expectations * Kick off with team | 1 day |  |
| **3** | Initial Review of Supplier Proposal | * Determine how to break down proposal (see *Subcontractor Full Financial Review Template* Section IV A) * Define initial allowable profit determination * Create first draft of *Subcontractor Full or Desktop Financial Review* based on received proposal | 1 week | Template: *Subcontractor Full Financial Review Template* |
| **4** | Define list of questions and Requests for Information for supplier | * Revise list of questions * Revise Requests for Information with supplier (if required) | 1 day | Example: [Appendix A](#_bookmark2) [Sample Questions for](#_bookmark2) [Supplier](#_bookmark2) |
| **5** | Non-Disclosure Agreement | * Determine if additional NDA clause is required with supplier to restrict viewers of supplier financial information. | ---- | Template: *Mutual Non- Disclosure Agreement for NSS Programs (Annex 1)* |
| **6** | Kickoff with supplier | * Prepare kickoff deck for supplier * Teams meeting with supplier (1 hour) * Review list of questions and expectations for supplier | 1 hour meeting | Example: *Supplier Financial Review Presentation*  Example: [Appendix A](#_bookmark2) [Sample Questions for](#_bookmark2) [Supplier](#_bookmark2)  Example: [Appendix B](#_bookmark3) [Sample Agendas](#_bookmark3) |
| **7** | Supplier responds | * Supplier responds to questions, RFI (if applicable) | 2 weeks |  |
| **8** | Review Additional Documentation and Prepare for On-Site Review | * Review additional information provided by supplier * Update draft financial review * Revise Agenda for Financial Review | 1 week | Example: [Appendix B](#_bookmark3) [Sample Agendas](#_bookmark3) |
| **9** | Conduct Financial Review & complete report | * On site assessment at supplier * Closure of all open gaps | 1-2  weeks | Example: *Supplier Financial Review Presentation* |

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|  | **Milestone** | **Outcome** | **Duration** | **References** |
|  |  | * Complete *Subcontractor Full Financial Review* |  |  |
| **10** | Analyze conclusions from review to draw negotiation objectives and strategy | * Each element of the proposal (hours, profit, cost) determined, with rationale, to be *fair and reasonable*, *understated*, or *overstated* * Completed negotiations objectives | 1 week | Work Instruction: *Negotiation Strategy and Objectives* |
| **11** | Archive documentation in accordance with department standard practices | * Final Full Financial Review Report * Negotiation Strategy and Objectives | 1 day |  |

* 1. **Full Financial Review Process**

You must complete the required training prior to leading or participating in a financial review. To learn more about becoming certified to lead or participate in a financial review, see *Financial Review Training and Certification*.

### Conduct an Initial Review of Supplier Proposal

This step is conducted collaboratively between the Financial Lead, Subcontract Authority, and Functional Expert. The goal of this step is to have a full understanding of the supplier’s proposal and basis of estimate with the information provided thus far from the supplier. The on-site review should be used to confirm your understanding of the supplier’s proposal as well as close any gaps required to complete the full financial review. To complete this step, the team should write the *Subcontractor Full Financial Review* in a draft form and at a minimum complete the following:

* + - * Document the team’s understanding of the supplier’s basis of estimate
      * List initial analytics to identify opportunities (for sample analytics see the *Subcontractor Full Financial Review Template*)
      * Determine sampling for financial review on-site

### Define Initial Questions for Supplier

Your goal for this step is to help prepare the supplier for the financial review by making sure they are aware of information you will ask for during the review, so they can come prepared to provide adequate answers. The areas that have been known to cause most churn during the financial review are:

* + - * Basis of estimate for chosen samples from their proposal
      * Rates breakdown

Use the *Subcontractor Full Financial Review Template* as a guide to complete this step.

### Non-Disclosure Information

THE COMPANY has an obligation to protect sensitive supplier information. The general NDA that THE COMPANY signs with suppliers is a dual-executed NDA which allows supplier information to be shared within THE COMPANY. There is the option, if a supplier feels as though the general NDA does not provide enough protection for the type of sensitive information shared in the review, to include a more restrictive clause (see *Mutual Non-Disclosure Agreement for NSS Programs (Annex 1)*). In this clause, THE COMPANY will name individual

people that may see or receive the supplier confidential information shared in the financial review. This clause outlines the process that the supplier must label the specific data or information as confidential or sensitive and, in turn, THE COMPANY must protect that data by storing it in locked folders on a shared drive.

Please note, not all information shared in the financial review will be sensitive or confidential.

### Gate 1: Management Engagement

The Subcontract Manager should review with the team to make sure the team is fully prepared for the kick-off meeting and there is appropriate participation from both THE COMPANY and the supplier.

### Kick-Off with Supplier

It is important to set a positive tone with the supplier during the kick-off. The kick-off meeting is usually run by the THE COMPANY Subcontract Authority with support from the SCM Supply Chain Director and other THE COMPANY participants on the review.

The *Supplier Financial Review Presentation* provides key messages to cover with the supplier. Please tailor this deck for your specific review. Make sure to set clear deadlines for the supplier and the financial review.

Suggested attendees include:

* + - * Senior Leadership/ THE COMPANY Account Manager at supplier
      * Review participants at supplier
      * THE COMPANY Supply Chain Director
      * THE COMPANY Subcontract Authority
      * THE COMPANY review participants

### Review Supplier Initial Response

The supplier may provide information prior to the on-site review. Any information provided should be reviewed thoroughly by the team to help make sure the time on-site with the supplier is as effective and efficient as possible.

### Prepare for On-Site Review

With information provided thus far from the supplier, the team should draft the Full Financial Review report using the *Subcontractor Full Financial Review Template.* Any data analysis or review of additional information that can be done prior to the on-site review should also be completed and documented in the draft report. Gaps in each section of the report should be clearly documented to facilitate an effective on-site financial review.

If an on-site review is not feasible this part of the review may be carried out remotely.

Prior to the on-site review make sure:

1. Meetings with supplier personnel required to close gaps have been scheduled and confirmed.
2. The THE COMPANY review team has scheduled time in between supplier meetings to complete analyses and document findings in the final report.
3. Reserve the afternoon of Day 4 to complete the final report so any final gaps can be closed Day 5 of the review prior to leaving the supplier’s site.

### Gate 2: Management Engagement

The Subcontract Manager should review with the team to verify team is fully prepared before traveling to the supplier.

### Complete On-Site Financial Review and Final Report

Your goal is to have a completed final report at the end of the on-site financial review. The *Subcontractor Full Financial Review Template* has been created to follow the agenda of the on-site financial review. The facilitator of the on-site review (usually the Subcontract Authority) should follow the report template to ask questions during the financial review to close any noted gaps.

At the end of the on-site financial review (prior to leaving the supplier’s facility) the team should have accomplished the following:

* + - * Completed Full Financial Review report
      * Documented the basis of estimate in the report with examples (make sure the math works!)
      * Documented and understood breakdown of rates, hours, material costs, and staffing
      * Archived final report and any additional supporting documentation
      * Assessed each element of the proposal (hours, rates and material cost) and determine if pricing is fair and reasonable, overstated, or understated (see step [4.2.10](#_bookmark1))
      * Able to clearly articulate the supplier’s basis of estimate

### Analyse Conclusions and Assess Proposal

The final Subcontractor Full Financial Review report documents facts and methodology of the supplier’s basis of estimate. The negotiation strategy then draws conclusions from the facts collected during the financial review to determine THE COMPANY’s position on the supplier’s proposal (fair and reasonable, overstated, and understated). The team should complete this assessment with clearly documented rationale for each element (hours, rates, material costs) and sub-element (e.g. for rates-profit, overhead, direct) of the proposal. It is recommended this is completed on-site prior to leaving the supplier’s facility (if possible) as this will help identify any remaining gaps. The team may need to complete comparative analyses after the financial review to fully complete this assessment.

### Gate 3: Management Engagement

The completed Subcontractor Full Financial Review report and negotiation strategy is to be reviewed and approved by the Subcontract Manager (and/or Director).

### Archive Financial Review Documentation

Store the Subcontractor Full Financial Review report, negotiation strategy, signed NDA (if applicable) and any supporting documentation in a secure and locked folder in accordance with your department’s standard practices. It is the responsibility of the Subcontract Authority to ensure proper access controls exist on the shared folder to prevent access of supplier sensitive information to those that are not permitted to receive it.

1. **Referenced Documents**

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| **Document Number** | **Document Title** |
| SQMS-THE COMPANY-SCM-P041 | Supplier Contracting |
| SQMS-THE COMPANY-SCM-W015 | Negotiation Strategy and Objectives |
| SQMS-THE COMPANY-LD-F001 | Mutual Non-Disclosure Agreement for Programs (Annex 1) |
| SQMS-THE COMPANY-SCM-F051 | Subcontractor Desktop Financial Review Template |
| SQMS-THE COMPANY-SCM-F052 | Subcontractor Full Financial Review Template |

**Appendix A Sample Questions for Supplier**

This list is an example only.

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| **#** | **Cost Element** | **Question** | **Key POC for follow up (Supplier and THE COMPANY)** | **Supplier Response** |
| 1 | Labour Cost (Hours and Rates) | Direct Labour is the labour required to perform the work  Labour cost is usually broken down in two components, hours and rates. In a proposal each element needs to be evaluated.  Obtain a breakdown, from the supplier, of the proposed labour costs by hours, rates and level of efforts. (Likely will need breakdown to include the rate classification and rate periods.) |  |  |
| 2 | Labour Cost (Hours and Rates) | What was the basis for how the supplier developed the estimate for labour costs?   * Historical records? Review past labour returns * Has the supplier considered some learning curve, workloads regarding overtime and other factors that would cause fluctuations in the historical data. * Has the supplier applied the learning curve to the historical base? |  |  |
| 3 | Labour Cost (Hours and Rates) | Does the supplier maintain a job order costing system or a process costing? Understanding of how the supplier collects costs and utilizing them for estimating our SOW is key to determining fair and reasonable. |  |  |

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| **#** | **Cost Element** | **Question** | **Key POC for follow up (Supplier and THE COMPANY)** | **Supplier Response** |
| 11 | Labour Hours | How has the supplier supported the proposed labour hours?   * Time sheets * Other records * Prior job experience (for similar efforts) |  |  |
| 12 | Labour Hours | How often are the labour standards reviewed and updated? Who performs the reviews: finance or management area? Has the supplier incorporated new technology in their process that will impact the labour standards? |  |  |
| 13 | Labour Hours | Have learning curves been built in the proposal? How was the curve estimated? Does the process meet the criteria for the use of the learning curve? What are the supplier's learning rates? |  |  |
| 20 | Other Direct Costs | Other direct costs include expenses such as travel.  Ask supplier to provide supporting documentation to justify and substantiate each charge. |  |  |
| 21 | Other Direct Costs | Provide invoices to support costs. |  |  |
| 22 | Other Direct Costs | If travel has been proposed: How many trips and to where? Length of stay? Mode and type of transportation? Compare per diem to Gov't. allowances. |  |  |

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| **#** | **Cost Element** | **Question** | **Key POC for follow up (Supplier and THE COMPANY)** | **Supplier Response** |
| 23 | Overhead | Overhead costs represent supporting effort to the main business of the company, however, are difficult to directly assign to the individual project. These costs are accumulated by logical cost groupings of pools, such as material and general and administrative, with due consideration of the reasons for incurring the costs. |  |  |
| 24 | Overhead | Obtain from the supplier the supporting calculations as to how the overhead rates were developed. |  |  |
| 25 | Overhead | Review the cost elements to ensure they are applicable, allowable and reasonable in comparison to prior years and Canadian Laws. |  |  |
| 26 | Overhead | What were the supplier's overhead rates for the past 2-3 years? |  |  |
| 27 | Overhead | Is the proposed rate the supplier’s current rate? |  |  |
| 28 | Overhead | If possible, obtain a copy of the supplier's most current audited financial statements.  - Compare the overhead elements of cost proposed to the actual.  -Company's financial stability? |  |  |
| 38 | General & Administrative Expenses (G&A) | Ensure that the rate applied in the proposal is consistent with the supplier’s accounting practices. |  |  |

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| **#** | **Cost Element** | **Question** | **Key POC for follow up (Supplier and THE COMPANY)** | **Supplier Response** |
| 39 | Unallowable Costs | Review the cost pools allocated, such as General and Administrative (G&A) and overhead, to ensure they do not contain unallowable expenses as per Canadian law. |  |  |
| 40 | Profit | Profit is an assessment of the risk associated with performance, contract type, the portion of costs financed by the supplier and the capital invested on facilities.  Is the proposed profit % in line with what is allowable by Canadian law for this type of contract? |  |  |
| 41 | Overall performance to budget/ original proposal | Provide a sample of 3-5 comparable projects, what your original bid was and actual completion (hours or $). |  |  |

# Appendix B Sample Agendas

## B.1 Sample Agenda: Financial Review

1. Why a Financial Review?
2. What is a Financial Review?
3. Protection of Supplier Confidential Information
4. Review Preparation
5. On-Site Review
6. Review Conclusion

## B.2 Sample Agenda: Supplier Kick-Off

1. Overview of Financial Review
2. Overview of [Supplier] as a company including:
   * Core competencies
   * Office and Headquarter locations
   * Size of Company (personnel, revenue, etc)
3. Team Introductions
   * THE COMPANY
   * [Supplier]