We've been holding off writing about Raytheon's near-total victory at the ASBCA, but now it's time to get into that 100+ page decision that covers multiple appeals and multiple issues and multiple years. It's a must-read if you are dealing with cost allowability or CAS 405 noncompliance allegations. It sets things straight in a number of areas that have long vexed the contracting parties. On the other hand, we understand the government is going to appeal the Board's decision, so it's possible that many of the things that were set straight will be made crooked again in the near future.

Here is **a link** to the massive (and massively complex) decision. We spent hours trying to sort the various appeals and issues. (Remember, we are not attorneys.) The decision is so massive, we will need multiple blog articles to tackle it all. In today's article, we'll attempt to sort out the decision and tackle one of the many issues: airfare allowability.

Here's what we sorted:

1.

2007 and 2008 indirect rates at Raytheon Missile Systems (RMS) included allocations from Raytheon's Corporate Home Office. DCAA asserted that some Corporate Home Office costs were unallowable and others were expressly unallowable. Because Raytheon allegedly had included expressly unallowable costs, DCAA also asserted non-compliance with CAS 405 requirements for those two years.

2.

The CACO issued a Final Decision (COFD)--$10,468,740 related to 2007 for unallowable costs, interest, and penalties. Raytheon appealed (ASBCA No. 59435)

3.

The CACO issued a COFD related to 2007 noncompliance with CAS 405—$7,469,506; but Raytheon only appealed $1,870,428+$307,776=$2,178,204 of that amount. (ASBCA No. 59436)

4.

The CACO issued a COFD--$1,154,383 related to 2008 for unallowable costs, interest, and penalties. Raytheon appealed (ASBCA No. 60056)

5.

The CACO issued a COFD related to 2008 noncompliance with CAS 405—$2,030,636. Raytheon appealed. (ASBCA No. 60058)

6.

The CACO issued a COFD related to claimed 2008 Corporate airfare--$760,861. Raytheon appealed and settled most of the disputed amount; the amount remaining was $76,556. (ASBCA No. 60057) The Board noted that “numerous appeals from government claims relating to corporate airfare costs have been stayed pending the outcome of the instant appeals.”

7.

The RMS DACO issued a COFD related to 2007 claimed airfare, outside legal costs related to patents, and employee recruiting costs. Raytheon appealed. (ASBCA No. 59437)

8.

The RMS DACO issued a COFD for penalties and interest, related to Raytheon’s inclusion of allegedly expressly unallowable costs in 2007. Raytheon appealed. (ASBCA No. 59438)

9.

The RMS DACO issued a COFD, disallowing RMS’ indirect airfare costs claimed in 2008; but he did not make a payment demand because the amount of costs claimed to be unallowable, plus an amount Raytheon had agreed to remove from its claim for other indirect costs, was less than the amount being withheld from current approved billing rates for 2008. Raytheon appealed. (ASBCA No. 60059)

10.

The RMS DACO issued two COFDs, disallowing RMS’ direct airfare costs that had been included in its billings under two named contracts and demanding payment of $167,427 and $17,274. Raytheon appealed. (ASBCA Nos. 60060 and 60061)

The parties prepared the following table explaining the amounts in dispute and the reasons for disallowable. Where the parties disagreed on the amounts, both amounts are shown.

Segment

Cost Type

Year

Amount

Basis for Disallowance

Corp

Airfare

2008

$76,556

31.205-46, Travel costs

RMS

Indirect airfare

2007

$815,036

31.201-2(d) (supporting documentation);31.205-46

RMS

Indirect airfare

2008

$978,429

31.201-2(d) (supporting documentation);31.205-46

RMS

Direct Airfare

2008

$184,701

31.205-46, Travel costs

Corp

Corp. Development

2007

$307,776

(Gov’t $862,010)

31.205-27, Organization costs (Expressly unallowable)

Corp

Corp. Development

2008

$868,322

(Gov’t $831,797)

31.205-27, Organization costs (Expressly unallowable)

Corp

Gov’t. Relations

2007

$1,870,428

31.205-22, Lobbying and political activity costs (Expressly unallowable)

Corp

Gov't. Relations

2008

$1,065,481

31.205-22; however, only $981,822 is expressly unallowable

RMS

Outside legal – patents

2007

$120,600

31.201-2(d) (supporting documentation); 31.205-30, Patent costs

RMS

Engineering Labor Ovhd

2007

$96,701

31.205-30, Patent costs (Expressly unallowable)

RMS

Recruiting Travel Costs

2007

$51,436

31.201-2(d) (supporting documentation); 31.205-34, Recruitment costs

Corp

Restricted Stock, Incentive Comp, Bonus

2007

$1,242,895

FAR 31.205-22, Lobbying; FAR 31.205-27, Organization costs; FAR 31.205-47, Costs re

Corp

Restricted Stock, Incentive Comp, Bonus

2008

$125,280

FAR 31.205-22; FAR 31.205-27; FAR 31.205-47 (Expressly unallowable)

Corp

Recruitment Souvenirs

2008

$17,780

31.205-1, Public relations and advertising costs

Corp

CAS 405 Noncompliance

2007

$2,178,204

31.201-6, Accounting for unallowable costs; CAS 405; inclusion of expressly unallowable

Corp

CAS 405 Noncompliance

2008

$1,813,619

31.201-6, Accounting for unallowable costs; CAS 405; inclusion of expressly unallowable

Airfare Costs

Long-time readers of this blog will know that the FAR travel cost principle was revised in 2010, muddying what had, up to that point, been a relatively well-understood cost principle—at least with respect to how to determine the allowability of airfare. Prior to the 2010 regulatory revision, the cost principle read:

Airfare costs in excess of the lowest customary standard, coach, or equivalent airfare offered during normal business hours are unallowable except when such accommodations require circuitous routing, require travel during unreasonable hours, excessively prolong travel, result in increased cost that would offset transportation savings, are not reasonably adequate for the physical or medical needs of the traveler, or are not reasonably available to meet mission requirements.

After the 2010 revision, the cost principle read:

Airfare costs in excess of the lowest priced airfare available to the contractor during normal business hours are unallowable except when such accommodations require circuitous routing, require travel during unreasonable hours, excessively prolong travel, result in increased cost that would offset transportation savings, are not reasonably adequate for the physical or medical needs of the traveler, or are not reasonably available to meet mission requirements.

Notice that change? It turns out the change was driven by DCAA's fanatical belief that Raytheon had taken advantage of the government by negotiating volume-based discounts with certain air carriers. Those discounts permitted Raytheon, in certain circumstances, to claim premium class airfare as fully allowable because the premium airfare was actually lower than the "lowest customary standard, coach, or equivalent airfare offered during normal business hours." DCAA *really*
didn't like that. DCAA didn't like that so much that when DCMA and the Office of the Secretary of Defense and the DAR Council all told DCAA that its interpretation of the cost principle was wrong, and that "the words in the FAR [ ] would support the company's position," DCAA did an

end-run by issuing an MRD in November, 2002, that told auditors to question Raytheon's airfare costs based on their insistence that everybody else was wrong. Fortunately for Raytheon, the DCMA Defense Corporate Executive—what we would now call the CACO—told DCAA to stuff it, writing "DCMA Headquarters disagrees with the guidance in the attached DCAA memorandum. … There is nothing in the record to indicate defense contractors are to negotiate airfare rates with carriers and that the negotiated rates are the customary rates to be used for determining the unallowable amount. Accordingly, I can't support or sustain DCAA's audit position."

Several years later (2006) DCAA sponsored a new DAR Case to "clarify" the cost principle to match their interpretation. Despite the fact that the majority recommended that the Case be closed "with no further action," it turns out that DCAA didn't want to accept that answer. Instead, "DCAA persisted and brought the travel cost principle issue to the Office of Defense Procurement and Acquisition Policy (DPAP)." What did DPAP think? "While DPAP does not concur with our interpretation of the existing language, (nor do they wish to take a position regarding the proper interpretation of the current language), they have conceded that the language is ambiguous." Thus, the FAR Case was opened and the rest was history.

Well, except for the fact that DCAA applied the revised cost principle retroactively, because it was only a clarification of the ambiguity of which DCAA had always understood the correct interpretation—at least with respect to Raytheon. And then DCMA decided to go along with the DCAA's retroactive interpretation, and issue a COFD using the revised cost principle to address the allowability of airfare incurred five or six years before the regulatory revision. Which required Raytheon to appeal…

In addition, DCAA questioned Raytheon's use of a "10-hour rule" to justify an upgrade from coach to a premium fare. After much back and forth, DCMA and Raytheon had agreed that an upgrade would be an allowable cost if three conditions were met: (1) Travel primarily took place during non-customary business hours; (2) Raytheon employees reported directly to their TDY or permanent duly station (PDS) after arrival at their destination airport; and (3) Actual flight time (not an employee's departure from their residence and travel time to a TDY site, and the reverse when returning home), must exceed 10 hours in duration. When all three factors were met, the cost of premium airfare was allowable. The agreement was memorialized and Raytheon revised its travel policy accordingly. Naturally, DCAA—who was not a signatory to the agreement—had a problem with that it.

The successor DCE rescinded the MOU. Upon the recission, Raytheon revised its travel policy again, this time by *relaxing* the requirement that employees must report for work upon arrival.

DCAA countered by questioning premium class airfare incurred in accordance with the revised policy, and then citing Raytheon for a significant deficiency in its accounting system because it failed to properly account for the allegedly unallowable airfare. “After a five-year audit of Raytheon’s accounting system, on January 29, 2015, DCAA issued an audit report questioning how Raytheon accounted for allowable and unallowable costs. DCAA found a significant deficiency in Raytheon’s accounting system due to its treatment of premium class airfare.”

Seriously: *a five-year accounting system audit? Are you kidding us?* The Board did not express an opinion on why in the world it would take DCAA five years to complete an audit, so we will just leave that little factoid there.

Then DCAA issued another audit report that found the Missile Systems’ business unit estimating system had deficient controls because the business unit estimated premium class airfare in accordance with the Corporate travel policy. This caused Raytheon to revise its travel policy for the third time (in order to not have its estimating system determined to be inadequate). In the third iteration of the travel policy, in order to make the premium airfare allowable, the employee must perform “meaningful work upon arrival.”

If you are getting the impression that DCAA was “out to get” Raytheon in this matter, welcome to the club. So much for independence and objectivity….

Back to allowability, DCAA not only retroactively applied the 2010 cost principle “clarification” to costs incurred prior to 2010, but they questioned all premium airfares regardless of whether there was a justification that would have made the costs allowable under the exceptions found in the cost principle itself. Further, there were some errors or, shall we say, questionable assumptions made by DCAA when quantifying the allegedly unallowable premium airfare costs.

Under oath, the DCAA auditor defended the methodology used thusly:

Because we were just trying to determine -- when we were doing the audit, we were just trying to determine a reasonable amount. We understand these are negotiations, so we were just trying to give the government some kind of platform to, kind of, base where they should start at.

Accordingly, it seems that DCAA made no real attempt to be accurate when quantifying costs that were allegedly unallowable, notwithstanding that the agency would also allege that Raytheon's failure to properly account for those allegedly unallowable airfare costs represented a significant deficiency in the accounting system as well as the estimating system; and notwithstanding that at the Missile Systems business unit, DCAA and the DCMA DACO were also making similar allegations based on similarly flawed audit methodologies.

How this was all not a massive GAGAS violation remains a mystery to us.

Anyway, at the end of the day the Board sided with Raytheon, finding that "the government has failed to prove its contention that the policy did not comply with the regulation." Along the way, the Board made some statements that have important implications for government contractors seeking to comply with the 31.205-46 rules on airfare allowability. Let us quote them for you.

1.

"While Raytheon's interpretation of the pre-2010 version of FAR 31.205-46(b) as referring to a standard coach fare available to the general public is reasonable, the government's interpretation is not reasonable. As noted, the governing statute makes commercial aircraft travel costs that exceed the 'standard commercial fare' unallowable. It does not refer to any negotiated airfare available to a particular contractor. Similarly, the pre-2010 implementing regulation, FAR 31.205-46(b), refers to the 'lowest customary standard, coach, or equivalent airfare.' … Contrary to the government's stance, its revision of the regulation in 2010 was not a mere clarification, it was a change. If that change were made to apply to the 2007 and 2008 costs in question, it would be an impermissible retroactive change."

1.

"Under FAR 31.205-46 '[c]osts incurred by contractor personnel on official company business are allowable,' subject to certain limitations, including those in FAR 31.205-46(b) regarding premium airfare. However, we agree with Raytheon that, by its plain language, the pre-2010 version of FAR 31.205-46(b) does not make premium class travel unallowable *per se*. Rather, it imposes an allowability limitation upon airfare costs that exceed the 'lowest customary standard, coach, or equivalent airfare offered during normal business hours,' which Raytheon reasonably interprets as a baseline of standard coach fare available to the general public. Therefore, as long as airfare costs do not exceed that limitation, they are not unallowable under FAR 31.205-46."

1.

Importantly, the Board let stand Raytheon's policy that permitted premium airfare costs to be claimed as being allowable when the circumstances met criteria established by the Federal Travel Regulations and Joint Travel Regulations. (See FTR §301-10.123 and §301-10.125.) Often, DCAA auditors will point to the exception circumstances found in 31.205-46(b) as the sole determinants of premium airfare allowability (*e.g.*, circuitous routing, require travel during unreasonable hours, excessively prolong travel, result in increased cost that would offset transportation savings, are not reasonably adequate for the physical or medical needs of the traveler, or are not reasonably available to meet mission requirements.) However, it is clear that the additional FTR exception criteria may be used, or at least used to justify the reasonableness of the additional airfare costs.

Okay, that's it for today. Part 1 complete. We still have many aspects of this important ASBCA decision to discuss. Stay tuned.