We start these types of articles with our usual disclaimer: We are not attorneys; we are not giving legal advice. You should obtain legal advice from a licensed attorney. That said, the fact that we are not attorneys does not keep us from reading legal decisions and thinking about how they may implicate government contract cost accounting and compliance matters. Indeed, anybody who is serious about such matters needs to have a solid layperson's understanding of relevant case law. If all one did was read the FAR and contract clauses, one would know the language, but be sadly uninformed about the *meaning* of the regulations and clauses—because it is only through judicial interpretation that the regulatory language is parsed and given meaning. (For an example of what we mean, see **our article** discussing how the U.S. Court of Federal Claims clarified the distinctions between CAS 418-50(d) and 418-50(e) as they pertained to a dispute between Sikorsky Aircraft Corporation and the Department of Defense.)

Today we want to address the Statute of Limitations (SoL) found in the Contract Disputes Act (CDA). This is not the first time we've discussed the CDA's SoL. By now, readers should understand that the CDA's SoL runs for six years from the time that the aggrieved party "knew or should have known" it had suffered damage. The entity filing a claim under the CDA has six years from that moment in time to file its claim and to have that claim heard by a court. Any claim filed after that time will be rejected.

The primary reason for creating a Statute of Limitations (according to Wikipedia) is that, "over time, evidence can be corrupted or disappear, memories fade, crime scenes are changed, and companies dispose of records. The best time to bring a lawsuit is while the evidence is not lost and as close as possible to the alleged illegal behavior." Keep that in mind as we discuss this issue.

In our **most recent article** on the topic, we took the government to task for continuing to litigate SoL cases, even though they were racking up an impressive string of losses (each of which we discussed in a separate blog article). We asked, "Boeing has won twice at the ASBCA; now Raytheon has won at the Court of Federal Claims. When will the Government get the message that the CDA's statute of limitations will be strictly enforced by the Courts?"

We were, perhaps, being overly harsh on government attorneys, because the truth is that not every aspect of the CDA's SoL has been litigated. In particular, nobody knows for sure when the SoL starts running with respect to a contractor's final indirect rate proposals (aka "incurred

cost submissions"). Does the six-year clock start running when the contractor's fiscal year ends, or when it submits its certified proposal roughly six months later? Or does it start running when the proposal is determined to be adequate for audit? Or perhaps when the audit starts? Or maybe when the audit report is drafted? Or maybe when the audit report is issued? Or what about when the cognizant Administrative Contracting Officer receives the audit report? Nobody knows the answer to those questions because the courts haven't squarely addressed the issue and given the contracting parties a "bright line" answer.

So in the meantime, parties with unresolved disputes file claims with either the ASBCA or the Court of Federal Claims. The lawyers are busy these days; very busy indeed.

The issue of the application of the CDA SoL to contractors' final indirect rates matters a heckuva lot. We have written several recent blog articles on the unbelievably huge backlog of unaudited and/or unissued DCAA audit reports in this area. We told readers that, at its current level of audit report output, DCAA has on hand *nearly 70 years' worth of audits* to grind through—and it's taking DCAA almost three years to audit a single year's worth of contractor cost information. Richard Loeb touched on it in his
now famous article
—at some point there's no sense in auditing the contractors' cost information because any enforcement action will not be heard by the courts (because the CDA SoL precludes any claim). Professor Loeb wrote—

Without a significant course correction in the manner that DCAA conducts its audits, which seems unlikely given the 400-percent decrease in audits performed by DCAA since 2008, one does not have to be a statistician to conclude that DCAA will not reduce the backlog in any meaningful manner. It is very likely that for many of the contracts, the statute of limitations for recouping overpayments will run out before DCAA gets around to completing the audits, resulting in a significant loss of savings to the taxpayer.

As we reported, the official DCAA spokesperson pooh-poohed Professor Loeb's assertion, telling reporters that "few audits in the current backlog are at risk of running up against the six-year limitation [though] an exact number could not be immediately determined." Essentially, then, the official DCAA position is that they have not aged the 24,000 unaudited contractor proposals for final indirect cost rates that are in its possession. But nobody should worry, because "few" of them are going to exceed the six-year CDA SoL.

Well, readers, perhaps one reason that DCAA and DCMA and DOD are not too worried about the SoL is because they think the courts are going to rule that the six-year clock doesn't start running *until after DCAA issues its audit report*. In that case, why worry? If DCAA takes 70

years to get around to questioning some contractor costs and recommending some final indirect cost rates to be used to close contracts (which will, hypothetically, be disputed by the contractor), then they think the courts will hear the matter. And if they're wrong, then all the DCAA and DCMA and DOD SES policy-makers will be long, long, long retired by that time. It will be somebody else's problem to deal with.

The thing is, we can't say with any certainty that they're wrong. In fact, a recent **ASBCA case** cast significant doubt into what we thought we already knew about this issue.

Lockheed Martin appealed a final decision by its cognizant Divisional Administrative Contracting Officer (DACO) that found LockMart to be in noncompliance with CAS 418, 420 and the Cost Principle at FAR 31.205-18, because the company had claimed as Independent Research and Development (IR&D or IRAD) costs that were required in the performance of a contract. The government demanded that LockMart hand over roughly $30 million (plus interest) for its alleged noncompliances. LockMart appealed and moved for summary judgment, asking the Judge to find that the government's demand was time-barred because it was filed after the CDA's six-year SoL time period.

Here's a high-level chronology of the events, as we understand them.

In 2001, LockMart submitted a proposal for an Air Force Advance Targeting Pod (ATP) system. In its proposal, the company told the Air Force that it would be performing concurrent IR&D efforts that it did not consider to be required in the performance of the ATP contract. Importantly (according to the Judge), LockMart did not clearly identify its IR&D efforts as IR&D; instead, they were labeled as "company-funded". (The Judge's decision offers a solid lesson learned in that respect. Readers might want to train management and business development staff on the significant differences between the phrases "company-funded out of profit dollars" and "indirect costs to be allocated to contracts".)

A firm, fixed-price contract was awarded to LockMart in 2001. On December 31, 2002, DCAA issued a letter to LockMart (the DACO received a copy) asserting that costs associated the company's concurrent IR&D efforts were not allowable as IR&D expenses because the efforts were required in order for LockMart to perform its contract.

Importantly, the Judge found that, in DCAA's letter—

DCAA recommended a net downward adjustment to LMC's proposed G&A expense pool and an upward adjustment to direct costs and associated indirect costs in the G&A base pools …. [But]
DCAA did not identify any overbillings or increased costs paid by the government resulting from the alleged inappropriate charges.

[Emphasis added.]

LockMart disagreed with DCAA's position, though DCAA continued to assert its findings in subsequent letters and audit reports to the DACO. Finally, in September 2005, DCAA issued a "draft/preliminary report" that calculated a cost impact associated with the various alleged noncompliances. In that report, "DCAA calculated the impact of the noncompliance on appellant's G&A rates for CFY 2001, 2002, and 2003, and stated that appellant's noncompliance resulted in overbillings to the government." The final report was issued in February 2007; roughly eighteen months after the draft report had been issued.

The DACO issued the final decision in September 2008, roughly eighteen months after the final audit report had been issued and three years after the draft report had been provided by DCAA—and nearly but not quite six years after DCAA's initial 2002 letter. In that final decision, the DACO demanded that LockMart calculate its own cost impact, which was provided in March 2009. LockMart's analysis calculated a $13 million cost impact, less than half of DCAA's calculated number.

The DACO ignored LockMart's calculations and issued a final decision/demand letter in December 2010 (almost two years after receiving LockMart's cost impact and more than five years after receiving the draft DCAA audit report—and almost exactly eight years after receiving DCAA's initial 2002 letter). LockMart filed a claim at the ASBCA, appealing the DACO's final decision and monetary demand.

Judge Delman wrote—

For purposes of this appeal, the government claim before us is the DACO final decision dated 8 December 2010, timely appealed to this Board, in which the DACO asserted a monetary claim

against appellant for CAS noncompliance. …

When the DCAA questioned the IR&D costs in late December 2002 … appellant's subsequent billings and the government's payments under the Sniper contract in late 2002 and thereafter also did not necessarily make known to the government any potential monetary CAS claim to recover increased costs because the Sniper contract was a firm fixed price contract. The record also does not show that the government knew or should have known at this time that the contract price itself was increased as a result of the alleged misallocation of these costs. … Appellant has not persuaded us on this record that the government knew, or should have known of any injury to the government at or around the time of the 31 December 2002 DCAA letter arising out of the Sniper contract. As for the impact of the costs questioned by DCAA on appellant's other government contracts during this period, the record also does not show that the government knew, or should have known of any injury to the government on those contracts at that time.

It is true that DCAA's letters to appellant of 31 December 2002 and 30 March 2004 recommended adjustment of certain accounts of appellant some downwards and some upwards -for CFY 2002 and CFY 2003 but there were no statements in either letter regarding overbillings to, or overpayments made by the government on government contracts …. As far as this record shows, it was the DCAA draft/preliminary report of September 2005, copied to the DACO, that indicated that appellant's CAS noncompliance resulted in overbillings to the government …. The CO's 8 December 2010 final decision asserting the government's monetary claim was issued within six years of this report.

Based on the foregoing, the Judge refused to dismiss the appeal.

Well. That's the kind of decision that makes us question what we thought we already knew, and keeps parties going back to the litigation bar instead of negotiating resolutions. According to Judge Delman, a letter from DCAA alleging CAS/FAR noncompliance and recommending downward adjustments to indirect costs is insufficient information for the government to understand it has suffered a monetary injury and has a claim to assert against the contractor. Instead, the DCAA letter/report must clearly state that, as a result of the noncompliance(s), the contractor had over-billed the government. Only those magic words can invoke the CDA Statute of Limitations.

In our view, the Judge's decision gives short shrift to *all* the words in the applicable regulatory language, which is that the SoL clock starts running when the injured party knew or *should have known* that it had been injured. The Judge's decision eviscerates the "should have known" test. There is no doubt in our minds that the DCAA auditors understood that their assertions that LockMart had overstated its indirect costs and understated its firm, fixed-price contract costs led to a situation where the government had been over-billed. Nor do we doubt for a minute that the

DACO understood the same thing.

To think otherwise is to assert that neither DCAA auditors nor the warranted DACO understood the nature of the firm, fixed-price contract type. To think otherwise is to assert that neither the DCAA auditors nor the warranted DACO understood that the claimed allowable G&A expenses that were (allegedly) increased by means of noncompliant cost accounting practices meant that the invoices submitted on flexibly priced contract types contained overstated G&A expense rates, or that those invoices with the (allegedly) overstated G&A expense rates had been paid, creating a situation where the government had been overbilled and had paid the costs. To call that position naïve is to understate its preposterousness; instead, we think it's insulting.

To think magic words must be included in DCAA correspondence in order to invoke the government's knowledge of an injury is to insult the men and women who work at DCAA and, most especially, the men and women who work at DCMA as warranted contracting officers. They receive lots and lots of training and, in order to receive a warrant, a contracting officer must meet certain coursework and **knowledge standards** . The auditors and the DACO involved in this case had to know the implications associated with overstated IR&D expenses and understated FFP contract costs. Either they knew or they were incompetent.

While we often take issue with agency policy guidance and individual decisions from auditors and contracting officers, the fact is that most of these people are not stupid. Nor are they incompetent. Judge Delman's decision is predicated on the assumption that they are.

We hope LockMart appeals this decision. In fact, we think a demand for a written apology from Judge Delman to the cognizant DACO would not be too far out of line. But in the meantime, the decision does impact our understanding of the CDA SoL and gives support to the notion that the CDA Statute of Limitations does not start running until DCAA issues an audit report containing magic words.

So to those who think 70 years is too long to wait for the parties to know whether or not they have an injury requiring redress under the Contracts Dispute Act, we say—"We know; we get it. We feel your pain and frustration." But we also say, "Tell it to the Judge."