Cost and Pricing Issues

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Game Plan

• Commercial Pricing
• DCAA Audit Progress
• 2017 NDAA
• 2016 NDAA Section 809 Panel
• Prime Contractor Responsibilities for Managing Subcontractors
• Trends in Statute of Limitations Cases
• Intersegment Pricing
• Allowability of Various Costs
Promoting Commercial Acquisition And Making Commercial-Item Pricing More Commercial
Increasing emphasis on Commercial Acquisition by DoD

- Court decisions adding strength
- DoD implementation catching up
Promoting a Commercial Approach

Congressional Action in Recent NDAAs

• **IT products and services** – 2016 NDAA § 855
  – Required DoD to establish procedural hurdles to acquisition of IT products and services as anything other than commercial items [See DFARS Proposed Rule, 81 Fed. Reg. 53101 (Aug. 11, 2016)]

• **Other services** – 2017 NDAA § 876
  – Requires DoD guidance with preference for commercial acquisition of facilities related services, knowledge-based services (except engineering), construction services, medical services, transportation services
Promoting a Commercial Approach

Congressional Action in Recent NDAAAs

- Preference for maintaining commercial status
  - 2016 NDAA § 851, Amended TINA (10 U.S.C. § 2306a)
  - Default to reliance on prior Commercial-Item Determinations by DoD/Military department / Defense agency
  - Imposes special review requirements if change approach

Nontraditional Defense Contractors

- **2016 NDAA (Generally)**
  - 10 U.S.C. § 2380a - allows COs to treat acquisition from NDC as commercial
  - DFARS proposed rule:
    - “intended to enhance defense innovation and create incentives for cutting-edge firms to do business with DoD.”
    - NDC may include “business segments . . . established under traditional defense contractors”

- **2017 NDAA (Services)**
  - 10 U.S.C. § 2380a(b) – requires treatment of services from NDC as commercial:
    - To the extent services “use the same pool of employees” as used for commercial customers; and
    - If priced “using methodology similar to methodology used for commercial pricing.”

Promoting a Commercial Approach
Commingled Items

• 2017 NDAA § 877
• New requirement (at 10 U.S.C. § 2380B) to treat as commercial items:
  – “valued at less than $10,000”;
  – purchased by a contractor for use in the performance of multiple contracts “with the Department of Defense and other parties”; and
  – not identifiable to any particular contract
Promoting a Commercial Approach

Court Decisions

• *Palantir USG, Inc. v. United States* (COFC 2016)

• *CGI Federal Inc. v. United States* (Fed. Cir. 2015)
Pricing Commercial Items

DCMA Commercial Item Group

- 2016 NDAA § 851 created 10 U.S.C. § 2380
  - Required a centralized DoD capability to oversee CIDs
  - Required public access to determinations

- 2017 NDAA § 873 Amended 10 U.S.C. § 2380
  - Changed “oversee” to “provide assistance”
  - Removed public access requirement
  - Added requirement to support price-reasonableness analyses

- DCMA Commercial Item Group
  - Operational June 2016
  - Maintains public list of CIDs reviewed (w/out determination)
  http://www.dcma.mil/commercial-item-group/
Pricing Commercial Items

Market Research

• 2017 NDAA § 871
• Adds 10 U.S.C. § 2377(d) “Market Research for Price Analysis”
  – Requires DoD to conduct or obtain market research to support the determination of price reasonableness in commercial-item procurements
  – May require the offeror to submit “relevant information”
  – For Major Weapon System procurements, use information submitted under 10 USC § 2379(d)
Pricing Commercial Items

Value Analysis

• 2017 NDAA § 872
• Adds a new 10 U.S.C. § 2379(d)(2) [Major Weapons Systems]:
  – Offeror may submit information re the “value” of a commercial item to aid in the determination of price reasonableness
  – CO may consider that information “in addition to” information such as prices paid for the same or similar item, or other relevant information authorized under 10 U.S.C. § 2379(d)(1)
  – Similar to FAR 15.404-1(b)(4)
• New draft DoD Guidebook for Acquiring Commercial Items (Feb. 24, 2017)
DCAA Audit Process and 2017 NDAA
DCAA Audit Progress

• September 2016 DCAA Memo
  – Revival of DCAA’s ability to provide audit support for non-Defense agencies because DCAA had "met the requirement of less than 18 months of incurred cost inventory"

• FY 2016 Report to Congress
  – Impact of hiring freeze on audit backlog

• April 2017 HASC Hearing on Defense Contract Auditing Process
  – Concurrent auditing v. multi-year auditing
  – Involvement of independent public auditors
2017 NDAA – Audit Process

• Section 820
  – Requires DCAA (without performing additional audits) to accept a summary of findings prepared by a commercial auditor under certain circumstances
    • Limits DCAA audit authority to direct costs unless contractor has “predominantly” cost-type contracts
  – Revises CAS statute
  – Creates Defense CAS Board
2017 NDAA – Audit Process

- **Section 892**
  - Requires DoD to select audit service providers on a best value, not LPTA, basis

- **Section 893**
  - Allows contractors to use third-party independent audits of their contractor business systems in certain circumstances, thereby eliminating the need for further DoD review
2017 NDAA – Cost Principles

- **Section 823**
  - Repeals most retroactive aspects of executive compensation ceiling

- **Section 824**
  - Requires contractors to report IR&D and B&P separately from other allowable indirect costs (and separately from each other)
  - Codifies and limits requirements for disclosure of IR&D efforts
  - Applies to indirect costs incurred on or after 10/1/17
  - Requires DoD to established an annual goal limiting amount of reimbursable B&P costs
2017 NDAA – Statutory Preferences

• **Section 831**
  
  – Establishes preference for performance-based payments (PBPs)
  
  – May not limit PBPs to costs incurred
  
  – Requires non-traditional contractor’s accounting system to be GAAP-compliant to qualify for PBPs, but does not require development of government-unique accounting systems or practices as a prerequisite

  – DFARS revision within 120 days of enactment
2016 NDAA Section 809 Panel
2016 NDAA Section 809 Panel

• Panel to review all DOD procurement issues
• 9 subpanels, one for CAS and other accounting issues
• Potential issues
  – Relocate DCAA
  – Relocate CAS Board
  – Need for DCAS Board
  – Offsetting multiple changes
  – Coverage issues
Prime Contractor Responsibilities for Managing Subcontractors

• *LMIS* decision about subcontractor management
  
  – ASBCA dismissed Government’s $100M breach of contract claim for failure to state a claim, finding it was “based on nothing more than a plainly invalid legal theory”
Trends in Statute of Limitations Cases

- *Kellogg Brown & Root Servs., Inc.*, ASBCA No. 58518, 16-1 BCA ¶ 36,408 (June 16, 2016)
- *Crane & Co. v. Dep’t of the Treasury*, CBCA No. 4965, 16-1 BCA ¶ 36,539 (Nov. 8, 2016)
- *Adamant Group for Contracting & Gen. Trading*, ASBCA No. 60316, 16-1 BCA ¶ 36,577 (Nov. 29, 2016)
- *Sparton DeLeon Springs, LLC*, ASBCA No. 60416, 17-1 BCA ¶ 36,601 (Dec. 28, 2016)
- *Technology Sys., Inc.*, ASBCA No. 59577, 17-1 BCA ¶ 36,631 (Jan. 12, 2017)
Intersegment Pricing

• A-T Solutions, Inc., ASBCA No. 59338, 2017 WL 706919
  – Concerned the pricing of items transferred between a contractor’s commonly controlled subdivisions
  – Transfer at price under FAR 31.205-26(e) permitted where the company demonstrated an “established practice” of pricing interorganizational transfers at other than cost for commercial work, as evidenced by records and testimony
  – FAR 31.205-26(e) does not impose any “economic substance” requirement
Allowability of Various Costs

  - Lobbying costs
    - Unclear whether Board found salary paid to employees engaged in lobbying is expressly unallowable (but probably did)
    - Clear that Board found that such costs are unallowable as “directly associated costs” and subject to penalties on that basis
  - Design and build costs of an M&A application intended to be used both for general planning and specific M&A purposes, but terminated before completion and never used in connection with any M&A target, are allowable economic and market planning costs
  - Testimony and other credible evidence be used to demonstrate allowability of consultant costs in the absence of perfect documentation
  - Contractor has burden to prove CO’s decision not to waive penalty for expressly unallowable costs is an arbitrary and capricious abuse of discretion
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