

## Protecting the Government's Interests

Written by Nick Sanders

Wednesday, 26 June 2013 00:00

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We have written quite a bit about the Contract Disputes Act Statute of Limitations (CDA SoL). We've written quite a bit because it's an area where the law is evolving, and because it involves a nice intersection between contract administration and contract cost accounting.

And because it involves DCMA and DCAA.

And you know how much we love to write about Department of Defense oversight agencies.

Anyway, we were discussing issues associated with the CDA SoL with a group of knowledgeable practitioners, and the topic came up about the door swinging both ways. This means that the same Statute of Limitations that prevents the Government bringing an untimely claim against the contractor also means that the contractor cannot bring an untimely claim against the Government. There was much discussion about what to do if one's final billing rates were significantly in excess of one's provisional billing rates, and DCAA hadn't yet gotten around to auditing the proposal to establish final billing rates, and it was nearing the six-year SoL.

What to do *indeed*.

First of all, we've written about this before. We are certain that we've addressed this and told our readers that if they let the CDA SoL pass without asserting their claim(s), then they are in a very untenable negotiating position. So this topic is not particularly new news to us or our readers. We confess we got a little bored with the discussion, and our mind wandered a bit.

While others discussed what might be done as they approached their particular SoL deadlines, we started wondering about a slightly different topic.

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We wondered how one might avoid getting into this predicament in the first place.

Our first thought was that one should never have provisional billing rates that are significantly lower than one's proposed final billing rates.

As we've [discussed before](#), the Allowable Cost and Payment Clause (52.216-7) states (at 52.216-7(e) *Billing Rates*) that provisional billing rates "*shall be the anticipated final rates.*" (Emphasis added.) If, during the course of contract performance, either contracting party believes that the provisional billing rates will be materially different from the final billing rates for the cost accounting period, then either party may request that the provisional billing rates be "prospectively or retroactively revised by mutual agreement ... to prevent a substantial overpayment or underpayment."

So if the parties are complying with the requirements of the Allowable Cost and Payment Clause, then the difference between provisional and final billing rates should be *de minimis*.

That's the theory, anyway. We're quite certain that practice does not match theory in this area. The primary reason for the deviation between theory and practice is that many Contracting Officers apply decrement factors to contractor's proposed provisional billing rates in order to "protect the Government's interests." As a result of the desire to protect the Government's interests, contractors are only approved to bill at provisional rates that are lower than the estimated final billing rates. The size of the decrements seems to depend on the individual Contracting Officer; some contractors have rather small decrements and others have rather larger decrements. The immediate impact is to reduce contractors' cash flows, which is annoying, no doubt. But since the provisional billing rates should be synced up to final billing rates over time, the cash flow impact primarily manifests during the current performance year and, accordingly, is perceived as a temporary phenomenon and not something to get overly worked-up about.

There are two opportunities to sync up provisional and final billing rates. The first opportunity is at year-end, when the books close and indirect cost pools and allocation bases are known with some certainty. The other opportunity is when the proposal to establish final billing rates is submitted to the cognizant Administrative Contracting Officer. In that regard, FAR 42.704(e) states—

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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.

And of course, the provisional billing rates may be adjusted at any other time, so as to prevent a substantial overpayment or underpayment.

The express goal of the process is to have the provisional billing rates be as close as possible to the final billing rates that will, eventually, be negotiated and settled by the ACO and the contractor. So if the process is being followed by the contracting parties, then why should a contractor have a significant difference between its provisional and final billing rates, such that it would be compelled to file a "protective claim" with the ACO as the six-year CDA SoL approaches?

The answer would appear to be that either (a) too many Contracting Officers are not adjusting provisional billing rates to better reflect estimated final billing rates, or (b) too many contractors are failing to request adjustments to their provisional billing rates, so as to avoid a significant difference. In the latter case, shame on those contractors. In the former case, shame on those Contracting Officers.

The fact of the matter is that provisional billing rates should closely approximate final billing rates. Imposition of a large decrement factor on a contractor risks the government being unaware of a contract's true costs, and receiving a large "surprise" when the final billing rates are negotiated. (We note for the record that too-low provisional billing rates do not relieve a contractor from having to comply with the Limitation of Cost/Limitation of Funds clause requirements.) Moreover, from the contractor's perspective, having provisional billing rates closely approximate final billing rates means that the settlement of final rates will not have a significant impact on cash flow.

Contracting Officers who seek to "protect the Government's interests" by imposing large decrements that reduce contractors' provisional billing rates do themselves no favors. Unless those decrements are justified by historically experienced unallowable costs at the contractor, we think there's a strong argument that those Contracting Officers are violating the express requirements of the 52.216-7 Allowable Cost and Payment Clause. (Remember that the clause states that provisional billing rates "shall be" the anticipated final billing rates. "Shall be" is an

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imperative direction that the Contracting Officer cannot ignore—see FAR 2.1, *Definitions*.)

Contractors who let themselves be put at a financial disadvantage by those Contracting Officers do themselves no favor either. Not only have they agreed (if only tacitly) to reduced cash flow, they've also let themselves be tied to the Government's timeline for auditing, negotiating, and settling billing rates. As we all know, that process can take many years.

And for those contractors, as they approach the CDA SoL deadline, they must pay for their past decision(s) by submitting a claim for the money they've left on the table, lest they lose their right to assert that claim in the future.