

Written by Nick Sanders  
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We noticed a recent [PR announcement](#) from the Centre Law Group touting its December 15, 2010 victory in Virginia's Fairfax Circuit Court for its client, Thomas Computer Solutions, LLC (TCS). TCS was a subcontractor to L-3 Communications. Pursuant to the terms of its cost-reimbursement subcontract, TCS submitted interim adjustment vouchers for variances to its indirect cost rates. According to the press release, L-3 refused to pay those adjustment vouchers "until the Defense Contract Audit Agency conducted a final audit" and recommended final indirect cost rates.

As our readers know, DCAA can take several years to commence its final indirect rate audits, and the audits themselves can last for a year or more. (This situation has recently been exacerbated by DCAA halting initiation of new indirect rate audits for many contractors, because it has redirected its audit resources elsewhere—such as the unnecessary audit of interim vouchers because of the withdrawal of "direct billing authority".) Thus, neither L-3 nor TCS could reasonably expect that TCS would have final audited rates for many, many years. And L-3's refusal to pay TCS' adjustment vouchers would significantly impair TCS' cash flow and—potentially—TCS' financial capability.

At one point, L-3 offered to pay TCS 70% of its requested amounts, but then withdrew that offer. As the press release notes, that about-face "occurred at a time when TCS and L-3 began competing for the same government contracts to provide linguistic services to support the war effort." Moreover (according to the press release)—

In addition to failing to pay the invoices due, L-3 also refused to provide past performance (when it had done so previously) and trashed TCS to the government client by falsely stating (without solicitation) in an e-mail '[t]he solvency of TCS is an issue (not sure if they even still exist)...' The Court found that this was an attack on a competitor.

Even though the parties "went through a lengthy and time consuming reconciliation process to verify the invoices and correct any mistakes," L-3 refused to pay TCS for its indirect rate variances, which was (allegedly) "contrary to FAR 52.216-7, which allowed for interim rate adjustments prior to contract closeout."

The press release doesn't mention other helpful FAR language, which we post here for your use.

## Subcontractor Challenges Prime Contractor's Refusal to Pay Rate Adjustment Vouchers—and Wins!

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FAR 42.704(b) clearly permits some latitude in the establishment of billing rates (rates used on vouchers prior to the establishment of final indirect cost rates). It says—

The contracting officer (or cognizant Federal agency official) or auditor shall establish billing rates on the basis of information resulting from recent review, previous rate audits or experience, or similar reliable data or experience of other contracting activities. In establishing billing rates, the contracting officer (or cognizant Federal agency official) or auditor should ensure that the billing rates are as close as possible to the final indirect cost rates anticipated for the contractor's fiscal period, as adjusted for any unallowable costs. When the contracting officer (or cognizant Federal agency official) or auditor determines that the dollar value of contracts requiring use of billing rates does not warrant submission of a detailed billing rate proposal, the billing rates may be established by making appropriate adjustments from the prior year's indirect cost experience to eliminate unallowable and nonrecurring costs and to reflect new or changed conditions.

In addition, FAR 42.704(e) states—

When the contractor provides to the cognizant contracting officer the certified final indirect cost rate proposal in accordance with 42.705-1(b) or 42.705-2(b), the contractor and the Government may mutually agree to revise billing rates to reflect the proposed indirect cost rates, as approved by the Government to reflect historically disallowed amounts from prior years' audits, until the proposal has been audited and settled. The historical decrement will be determined by either the cognizant contracting officer (42.705-1(b)) or the cognizant auditor (42.705-2 (b)).

Given the foregoing, we tend to agree that L-3 didn't have much of a leg to stand on. And when one adds in the negative comments, we are unsurprised that TCS prevailed and obtained a \$3.3 million verdict described by the Centre Law Group as, "one of the ten largest reported verdicts in Virginia this year and the fourth largest verdict involving business claims."