From time to time contractors attempt to limit auditor access to certain records, data, or documents. Generally, the attempted limits stem from a contract clause, or from a lack of a contract clause. Recently, the Civilian Board of Contract Appeals (CBCA) tackled another contractor attempt. In doing so, the CBCA established some interesting positions of which government accounting and compliance practitioners should be aware.

We could tell you that the July, 2023, CBCA decision in the matter of HPM Corp. v. Dept. of Energy will likely be of limited use as a precedent—but that wouldn't be entirely accurate. While the decision was issued from the civilian BCA, it is well-written and could be persuasive to Judges of other fora. (I mean, what do I know? I'm not a lawyer. But the decision seems to me to be potentially persuasive. We'll have to see.)

HPM was awarded a contract by DOE in 2018 "to perform occupational medical services at the Hanford Site in Washington state." (There it is: Hanford. *Again.* What is it about that place, anyway?) What type of contract was it? Yes. It was all the types of contracts.

Here's how the CBCA described HPM's contract: "a performance-based Contract that includes Firm-Fixed-Price (FFP) Contract Transition, FFP Occupational Medical Services, Cost Reimbursement (CR) Occupational Medical Support Services, and Indefinite Delivery/Indefinite Quantity (IDIQ) Contract Line Item Numbers (CLIN)." A "hybrid contract," in short.

Hybrid contracts are all the rage these days. It's not really unusual at all. The question is: which contract clauses apply to which contract types within the hybrid contract? Do all clauses apply to all contract types? That cannot be the case! For example, it would be absurd to say that the Allowable Cost and Payment Clause (52.216-7)—which is a mandatory clause for all cost-type contracts—applies to the FFP portions of a contract. Similarly, we know (through judicial decisions) that, even though 52.216-7 is mandatory for T&M contract types, it really only applies to the cost-reimbursement portion and not to the FFP-per-labor-hour portion. So you can't say that all clauses apply to everything everywhere in the contract. The question remains: which clauses apply to what?

Therein lies the gravamen of the dispute.

The CBCA noted that HPM's contract included the FAR clause 52.215-2 ("Audits and Records–Negotiation," Oct 2010). The contract also included the FAR clause 52.216-7 ("Allowable Cost and Payment," Jun 2013) "… but with a limiting notation (added in bold lettering) that states as follows: 'Applies to Cost-Reimbursement.'"

The dispute started during DCAA's audit of HPM's FY2019 proposal to establish final billing rates. HPM was reluctant to provide DCAA with all requested supporting documents. The documents it did provide to the auditors were marked to prevent DCAA from providing them to others—i.e., to the DOE contracting officer. Apparently, HPM's rationale was based on the fact that "because HPMC did not submit any cost or pricing data for the FFP portion of the hybrid contract, it should not need to provide proprietary information to DOE regarding fixed-price costs."

Hmmm. Interesting position.

It is true and correct that certain cost data associated with FFP contracts awarded without submission of any cost or pricing data are exempt from audit. For example, FAR Part 14 sealed bid contracts are generally thought to be audit-exempt. Similarly, FAR Part 12 commercial product or services would likely be found to be exempt, as well. But it's a large step to go from there to "my FFP CLINs are exempt from audit." I mean … that's some kind of chutzpah right there, isn't it?

The dispute continued into the FY2020 proposal to establish final billing rates. As related by the CBCA—

For the FY 2020 incurred-cost audit, DOE designated Cohn Reznick (CRZ) as its auditor. On January 19, 2022, the DOE contracting officer, relying on the requirements of FAR 52.216-7 (clause I.36) and DEAR 970.5204-3 (clause I.173), directed HPMC to provide both CRZ and DOE with a final indirect-cost-rate proposal accompanied by 'adequate supporting data' that included 'any firm fixed price data needed to evaluate the indirect cost pool and base costs used to calculate indirect cost rates.' Counsel for HPMC responded on January 22, 2022, that the disputed information was proprietary and that DOE was not entitled to it. He argued that clause I.173 was intended to provide DOE with access only to materials related to environmental, safety, and health work plans to protect against ionizing radiation and radioactive materials. He indicated that HPMC would provide information necessary to the audit to CRZ but not to DOE.

(Internal citations omitted.)

Let's stop right here. If your legal counsel is already involved before the audit has really gotten started … well, you can be pretty sure your audit is not going to go well. As a *very* experienced government audit liaison (some would say too experienced), I have to opine that some battles just ain't worth fighting. When your counsel tells your auditor that they can't have access to information they want to see (or that whatever they see can't be shared with their customer, in this case DOE) the first thought that is going to pop into the auditor's head is "those guys are hiding something they don't want me or my DOE customer to see."

Why would you want to create that thought in your auditor's head? Yeah, don't do that.

In fact, my advice (after 40 years of doing this shit) is to keep your legal counsel far, far, away from ongoing audits unless they *must* be involved because a huge issue has been alleged (or has been found-out). There is a place for attorneys in protecting the company; of course there is! But there is an unfortunate tendency for attorneys to polarize the parties while they're carving-out their legal positions. They start preparing for litigation right away. Which is fine if you're excited to litigate. But as for me? My job as audit liaison is, generally, to *avoid* litigation. Litigation is expensive; it is time-consuming. It takes a long time and, while you're waiting for the judge's decision, you're stuck in limbo. Litigation is not something I enjoy; nor should you if your job is to make the audits run smoothly.

The attorneys were involved here and, fairly quickly, a nonmonetary claim was filed with the contracting officer. After rejection, an **appeal** was docketed at the CBCA.

I was interested in how the DOE contracting officer dealt with the issue. According to the CBCA,

The contracting officer found that, pursuant to the contract's inspection and audit clauses, DOE is permitted access to what HPMC views as proprietary material during an incurred-cost audit, even if some of the material relates to the FFP portion of the hybrid contract. The contracting officer then indicated that 'DOE will proceed with the remedy to *remove all unsupported costs*

associated with the FY 2020 indirect rates and FY 2022 provisional billing rates.
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(Internal citations omitted. Emphasis added.)

Yeah, that’s gonna hurt.

There’s a lot of stuff in the CBCA decision about whether the Board could even hear HPM’s claim. Here’s a summary:

HPMC is asking the Board to interpret its contract in a manner that would relieve HPMC from having to provide DOE with the audit support documents that DOE is demanding. Although HPMC presumably could continue to decline DOE’s production demand (as it now seems to be doing), wait for DOE to effectuate the indirect cost reductions that DOE has indicated it intends to impose, and then submit a monetary claim to recover that money, HPMC is not obligated to wait until DOE takes such action in order to seek a decision interpreting its audit production obligations under the contract.

Anyway, the CBCA Judges disagreed with HPM’s position. We’re going to quote extensively and you should read the quoted material, even though you probably won’t.

With regard to HPMC’s argument that these clauses only authorize DOE and its auditors to access information regarding the cost-reimbursement CLINs in its contract and that information associated with the FFP CLINs are completely off-limits, we disagree. HPMC’s contract expressly identifies one of the FAR clauses identified above (FAR 52.216-7) as being tied to the cost-reimbursement portions of HPMC’s contract, but the other FAR clause (FAR 52.215-2) provides generally for audits of ‘cost-reimbursement’ contracts. Although HPMC asks that we decide whether FAR 52.215-2 applies only to the cost reimbursement CLINs in its hybrid contract or to the contract as a whole, it is unnecessary to do so because, as far as we can tell, DOE’s auditors have not requested documents that would fall outside the context of a normal incurred-cost audit. Contractors’ incurred-cost submissions under cost-reimbursement contracts ‘are audited . . . to establish allowable direct costs and indirect cost rates for each fiscal year.’ Donald P. Arnavas, James J. Gildea & Normal E. Duquette, “DCAA Audits,” 94-09 Briefing Papers 1, 4 (Aug. 1994). DOE represents that ‘[a] well-known audit risk is misallocation and/or

cost shifting between fixed price, cost reimbursable, and indirect work/costs' and that 'HPMC has had a history of misallocating costs between FFP and [cost-reimbursement] portions of the Contract.' *The audit in question is being undertaken to ensure that indirect costs being charged to the cost-reimbursement CLINs are appropriately allocated to those CLINs and have not been, through some type of accounting mechanism, moved away from FFP CLINs.* …

The Board is in no position to impose some type of myopic limitation on the scope of documentation that auditors need to support an audit of the cost-reimbursement aspects of this contract or of HPMC's indirect cost rates. … HPMC has identified no basis upon which we would step into the shoes of the auditors and micromanage what documents they may, or may not, need to support their review or bar them from accessing certain categories of documents.

The Court of Claims made clear more than forty years ago that a contractor cannot complain during contract performance about the Government's reliance upon audit access rights, including the right to access what the contractor views as proprietary information, created by contract clauses to which the contractor, prior to award, did not object [quoting SCM Corp. v. United States, 645 F.2d 893, 902 (Ct. Cl. 1981)] ….

HPMC tells us that the documents which the auditors are seeking are far beyond what should be needed to evaluate HPMC's costs. Certainly, the Government's audit rights under these clauses are not limitless and do not provide a basis for wide-ranging document requests for corporate records unrelated to the verification of actual costs. *But the contractor does not get to stop an audit simply because it thinks that what it has produced is good enough.*

(Internal citations omitted. Emphasis added.)

So, at the end of the day, HPM managed to delay some audit procedures, coax from the DOE contracting officer a threat to unilaterally establish both final rates and provisional billing rates by removing "unsupported" costs, and to upset the working relationship with its auditors and with its government customer.

Not the greatest job of audit liaison, in my view.

I hope you will do better.